Hydro Québec

February 22, 2016

Ms. Susan M. Cosper, CPA
Technical Director
Financial Accounting Standards Board
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116
U.S.A.

Via Email to director@fasb.org

Subject: File Reference No. 2015-350

Dear Ms. Cosper,

On the behalf of Hydro-Québec, we thank you for giving us the opportunity to comment on the Board's Exposure Draft entitled *Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement.*

Hydro-Québec is a major North American producer, transmission provider and distributor of electricity, operating mainly in the province of Québec, Canada. Its sole shareholder is the Québec government. In Québec, the transmission and distribution of electricity are regulated by the Régie de l'énergie, which sets rates on the basis of cost of service plus a reasonable return on the rate base.

Attached is our detailed response to specific questions in the exposure draft. Disclosure requirements for fair value measurement affect us more specifically in the financial instruments area. Hence, our response focuses on that area.

Sincerely,

Lise Croteau

Lise Croteau, FCPA, FCA
Executive Vice President and Chief Financial Officer
Hydro-Québec

Question 1: *Would the proposed amendments result in more effective, decision-useful information about fair value measurements? If not, please explain why. Would the proposed amendments result in the elimination of decision-useful information about fair value measurements? If yes, please explain why.*

We agree with the proposed amendments that would result in the elimination of the following elements:

1. The amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy;
2. The policy for timing of transfers between levels;
3. The valuation policies and procedures for Level 3 fair value measurements.

- The *Conceptual Framework for Financial Reporting (Chapter 8: Notes to Financial Statements)* provides the Board with a framework for identifying information that could be appropriate for inclusion in notes to financial statements. According to this framework, relevance and cost constraints should be considered. In our view, the above elements are not aligned with the proposed Concepts Statement.

- Regarding the elimination of the third point, we believe that disclosure about an entity's procedures and internal controls is outside the scope of notes to the financial statements. In its management report, management asserts that it maintains an adequate internal control system. In the auditor's report, the auditor does not express an opinion on internal control but considers the internal controls in place to design audit procedures that will provide the basis for the auditor's opinion. The users of financial statements should rely on these assertions and do not need to analyze specifically disclosed internal procedures and controls used in the valuation process to form their own opinion. Moreover, management would still be responsible for complying with all the valuation procedures, and removing this requirement should not affect investors' confidence in the quality of fair value estimates.

We do not agree with the proposed amendments that would result in the addition of the following information:

1. The changes in unrealized gains and losses for the period included in other comprehensive income and earnings (or changes in net assets) for recurring Level 1, Level 2, and Level 3 fair value measurements held at the end of the reporting period, disaggregated by level of the fair value hierarchy;

2. For Level 3 fair value measurements, the range, weighted average, and time period used to develop significant unobservable inputs.

For the first point, we consider that fair value should not be disaggregated between realized and unrealized gains and losses for the following reasons:

- For many years, there has been a debate about cost and fair value for subsequent measurement. Proponents of cost argued the reliability, objectivity and verifiability of the measure while proponents of fair value argued its relevance. For some assets and liabilities (mainly financial instruments), standards moved from cost to fair value as the most appropriate measure. The application of cost measurements results mostly in realized gains and losses in the income statement, while the application of fair value measurements results in a mix of realized and unrealized gains and losses in the income statement. A decision has been made in the matter and we have to abide by it. Since fair value is considered to be the best measurement, it becomes irrelevant whether it should be disaggregated with regard to realized or unrealized gains and losses.

- Given that fair value is mandatory, we consider the applicable GAAP disclosure requirements to be sufficient. For example, ASC 815 requires considerable disclosure about the fair value of derivatives: by type of instrument, before and after offsetting, and by type of hedging relationship. Gains and losses already need to be disclosed by type of contract, by type of hedging relationship, disaggregated between the effective and ineffective portion, among other things. A requirement to distinguish between realized and unrealized gains and losses would greatly add to the workload of preparers because it is highly inconsistent with hedge accounting concepts. Systems are designed to match the effective portion of a hedging instrument with the corresponding hedged item and not to distinguish between realized and unrealized gains and losses. In addition, this would create confusion for the users of financial statements.

- We do not understand the Board's decision to add a requirement to distinguish between realized and unrealized gains and losses as a means of making a link between earnings and other comprehensive income, as stated in Question L16 of the Decision Questions Considered in Establishing Disclosure Requirements. Other comprehensive income was mainly created as a compromise between the relevance of applying fair value measurement to the balance sheet and limiting volatility in the income statement to a reasonable and relevant level. For some assets and liabilities, including available-for-sale securities, it is mainly the unrealized gain or loss that is allocated to other comprehensive income, whereas for other items such as derivatives, realization is not a relevant concept. The effective portion of a hedging instrument is allocated to other comprehensive income until it is matched with the corresponding hedged item. So, once again, mixing the concept of hedging with the concept of realized and unrealized gains and losses would definitely not be appropriate, in addition to being very confusing.

- In fair value measurement, unrealized gains and losses represent the less reliable portion of the value. For Level 3 measurements, this portion is based on hypotheses and estimates. However, for Level 1 and 2 measurements, unrealized gains and losses are based on observable inputs. It is therefore not relevant to disclose an unrealized gain or loss separately from the realized gain or loss for Level 1 and 2 measurements.

As mentioned earlier, in view of the foregoing, we disagree with the additional requirement to distinguish between realized and unrealized gains and losses for Level 1 and 2 fair value measurements, and we even question the relevance of the actual requirement for Level 3.

For the second point, we do not agree with the requirement to disclose the range, weighted average and time period for Level 3 fair value measurements:

- We understand that this added information would be used by financial statements users to assess fair value measurements made by the preparers and compare such information across entities in a sector. However, existing internal controls and external audits already ensure the accuracy of fair value measurements. We question the relevance of this information for financial statements users because it can be misinterpreted. Moreover, the actual standards (ASC 820-10-50-2(bbb)) already require disclosure of quantitative information about significant unobservable inputs. In our view, entities could use their discretion in choosing the information to be disclosed. Therefore, there is no need for a detailed list of requirements such as the range, weighted average, and time period.

- In addition, if the proposed information is required for an entire portfolio, it could result in the disclosure of a broad range of information that would not be representative. Disaggregating a portfolio to provide information for specific products would be quite burdensome. Moreover, it could reveal strategic and confidential information to the public.

We agree with the proposed amendments that would result in the modification of the following information:

Clarify the measurement uncertainty disclosure to communicate information about the uncertainty in measurement as of the reporting date rather than information about sensitivity to changes in the future.

- We think that this information is more relevant than a sensitivity analysis because it is based on the reporting date and not on future changes and is therefore more aligned with the *Conceptual Framework for Financial Reporting (Chapter 8: Notes to Financial Statements)*, which sets restrictions for future-oriented information.

Question 2: *Are the proposed disclosure requirements operable and auditable? If not, which aspects pose operability or auditability issues and why?*

Yes.

Question 3: *Would any of the proposed disclosures impose significant incremental costs? If so, please describe the nature and extent of the additional costs.*

Some entities use external firms to obtain fair value measurements. Requesting extra information to meet the proposed requirements will result in additional cost for the entity.

For the proposed amendment ASC 820-10-50-2(d), we estimate that incremental costs will be necessary to modify systems (financial instrument accounting) to disaggregate fair value between realized and unrealized gains and losses. As mentioned earlier, systems are now designed to meet the requirement of hedge accounting.

Question 4A: *The proposed amendments would apply to all entities, except for certain requirements in paragraph 820-10-50-2(bbb) through (d), for which private companies would be exempt. Do you agree with the exemption for private companies? If not, please describe why and which disclosures should be required for private companies.*

Not applicable.

Question 4B: *Should entities other than public business entities (for example, employee benefit plans and not-for-profit organizations) also be exempt from the proposed amendments mentioned in Question 4A? If yes, please describe why and which disclosures they should be exempt from.*

Not applicable.

Question 5: *The proposed amendments to paragraph 820-10-50-2(bbb) require that a reporting entity disclose the weighted average of significant unobservable inputs used in Level 3 fair value measurements. Are there classes of financial instruments for which this disclosure is inoperable or does not provide meaningful information? If yes, please describe those classes of financial instruments and explain why.*

See our response to ***Question 1***.

Question 6: *The proposed amendments to paragraph 820-10-50-2(bbb) require that a reporting entity disclose the time period used to develop significant unobservable inputs. What would be the costs associated with including this disclosure? Would this disclosure provide more effective, decision-useful information?*

No. See our response to ***Question 1 and Question 3.***

Question 7: *Are there any other disclosures that should be required by Topic 820 on the basis of the proposed Concepts Statement or for other reasons? Please explain why.*

No. We believe that there already is sufficient disclosure allowing financial statements users to understand fair value measurements.

Question 8: *Are there any other disclosure requirements retained following the review of Topic 820 that should be removed on the basis of the proposed Concepts Statement or for other reasons? Please explain why.*

Yes, see our response to ***Question 1***.
We also propose that the following disclosure requirement be eliminated:

"...If there are interrelationships between those inputs and other unobservable inputs used in the fair value measurement, a reporting entity shall also provide a description of those interrelationships and of how they might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement. To comply with that disclosure requirement, the narrative description of the uncertainty of the fair value measurement that would result from the use of unobservable inputs shall include the unobservable inputs disclosed when complying with paragraph 820-10-50-2(bbb)" ASC 820-10-50-2g)

Theoretically, this requirement seems relevant but in practice it suggests a higher level of precision than is practicable. Considering the number and types of unobservable inputs used in Level 3 measurements, the description of the interrelationships between all of these variables would require significant judgment on the part of management because the estimates involved would be based on unobservable inputs that are less reliable by nature.

Question 9: *How much time would be needed to implement the proposed amendments? Should the amount of time needed to implement the proposed amendments by nonpublic business entities be different from the amount of time needed by public business entities? Should early adoption be permitted? If yes to either question, please explain why.*

As mentioned earlier, implementing some of the proposed amendments would require modifications to systems that are already complex and process a large volume of financial instruments. Therefore, a time period ranging from six months to a year would be needed.