

VALUATION observations



SEC Recommends Keeping Mark-to-Market Accounting

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Under legislation enacted in October 2008 to help stabilize financial markets, the Securities and Exchange Commission ("SEC") was required to conduct a study of "mark-to-market" accounting. Issued on December 31, 2008, the study recommends that existing fair value and mark-to-market requirements should not be suspended, citing that "fair value and mark-to-market accounting has been in place for years and abruptly removing it would erode investor confidence in financial statements." Further, "suspending Financial Accounting Standards Board ("FASB") Statement Number 157, ("SFAS 157") itself would only revert practice to inconsistent and sometimes conflicting guidance on fair value measurements."

SEC: "Fair value and mark-to-market accounting has been in place for years and abruptly removing it would erode investor confidence in financial statements."

Under the terms of the legislation, the study was mandated, at a minimum, to focus on the following items:

- the effects of such accounting standards on a financial institution's balance sheet;
- the impacts of such accounting on bank failures in 2008;
- the impact of such standards on the quality of financial information available to investors;
- the process used by the FASB in developing accounting standards;
- the advisability and feasibility of modifications to such standards; and
- alternative accounting standards to those provided in SFAS 157.

The study outlines eight recommendations:


1. SFAS 157 should be improved, but not suspended;
2. existing fair value and mark-to-market requirements should not be suspended;
3. while the SEC does not recommend a suspension of existing fair value standards, additional measures should be taken to improve the application and practice related to existing fair value requirements

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- (particularly as they relate to both Level 2 and Level 3 estimates);
4. the accounting for financial asset impairments should be readdressed;
 5. implement further guidance to foster the use of sound judgment;
 6. accounting standards should continue to be established to meet the needs of investors;
 7. additional formal measures to address the operation of existing accounting standards in practice should be established; and
 8. address the need to simplify the accounting for investments in financial assets.

Our View

Fair Value accounting is here to stay. Allegations that fair value accounting was partially to blame for our country's financial crisis are dubious, and we applaud the SEC for their recommendation not to "take a step backwards" and suspend SFAS 157. Hopefully more and more companies will work harder to ensure that their fair value measurements are well-reasoned so that confidence among investors and other financial statement users is maximized. 

The study is available on the SEC's website:

<http://www.sec.gov/news/studies/2008/marktomarket123008.pdf>

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