# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

ROUNDTABLE

ON

MARK-TO-MARKET ACCOUNTING

Wednesday, October 29, 2008

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SEC Headquarters

Station Place Auditorium

100 F Street, N.E., L-002

Washington, D.C.

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PARTICIPANTS:

CHRISTOPHER COX, Chairman, Securities and Exchange

Commission

Kathleen Casey, Commissioner

Luis Aguilar, Commissioner

Troy Paredes, Commissioner

John White, Director, SEC Division of Corporation Finance,

Moderator

Jim Kroeker, Deputy Chief Accountant, SEC, Moderator

Conrad Hewitt, Chief Accountant, SEC, Moderator

Wayne Carnall, Chief Accountant, SEC, Moderator

Ray Ball, Professor of Accounting, University of Chicago

Vin Colman, Price Waterhouse Coopers

Scott Evans, Executive VP, Asset Management, TIAA-CREF

Bill Isaac, Chairman, Secura Group of LECG, former FDIC

Chairman

Richard Murray, Chief Claim Strategist, Swiss Re

Aubrey Patterson, Chairman and CEO, Bancorp South

Damon Silvers, Associate General Counsel, AFL-CIO

Randy Ferrell, CEO, Fauquier Bankshares Inc.

Patrick Finnegan, CFA institute, Director of Financial

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Tom Jones, Vice Chairman, IASB

Tom Linsmeier, FASB

CONTENTS

C O N T E N T S (Cont.)

P R O C E E D I N G S

CHAIRMAN COX: Good morning and welcome to a full auditorium. And to those who are participating by Webcast in today's Roundtable to mark to market accounting. On behalf of the commissioners here today, Commissioner Kathy Casey, Commissioner Luis Aguilar, and Commissioner Troy Paredes, I'd like to extend our appreciation to our distinguished panelists and observers who are with us to share their insights and advice on this very important topic.

This is the second roundtable the Commission has recently held on the subject of fair value accounting and it's the first of two that the Commission will hold specifically in connection with the congressionally mandated study on fair value accounting by financial institutions.

Our next roundtable in connection with the study will be held on November 21st. These roundtables serve in effect as public hearings to provide us with valuable insights from investors, companies, and other market participants who are affected by the use of fair value accounting in the current market conditions. Our ongoing study is mandated by the Emergency Economic Stabilization Act signed into law earlier this month. And under the terms of the act it will be completed by January 2nd, 2009.

We continue to work on this study in close consultation with the Secretary of the Treasury and the Board of Governors and the Federal Reserve System whose observers are here with us this morning. This 90-day study is being directed by Jim Kroeker, the deputy chief accountant at the Securities and Exchange Commission, and the work is being conducted in several of our divisions. As we begin our panel discussions it's important to keep firmly in mind the primary role of financial reporting as a communication tool for investors. It serves as well several other important purposes including its use by safety and soundness regulators of financial institutions.

Because of the many uses of financial information, today's topic is not simply an accounting matter, and the differences between the uses of financial information by investors, regulators and businesses themselves, among others, need to be recognized and appreciated in this process. As we've learned, illiquid markets are bringing new challenges to the measurement of fair value. These challenges have brought into focus the need for further work on improving the tools that companies have at their disposal to achieve transparent, decision useful, financial reporting information.

Transparency is the cornerstone of world class financial reporting. Transparent and unbiased financial reporting allows investors to make informed decisions based upon a companies financial performance and its disclosures.

A clear, concise and balanced view into the companies that participated in our capital markets is fundamentally important to those who choose to invest in our markets. Informed decisionmaking results in efficient capital allocation.

Regulators and accounting standard setters have been hard at work to address the challenging issues that we're facing today. In my role as chairman of the IOSCO technical committee, I'm working with our federal regulators throughout the world's capital markets to support accounting standards that afford investors transparency, maintain market integrity, and facilitate capital formation. We are also working to support the efforts of the IASB and the FASB as they together work jointly to address these accounting considerations in an independent and deliberative manner. Their objective is as it should be: to develop and maintain the high quality standards that provide transparency to investors.

I am pleased that members of each of these boards have joined us this morning as observers to our panel discussions. While July's roundtable addressed fair value generally, today's roundtable will be focused specifically on fair value as it is used by financial institutions. This focus is important because Congress has provided that our study focus on the effects of accounting standards on the company's balance sheets, as well as the impact that accounting standards have had on bank failures. In these roundtables and throughout our study the SEC will also be considering as Congress has provided the impact that fair value accounting standards have on the quality of financial information provided to investors.

The FASB's process for developing accounting standards, whether modifications to existing fair value measurements guidance is necessary or should be replaced by an alternative approach. As we conduct this study, the SEC will continue to welcome and solicit the views of investors, financial institutions, other companies, auditors and any interested persons. It's easy to submit comments to our website, and I encourage interested parties to do so.

Today we have a wonderful opportunity for the Commission, our professional staff and the public to learn about the implications of mark to market accounting for financial institutions. We have brought together two distinguished panels to share their perspectives, which I anticipated will be varied and expertly presented. I am confident that all of us will learn a great deal today.

This roundtable was organized by Bert Fox, Jim Kroeker, Lisa McAndrew Muberry, Jennifer Minkey Gerard and Neily Shah from the Office of the Chief Accountant. So with that I'm going to turn the panel over to our moderators, Jim

Kroeker, who as I said is the deputy chief accountant and the staff director for the congressionally mandated study, and John White who is the Director of the Division of Corporation Finance. So, Jim and John, the floor is yours.

MR. WHITE: Thank you, Chairman Cox, and good morning.

I am also very pleased to welcome everyone to our roundtable on mark to market accounting. Today's roundtable serves as an important information gathering tool and our efforts to conduct the study mandated by the emergency economic stabilization act. Throughout the day we will be hearing from a broad range of stakeholders about their views on the application and the usefulness of mark to market accounting.

I should also point out that we do have an open comment period with respect to the study. And that ends on November 13. There is a procedure on our website for submitting comments. As Chairman Cox said, joining me as my co-moderator is Jim Kroeker, and Jim of course is the person that is the person that is staring at the 30day deadline and January 2nd to complete the study.

MR. KROEKER: Ninety-day.

MR. WHITE: Ninety-day study, yes. Boy, you paid attention to that, didn't you? All right. So let me first introduce the panelists starting to my left: Ray Ball is the

Sidney Davidson professor of accounting at the University of Chicago; Vin Colman is the head of the National Office at Price Waterhouse Coopers, Scott Evens is Executive Vice President, Asset Management at TIAA-CREF, and also a member of the Commission's recent advisory committee on improvements to financial reporting, Bill Isaac is chairman of the Secura Group of LECG, but probably he is going to be speaking more today as the former chairman of the FDIC.

Richard Murray is managing director and chief claim strategist for Swiss Re. Aubrey Patterson is chairman and chief executive officer of Bancorp South, and Damon Silver is associate general counsel of AFL-CIO. I also want to introduce our observers starting to my far left: Dan Gelzer, board member of the PCOB; Charlie Holm, senior advisor to the Fed's division of banking supervision and regulation; Christian Daconi, senior policy advisory to the undersecretary for domestic finance, U.S. Treasury Department, Tom Jones, vice chairman, ISB, and Tom Linsmeier, board member of the FASB.

And finally, Chairman Cox, you already introduced yourself, but to introduce the other commissioners we are joined by three of our other commissioners: Kathleen Casey, Luis Aguilar, and Troy Paredes. So thank you all for joining. We've got a large group here. We have prepared a number of questions for the panelists.

I am assuming that we will be interrupted from time to time by the commissioners and by the observers. So this can hopefully run smoothly from him in my perspective. Signal us one way or another if you'd like to speak. If we don't seem to pay attention to you, you can always turn your tent card up and that will be a very obvious sign that you want to speak. But we will try to include everybody at the appropriate time.

What we want to do first, however, is give each of you the opportunity to make brief, and I hope I can underline "brief," one to two minutes opening remarks. So I will start on the left side of the podium and start with you, Ray.

MR. BALL: Chairman Cox, Commissioners, staff, thank you for inviting me. I have some sympathy for your position. This is a topic that's been debated in the accounting profession and the academic literature for five decades and you have 90 days to sort that out.

My view on this could be summarized very succinctly as the following. I think it would be a terrible shame if we shot the messenger and ignored the message. The message, I believe, is that the issue lies in the structure of the markets in which the securities were held. It doesn't make sense for correlated, risky positions to be held by financial institutions that are very highly levered and if that continues the market structure will simply find these same events repeating at a later date, the reason being that for various institutional considerations there are leverage constraints on the balance sheets of financial institutions.

They are either prudential regulatory constraints. There are contractual constraints, and there are debt financing. There are constraints generated by margin calls and other institutional phenomena such that the impairment of a balance sheet triggers asset sales that are correlated across the world and we have people lining up on one side of the market. I regard that as the fundamental problem. I think that's the message. The messenger was on his balance sheets prepared under fair value accounting. I think there can be some debate about exactly how the rules on fair value are structured and how they were interpreted, but nevertheless, I think that's the basic issue.

I think the short-term consequences of suspending fair value accounting for financial institutions would be to encourage what occurred in Japan. What occurred in Japan was banks were allowed to keep financial instruments on their balance sheets at historical cost for a very long period of time so that investors in the capital market did not know which were the strong banks and which were the weak banks. And capital was misallocated in the banking market for a substantial period of time, and that inhibited the recovery of the economy.

So I think there are short-term problems. I also believe that right now investors are acting as if they face huge risk and uncertainty. The last thing we want to do in those circumstances is just to reduce transparency. I think we should be increasing transparency. Long-term as I said, I believe this sort of episode could occur again if the basic structure of the ownership of the financial claims that created this problem is not addressed.

Thank you.

MR. WHITE: Vin?

MR. COLMAN: Chairman Cox, Commissioners, SEC staff and observers, good morning.

Thank you for the invitation to appear before you today and provide you with my prospectus on the top of mark to market accounting. And I hope it assists the Commission as it undertakes the 90-day study. I should note at the outset that I appear today on behalf of myself and my firm, and not necessarily the accounting profession as a whole.

We support the SEC's efforts to study current, fair value, accounting framework as required by the Economic Stabilization Act. This review is especially important in light of the challenge it presented by today's difficult market conditions. We also encourage the Commission and others to undertake a constructive review of the root causes of the credit crisis. Understanding the root causes will help in determining any necessary reforms including those that go beyond accounting and financial reporting.

We continue to believe that fair value reporting, despite its imperfections, is the best method for providing the level of transparency that our markets need to function effectively. Any fundamental change to fair value reporting runs the risk of reducing confidence among investors and other market participants, which in turn would like to restrict the flow of capital. We recognize there is a wide range of views concerning fair value reporting and we look forward to an open dialog.

We are committed to exploring any ideas that offer promise for improvements or enhancements to the application of fair value reporting principals. We appreciate the stress that fair value reporting sometimes places on the ability of financial institutions to comply with regulatory capital requirements. We also understand there are differences between the regulators safety and soundness mandate and the investor driven objectives of financial reporting.

In light of these tensions, we encourage the regulatory agencies to review and potentially refine capital adequacy guidelines as applicable. With respect to establishing or revising U.S. accounting standards, we continue to advocate an independent standard setting process free from undue political pressures and other outside influences. In this regard we appreciate Senator Dodd's recent statements affirming the importance and desirability of independent standard setting.

Recent events remind us of the inter-connectiveness of our global markets. As the debate around fair value reporting evolves, we believe it is critically important for standard setters and regulators to coordinate their efforts globally. This will help mitigate the potential for conflicting national and regional responses.

Lastly, we support exploring possible refinements in fair value reporting and the related disclosures of fair value measurements. Specifically, in the near term, we believe there are several areas that could be evaluated in regard to reporting periodic changes in fair value without compromising the core principles of fair value measurement. These include the first. Consider separating for accounting purposes the periodic changes in fair value into two components: incurred credit losses and other changes in fair value, including for example liquidity discounts.

Second, consider converging the guidance for reporting financial asset impairments by recognizing first, incurred credit losses in income and all other changes in fair value and other comprehensive income until the asset is sold or matures. Thirdly, consider changes in the format of the income statement to allow for more visibility to the income effects of items reported at fair value and the inclusion of other comprehensive income on the face of the income statement. We believe these actions will help enhance transparency and usefulness, providing a more consistent framework for recognizing impairment losses and by locating all changes in fair measurement items in a single, financial statement.

I look forward to discussing these ideas and responding to questions. In conclusion again I thank Chairman Cox, the Commissioners, and the SEC Commission staff, for the opportunity to appear before you this morning. I applaud your close and focused examination of these important issues. I would be happy to answer any questions you may have during this roundtable discussion.

Thank you.

MR. WHITE: Scott, the investor viewpoint?

MR. EVANS: Thanks, John.

As you stated before, I am with TIAA-CREF, and our company invests over $400 billion on behalf of three million individuals with 15,000 academic, medical and cultural institutions throughout the United States. However, the views that I'll express today are solely my own, based on my experience as an investor and money manager and do not necessarily represent the institutions and individuals for whom we manage money nor the colleagues with whom I work.

It's a privilege for me to appear before the Securities and Exchange Commission, members of its staff and its distinguished panel of observers. You've specifically asked my fellow panelists and I to address the interaction between mark to market accounting for financial institutions in the current economic situation.

Let me begin by saying that I recognize and appreciate the unprecedented stresses and challenges that our financial institutions are facing today. As a manager responsible for the stewardship of our insurance accounts, I know firsthand the challenges of obtaining fair evaluations in these market conditions. Nevertheless, I strongly believe that our public markets are best served by a system of financial reporting whose primary objective is to provide investors with decision-useful information on the economic position of reporting companies.

Fair value accounting, while far from perfect, and clearly a work in progress for accounting standard setters, is a fundamental mechanism to provide investors with important transparency and to the underlying risks in economic value of assets held by public entities. The roots of today's crisis have many causes, but fair value accounting is not one of them.

Those who argue the removal of volatile, fair value estimates will improve valuations are missing the point.

Consistent disclosure of management's best judgments regarding fair value of firm assets will narrow the margin of safety required by investors when otherwise confronted with the lack of information. Investors value transparency and they'll pay for the uncertainty that it removes.

I am sympathetic to arguments made by some that the interplay between fair value assessments under GAAP and the capital requirements of prudential regulators can have a pro-cyclical effect, exacerbating the effect of declining market values on the portfolios and capital structures of regulated financial institutions. Depending on the market environment, financial institutions may overcompensate and encourage steps like premature liquidations of portfolio positions at unfavorable prices, raising capital under inopportune conditions or in good times taking excessive risks.

In my opinion, the design of an appropriate solution for these issues properly lies with those responsible for prudential supervision and any potential remedy centered around providing less information to the users of financial statements may have the unintended affect of introducing additional pressure on valuations as transparency to investors is compromised.

I support the recent efforts of the staffs of the SEC and the FASB to provide practical clarification in the application fair value accounting during periods of market illiquidity or inactivity, this guidance properly recognizes the determination of fair value often requires significant judgment.  It advices that results of disorderly transactions sometimes known as fire sales are not determinative when measuring fair value and emphasizes the need for judgment in making determinations regarding other than temporary impairments.

I commend the SEC and FASB for being responsive to the needs of preparers and auditors in promptly furnishing such guidance.  I also support the Division of Corporate Finance's ongoing efforts to improve the quality of disclosure regarding fair value measurements.  Disclosure of the underlying risks, valuation methodologies assumptions and sensitivities are crucial inputs to allow investors to make informed assessments of the fair value judgments of preparers.

It's certainly understandable that those worried about the damage inflicted on our financial system would engage the SEC on this important issue.  Significant attention to our system of financial reporting can only lead to improvements, and over the long run, more effective capital markets.

I urge the Commission to maintain its resolve and continue to resist pressure to repeal or suspend fair value accounting. Resisting such calls can be difficult, but the needs of affected market participants are acute. Your steadfast support for fair value transparency is greatly appreciated by those of us who invest for the long-term interest of our taxpayers and citizens.

I believe that the Commission best serves its mission to the markets and investors particularly during uncertain times by promoting transparency, allowing the markets to work effectively and safeguarding the integrity of the private accounting, standard-setting process. Indeed, the IASB, with the support of the FASB, has issued a comprehensive discussion paper on reducing complexity and reporting on financial instruments.

We must allow the process to work and continue to improve upon the foundation that's been built. Any suspension of fair value accounting would reduce confidence in reported numbers, diminished comparability and potentially exacerbate market instability by enabling uncertainty to thrive. Consequently, I support statements by the CFA institute, the Center for Audit Quality, which have urged the Commission to reject any proposal that would suspend fair value accounting.

I would be pleased to clarify remarks or answer any questions.

Thank you.

MR. WHITE: Bill, you're next. I assume your views are going to be slightly different?

MR. ISAAC: Somewhat. First, I'll begin by I have full remarks that are on the web-site if you all would like to take a look at them.

I really sort of object at the outset to the appropriation of the name "fair value accounting," and if I were the FTC I'd be looking into that as unfair and misleading advertising. There is nothing fair about a system that is transparently wrong, and that's what this system is today and I couldn't object to it more strongly. And it has nothing to do with what's going on in Japan, but we'll get into that debate. But let me summarize my remarks.

I've been obviously a very vocal critic of mark to market or mark to index accounting as the case may be and it might surprise you to know that when I was Chairman of the FDIC I actually was a proponent of it for a while, because I thought it might help us solve a problem that we had with the thrift institutions, the savings banks and the S&Ls, which were insured by the FSLIC and the FDIC, and they had very long-term portfolios of mortgage loans and they were funded by short-term deposits. And the prime rate went to 21-1/2% and so we had a huge mismatch, which created hundreds of billions of dollars of mark to market insolvency, if we had been marking them to market. And I thought well, maybe a mark to market accounting system will cause these institutions to get their books in better balance.

Again, maybe it's a structural problem we can deal with. I asked the FDIC staff to study it and we did, and we got outside comments. We studied it for a year and we rejected going there for three reasons. One, market accounting could only be applied to a small portion of the balance sheet on the asset side, essentially marketable securities can be mark to market. The rest of the assets in the bank are not mark to market, still aren't today, and the liabilities aren't mark to market. And when you have government, let's say, interest rates go up, government bond prices go down on the asset side.

If they get mark to market and you don't do anything on the liability side, you've created a very false impression about the bank because of liabilities. The demand accounts, you know, the checking accounts, the savings accounts, the fixed rate CDs are all going up in value. And you're not taking that into account and the bank clearly has the ability to fund those long-term assets or make those assets that have gone down in value because they have liabilities that have increased in value very significantly.

Second, we believe that mark to market accounting would interfere with banks performing their fundamental function, which is to take relatively short-term deposits and convert them into relatively long-term loans to businesses and consumers, so banks necessarily must have a mismatch if they're going to do their job, so it's not a structural problem. I mean, it's the way banking is. Banking by its very nature is going to create a structural problem, and today's structural problem is not unique. Banks necessarily will have a mismatch between their assets and liabilities.

Third, we felt that mark to market accounting would be pro-cyclical, extremely pro-cyclical, and would make it very difficult for regulators to manage future banking crises. If we had had today's mark to market approach during the 1980s when I would tell you that the credit problems and the banking system and the economic problems in the economy were far more serious than they are today. Now, mark to market accounting is turning these into very serious problems -- a worldwide financial crisis that is due to the fact we have mark to market accounting -- but the fundamental economic problems in the 1980s and the fundamental banking problems were far more serious than we have today.

We had a prime rate of 21-1/2%. We had the money center banks were loaded up with third-world debt, which if you could sell it was worth about 10 cents on the dollar. We had the savings banks and the S&Ls under water to the tune of at least a couple hundred billion dollars. If we'd had to mark them to market, you'd had a rolling real estate recession that wiped out many of the regional banks in the country including nine of the ten largest banks in Texas. And we had a depression in the agricultural sector which caused hundreds of agricultural banks to fail.

The problems that we had in the banking system at that time were far more serious than anything we are facing today with the real estate portfolios, but yet they were not allowed to get out of control the way these problems have today, because we didn't have to contend with mark to market accounting. To me, it's beyond dispute that mark to market accounting has been senselessly destructive of bank capital and is a major cause of the current crisis we have in the financial markets and then economic decline we're facing now.

The rules have destroyed hundreds of billions of dollars of capital and have depleted lending capacity by 10 times that amount. It's imperative that the FASB and the SEC withdraw immediately, FAS 157, and I hope that the SEC will recommend it in its report to Congress that we do away with mark to market accounting all together.

Some advocates of mark to market accounting -- and I guess I've got some to my right -- gasp at the thought of suspending the rules. They argue that it would resolve in the loss of transparency and an overstatement of values. Quite to the contrary, mark to market accounting has produced terribly misleading disclosures by valuing assets at well below their true economic value. If we suspend mark to market accounting, banks and regulators will value the affected assets the same way they value all other assets on the books of banks. They will consider the cash flows on the assets, the likelihood that the assets will go into default, and the probable losses in the event of default.

We will improve our valuations and disclosures, not obscure them. I believe the proponents of mark to market accounting are in the state of denial regarding the utter disaster their rules have created. Historical cost accounting, the cornerstone of GAAP, is vastly superior. Under historical cost accounting, marketable assets are carried out on the books of banks at their amortized cost, and the balance sheet contains foot-noted tables showing the current market value of those portfolios.

This gives investors the information they need to evaluate the adequacy of a bank's capital and its future earnings power. Historical cost accounting does not run the market depreciation through the profit and loss statement and does not deplete capital unless the decline in value is considered permanent. Moreover, this system provides a more accurate and holistic, financial picture of a bank than today's destructive and misleading system of accounting.

I believe we've put too much pressure on accountants by subjecting them to huge liabilities when companies fail due to market conditions and faulty business strategies. One important consequence is that the profession is reacted by implementing rigid rules that leave little room for judgment and wisdom. I believe we should consider insulating auditors from liability when they are using reasonable business judgment. And I will tell you that I am part of the cause of the accounting profession's problems, because when I was chairman of the FDIC I authorized a lot of suits against accountants, and I wish I hadn't done it.

The current worldwide crisis in the financial system demonstrates that major principles of accounting are much too important to be left solely to accountants. I believe we urgently need to change our system of setting accounting standards to make it more accountable and more responsive. I recommend that accounting principles affecting our financial system be approved by both the Federal Reserve Board and the FDIC, the two agencies charged with maintaining stability and picking up the pieces when crises hit.

I also recommend that we not cede U.S. authority over accounting standards to an international board. Our current system is complicated enough and unresponsible enough that I don't want to go further and make it an international matter if we need to change some accounting rules. That's my opening remarks.

Thank you.

MR. WHITE: So, Aubrey, I guess you're one of these banks. You want to give us your remarks?

MR. PATTERSON: Yes, I am. Thank you.

Good morning, Mr. Chairman, Commissioners, staff, guests.

I am Aubrey Patterson, Chairman and CEO of Bancorp South in Tupelo, Mississippi. I am also a former chairman of the American Bankers Association. Obviously, I am here more as a chief executive officer than as a practitioner. I would like to add my thanks to the SEC for holding this roundtable on a topic that is in critical need of review. I know that the SEC September 320 release provided a good framework for third quarter reporting and much needed clarification for the current rules in an illiquid market and we certainly appreciated that release.

With respect to fair value, let me start by saying we think there is fundamentally nothing wrong with the basic concept of fair value. There certainly a re situations where fair value is useful. For example, if an entity's business is to actively trade or their operating model is based fundamentally on fair value, then fair value may well be the most relevant measurement. However, if the business model is not focused on fair value then using it as the basis of accounting as Bill has already expressed, can be misleading to users of financial statements. In order to be useful, as

I understand it, accounting should be relevant, reliable, and should be in sync with the business model. Otherwise, it won't be representative of the economic activity, nor of the economic reality.

In its purest sense, in my view, accounting as the language of economics should reflect economic activity and reality, and not drive it. The recent turmoil in the markets has clearly been impacted by fair value, illiquidity, and the often complete freeze-up of the markets has resulted in downward pressure on values and has been pro-cyclical. The lack of typical buyers and sellers in the market indicates that the sellers obviously believe their values are greater than the values the buyers are willing to pay, and yet in some cases, these low exit prices are being required for use in financial statements resulting in distressed sale valuations.

That process excludes the sellers as market participants and thus the notion of willing buyers and willing sellers and an arms-length transaction that is not a forced sale, the basic rule is ignored. This market demonstrates that fair values shouldn't be the accounting model for all financial instruments as is being proposed by FASB and ISB. The basis for the numbers in our financial statements must be both relevant and reliable, but the market's perception of value obviously has not reflected the true cash flow value and thus these are not what should be flowing through our financial statements. It's not that we are resistant to change adaptation and more useful information. Instead, we need to ensure that the resulting financial statements are truly valuable to an informed investor or potential investor.

With respect to business combinations, I'd also like to mention the impact of fair value here. The requirement to use business combinations, SFAS 141(r) has resulted in preventing mergers and acquisitions from occurring. Because the market's current perception of value is extremely low for some assets on the books, these low values may well result in the need for the then combined entity to immediately raise capital subsequent to the business combination.

Fair value and/or liquidation value do not reflect the economic value of a business or even a segment of a business. When a business is acquired, it is acquired as a going concern, that fundamental old standard of a going concern, not as discrete assets and liabilities about to be liquidated. And the true value of the acquisition consequently then differs from narrowly-defined, fair values. If you would in fact agree, the fair value of those individual assets in an acquisition are incorrect, that in fact the value is higher than the accounting is resulting in illogical actions in the marketplace, preventing mergers and acquisitions that might otherwise occur.

One of the biggest issues relating to fair value is other than temporary impairment, OTTI. If the fair value of an instrument is less than its book value, the OTTI obviously may exist, and if so the instrument must be written down to fair value. Over the years and including today there have been questions about whether OTTI should be recognized for financial instruments that are in fact current, not in default, and not expected to be in default.

Pooled trust for preferred securities are a good example, and that's one that we have raised with the SEC. The rules for ITTI should and must in fact be examined with a fresh look, particularly for those instruments who do not have identified credit problems. My suggestion for next steps are 1) to improve the definition of fair value so that when properly required by the accounting literature, the most appropriate measurement of fair value is used. This market has demonstrated clearly that the current definition, 157, does not work.

Two, stop the move for fair value for all financial instruments until the following are fully examined; and, by the way, I note that in our recent communication to the Chairman's office, we made reference to the 12 European countries meeting in Paris on the 12th of October, and their resultant draft declaration on a concerted European action plan, which we note as support for our recommendation for suspension of the rule, the draft declaration states if you'll indulge me, and I quote: "Under current exceptional circumstances financial institutions should be allowed to value their assets consistently with risk of default assumptions rather than immediate market value which in illiquid markets may be no longer appropriate."

The following steps, questions to be asked: Do the current requirements to use fair value actually improve financial reporting if it's a better model? What is the rationale for limiting it to financial instruments? If fair value continues to be limited to financial instruments, how does this impact financial institutions versus other kinds of industries?

That is, does it make our earnings and capital more volatile, thus increasing the cost of capital for financial institutions versus other industries? Does it reduce the confidence level that customers have in the financial reports of financial institutions versus other industries?

Three, examine the existing accounting standards to determine whether the move to fair value has been appropriate at all or whether historical amortized cost is more appropriate with accompanying disclosures. And, four, expeditiously examine the accounting guidance for OTTI as has already been requested of the FASB by the Commission.

In my view, essential to the elegance of accounting theory as many of us have studied and viewed it over the years is the concept of a going concern where the financial condition is depicted by measure of the flow of economic activity between stock measurements at discrete points in time. This is to me at the core of financial accounting, and to preserve this flow and stock concept, it's my view that footnotes may be a preferred venue for many of these fair value measures, and especially so in financial institutions.

Thank you, Mr. Chairman, and thanks to the Commission for the opportunity to share my views with you and I look forward to our discussion.

MR. WHITE: Rick?

MR. MURRAY: Good morning, and my appreciation to the Commission and the staff for the opportunity to appear here on behalf of Swiss Reinsurance and also as chairman of the Center for Capital Markets Competitiveness of the U.S. Chamber.

We welcome the intense conduct of this study by the Commission which we have urged be undertaken. We do not presume to hold the key to what the Commission should conclude at the end of the 90-day period, and so I can be brief. We do however urge that the Commission take a very broad view of its mandate in reaching its conclusions, because we view the current dialog as unhelpfully rigid. Three particular suggestions in that regard.

We urge you to take a full, historical, contextual look at the issue. As Mr. Isaac's notes, this is not the first time that the issue has become a critical matter following the S&L experience, but one can look back to the fact that mark to market accounting was U.S. GAAP prior to the great depression. It was perceived widely as one of the contributing factors leading to the depth of that depression and was replaced by historical cost accounting in the decades following the creation of the SEC. Conditions in all those situations differ, but the potential for lessons to be learned are valuable.

Secondly, we urge a broad view of your mandate with respect to the scope of the topic. Much of the current dialog focuses on the particulars of mark to market accounting as a fundamental principle and the application of that through the specific rules of FAS 157, 159 and other measures. We believe that it needs to be recognized that if those particulars were removed from the scene and any other set of particular applications of measurement were to replace them at the moment, the issues would not be resolved and the measurement difficulties would not go away and the challenges the Commission faces in this study would not be fundamentally different. So we urge that the attention be to the underlying challenges and not to the current applications.

Our third suggested attention to the breadth of your challenge arises from the current dialog that so frequently asks the question of whether the rules, the rulemakers and the auditors are right or wrong, we think that is an unhelpful premise.  A more useful starting point is to recognize that in the five decades that the accounting profession and its regulators and standard setters have been trying to enhance the role of financial reporting in the economy, a fundamental premise is that accounting principles should mirror economic reality rather than create or drive economic reality.

We believe that may not be an attainable goal in the current context and that the intrinsic interwinding of accounting measurements with economic and financial conditions must be recognized and that recognition will require resolution through the adoption by the process the Commission has undertaken of establishing a national policy mandate on how you wish to see the interlinkage of measurement procedures and economic conditions.  Only the SEC and Congress can establish that national mandate.  We do not perceive that one clearly exists at this time and urge that that be the most fundamental objective of your undertaking.

We have other perspectives that may have time for discussion later on, but in the interest of time I would just note that we strongly encourage attention to the creation of an appropriate role for both business and professional judgments in the application of whatever emerges. And, finally, we wish to encourage that the inhibiting influence of liability be avoided in this condition. I agree with Mr. Isaac's hindsight reflection on the damage created by the liability implications of the savings and loan crisis and urge that that not be replicated here.

Thank you.

MR. WHITE: Damon?

MR. SILVERS: Yes, thank you.

I am Damon Silvers. I am associate general counsel of the AFL-CIO. We represent 12 million working Americans and their families who have about $5 trillion, at least until recently invested on their behalf in benefit funds. We also, our members, like I think most Americans value their jobs a great deal and are deeply concerned about the economic crisis we find ourselves in from each dimension of their economic lives as investors saving for retirement, as employees, as homeowners, and as members of their communities.

The AFL-CIO has engaged in the question of how far to move from historic cost accounting system through the mixed attribute system that we have today toward the mark to market, or as its advocates would put it, fair value system, over a period of years, fairly intensively since the Enron and WorldCom scandals and the associated financial crisis earlier in this decade.

In the course of that engagement we came to the view and expressed to the FASB and the PCAOB that we did not agree with the proposition that mark to market accounting was always the best approach in business, generally. And we expressed the view, and I think some of my fellow panelists have said this, that there needs to be a recognition of the relationship of accounting principles to business strategies.

However -- and I think in retrospect this was somewhat na‹ve -- we took the view that the two basic concepts that should guide accounting regulators in making these distinctions were whether the assets or liabilities at issue, whether they were liquid markets where there were prices available, and whether those assets and liabilities in the course of the business that they were part of were reasonably likely to be transacted in those markets.

We are deeply skeptical about the notion that for example property plant and equipment ought to be mark to market on a quarterly basis, or that a company's own debt ought to be mark to market on a quarterly basis. If one did that, one could imagine a company going profitably bankrupt. Now, I say "na‹ve" because that point of view led us to the view that one area that mark to market accounting would seem to clearly apply to would be marketable public securities,

securities where there is a liquid market held by financial institutions that could quite likely have to sell them, for example, to meet demand deposits being withdrawn.

That would seem to be the sort of simple case. Obviously, that's not true. That presumed a situation in which we had liquid markets. Given that that area has turned out to be rather complicated and problematic, we have had to reassess our views a little bit, and in doing so we have kept two things in mind. We are concerned about pro-cyclicality that has been discussed several times here, but pro-cyclicality has a double-edged sword. On the one hand, if marking assets to market or marketing them to model in a context where there are illiquid markets and a na‹ve following of that approach by bank regulators leads to a dramatic contraction in lending by private institutions, that clearly presents the potential of contributing to a downward spiral in our economy, and the threat of that today when leading economists are forecasting unemployment rates unseen since the crisis of the early '80s on a global basis cannot be ignored.

On the other hand, it is our view and the view of many of the world's leading economists that the fundamental problem in our economy today, the fundamental drag, is the unresolved housing crisis, the millions of Americans facing home foreclosure and the apparent inability of the housing finance system to restructure those loans on a viable basis. If we move in a direction of allowing financial institutions to pretend that subprime loans are actually going to be repaid on a full value basis, we create incentives not to restructure those loans. That clearly is also pro-cyclical.

It is difficult in that context to determine precisely what the right thing to do is. We believe, tentatively, that the right approach is that expressed by several of the panelists here, I think on sort of both sides of the divide that exists among some of us, and by Chairman Barney Frank of the House Financial Services Committee that at least as an initial matter the approach ought to be looking more toward safety and soundness regulators to act in an anti-cyclical matter around capital issues, more in that direction, unless in the direction of trying to alter the accounting rules and the data that is disclosed to the public.

However, I think there are two sort of caveats to that. One is that it appears to us that the way mark to market accounting has been applied is not adequately addressed the nature of financial intermediary institutions that intermediate long and short-term investments, and that the Commission in this process ought to look at that closely. Thanks to one such institution they are not the only one.

Secondly, there is the real risk here that things are not what they seem to be, that mark to market accounting in the absence of the market quickly turns into something completely different, which is the assignment by management in its discretion of values to assets. In a way, mark to market accounting has turned out, and certainly in this context, to be like a scientific theory which appears to be correct, but which you apply it to the facts becomes more and more baroque. This is sort of like the theory that the sun goes around the earth. You can build it up in such a way that it appears to be correct, but the complexity shows you it's not.

One of the consequences of that building up is that there is a risk that in the increasingly attenuated and baroque application of mark to market principles in the absence of liquid markets, or the application of those principles in a way that doesn't deal with the question of whether those assets or liabilities are actually going to be bought or sold on markets, that ignores the notion of realization entirely, will make a complete hash of financial statements, that you won't actually have been investors and the public won't actually be able to tell from looking at central numbers like income what is really happening in the business. Which of these movements in asset values are likely to ever be realized?

And that could clearly detract from the information available to investors and the value of financial statements as a whole. That type of thing, by the way, was critical. That kind of abuse of mark to market accounting was critical, not just in this situation, but in the Enron scandal.

I will conclude by saying this. I hope that these comments reflect the complexity of this problem and the extent to which we view from the perspective of working Americans whose interest is in fundamentally the economy as a whole that this is an area where the Commission and the accounting regulators ought to look at it in a multi-faceted way and perhaps not with quite the level of polarization that some of the debate has had to date.

Thank you.

MR. WHITE: Thank you all.

Jim and I were trying to figure out how to conduct the next 45 minutes and we thought we would at least try to get us into the three general topics. So maybe we can take them in the order I'll describe them.

I recognize you all commented on them all and they all overlap, but the first topic would be the usefulness of fair value accounting, generally. Is it being used in the right places, and are there alternatives?

The second topic will be the application of fair value accounting. I guess another way, is 157 doing its job. Does it need improvement under current conditions, and so on.

And then the third topic would be the economic impacts of fair value accounting. And if we can kind of try to keep ourselves on those three topics if we go through without mixing them up too much, maybe this will work. So if we can start with the first topic of usefulness, I guess I'd like to start with usefulness of the fair value information to investors.

Scott, I want to start with you. You've already said it, obviously, that you think that fair value information is useful to investors, but we certainly heard Bill and Aubrey express some different views after you spoke, so maybe you could comment some more. And maybe particularly in response to what we heard from Bill and Aubrey.

MR. EVANS: I have said that I think fair value accounting is useful to investors. It provides very needed transparency to investors; not as a single number, but importantly as communication for management to investors about all of the issues that surround a fair value of assets. So the footnote disclosures, the assumptions that go into fair value assessments, are extremely valuable to investors.

I think we're on the right track. I think it's a steep hill to climb, and the gentlemen to my left have articulated some of the obstacles that we have. But to give up now would be counter productive and would harm the markets and the usefulness to investors more than forging ahead and trying to solve some of the problems that we're all wrestling.

MR. WHITE: Ray, do you have a reaction here?

MR. BALL: Yes, I'd like to differentiate between balance sheet treatment and footnote disclosure, or MD&A disclosure. I think it's fairly clear the information is useful for the same reason. Managers giving the information they have about the value of their asset portfolios, it has to be a value.

When you start to put it on the balance sheet, it becomes an issue of information not only to the equity markets, but to the debt markets. And bearing in mind we're dealing with institutions, some of which were levered 35 to 1, where most of the finance was debt, and the role of the balance sheet treatment of fair value historically has been to protect lenders.

Why does it protect lenders? Well, if an asset portfolio is impaired and is written down on the balance sheet, you can trigger a number of contractual rights in debt contracts to protect lenders against further actions that will harm them and so I think we should look at that aspect as well. Fair value is not just a matter of giving out the information, but it is putting it on the balance sheet for contractual purposes. It also in a regular fee supervision sense has effects.

I think the distinction between accounting reflecting and driving economic reality is a false one. The Heisenberg uncertainty principle says if you measure something it affects what's being measured, and once you put something on a balance sheet, you affect people's behavior. You can't stop that.

MR. WHITE: Okay. I will come back to you Bill, but Vin, do we want to go to you for a second? I want to get everybody who spoke before Bill, because Bill and Aubrey obviously took a different view than the first three of you. So I'd like to get your reactions.

MR. COLMAN: Similar to my opening comments, we have tried to be open-minded and look at the alternatives to fair value, and I think when individuals look at it objectively, you can clearly have concerns. The issue is when you look at the alternatives, are those concerns even deeper, right?

And I think our concern is when you particularly as it relates to financial instruments and the current model, what would be the unintended consequences of either changing today while we're in the middle of where we are, and what would happen, and then secondly, for instance, just to continue there is perhaps people would then begin to impute what they view the values to be. And that could be just as concerned.

When we looked at the various alternatives, I don't think we have found a better one. You can talk about amortized costs, and you could get into a very detailed debate of some of the consequences of some of the alternatives, whether its amortized cost, fundamental value. There's a bunch of other ideas that are out there that all would have consequences.

MR. WHITE: Bill, can I ask you to respond here and put an investor hat on when you do that?

MR. ISAAC: Of course. That's what I'm all about is trying to protect our banking system and our economy, and our investors. Nobody ever talks about the hundreds of billions of dollars that pension funds have lost because of these rules, that my aunt has lost because she had her money conservatively invested in banks that were a stable source for an investor to earn dividends and have values that would creep up. She wasn't a dot.com investor. She got wiped out in banks, a conservative bank, she thought.

And that's what I'm concerned about, are the investors. And I'm concerned about our economy and all the unemployment we're going to cause. It's senseless. We had one hand of the government, the treasury, handing out capital, just about as fast but not quite as fast as the SEC and the FASB are destroying it with mark to market accounting. It doesn't make any sense to me as a taxpayer that these rules are destroying capital and then you're asking me as a taxpayer to spend money to put more capital in banks, to replace the capital that we're destroying senselessly -- not because there are real losses, but because there are paper losses. When you market against some computer model, it doesn't make any sense.

We keep on hearing about 35 to 1 leverage. Our banking system doesn't have 35 to 1 leverage? A couple of investment banks did that failed. But our banks are the best capitalized banks in the world by far, and we're destroying them with these losses that are being run through the income statement that are not real losses. They're paper losses. They may never be realized. And I want to take back the words "fair value."

You can't have those words. You can't own those, because I am for fair value accounting. So we're arguing about what is fair value, and I'm telling you that I don't believe that marking to a computer model or fire sale prices based on distressed sales is fair value. Fair value is to take a look at the assets, look at the cash flows on them, look at the probability of default, look at the probable losses if you have a default, and then value those assets.

Let's take the 1980s. I said the money center banks were loaded up with third-world debt, and they were. And if you could sell it, you would fetch about ten cents on the dollar. If we had made them mark that to then cents on a dollar, which we did not consider to be a fair value for those assets, if we had made them mark that to ten cents on a dollar, we had a pan in place that we were going to nationalize all the major banks in the country, because they couldn't have survived that mark.

Now, did you want us to do that? Would that be right for investors? Would that be right for the economy and the country? Did you really want us to put the country into a depression and all the stuff that comes with that? I'd say no. So what we did is we looked at those assets and we said "What's the income off of them? What's the likelihood there is going to be a default? And what's the likelihood that these countries are going to renounce the debt and never pay it back?

And we factored that in and I don't remember what we marked them to, but let's say we marked them down 25%, and then a year later we would look at them again and say, was that mark okay, or should we mark them down more? And that's what I'm asking, is that we use some judgment. We let the bank examiners do what bank examiners do best and we let the auditors get involved in that process as well, and mark these assets to what is their fair, their true, economic value, not some arbitrary value based on computer models.

So I have my investor hat on and I have my taxpayer hat on and I have my bank regulator hat on, and I think this is an issue we all ought to care about very deeply. Well, we do care about it, so that's why we're all here.

MR. WHITE: Vin?

MR. COLMAN: Tom is here from the FASB, but I just want to clarify a more technical point. I mean, first of all, what the FASB and SEC in the press release put out was your comment around agreeing with judgment. I absolutely agree.

We need more judgment in the system. But one of the things that was tried to be clarified in the guidance that was out just recently was the concept of distress sale or distress market. To make it clear that those transactions are not determinative, they are input in the current market. But you should not be writing to distressed values, necessarily.

MR. ISAAC: But we have been.

MR. COLMAN: and, lastly, I just wanted to comment on it again, to repeat maybe from my opening comments, the difference when you said, you know, and then we go to regulators. To separate the accounting and information for financial reporting of an investor to the information that you're giving to regulators for capital purposes, because those discussions get gray and they come together.

MR. ISAAC: Okay. Well, let's deal with that, because that's a very important point. I don't understand how you can have applied these rules to a bank holding company that has publicly-traded securities, the mark to market rules, and then say, but regulators can do whatever they want with the banks, because when you are reporting that Citicorp let's say loses $20 billion in the year, nobody stop to ask, well what do the bank regulators think about that? And so I don't think that works. And I'm also not trying to hide any disclosure.

I think all the disclosure ought to be there as it is under the historical cost basis. You have footnotes. You have tables that show all the market depreciations. Anybody can look at it. I just don't think it's appropriate to mark something arbitrarily to an index or to a market price when the market's not functioning and destroy value, run it through the income statement, and take it out of the capital accounts of the company. Because then the rating agencies pile on, the short sellers pile on, and they destroy the company. And it doesn't matter what the regulators think.

I don't believe that a regulator would have wanted to close down Wachovia, but the market was sure closing it down. I don't think a regulatory would have wanted to have closed down WaMu, but the market sure wanted to close it down, because of these reports we're forcing them to make about their losses and the depletion of their capital. So nobody even asks what the regulators think.

MR. WHITE: Okay. Scott?

MR. EVANS: First of all, on the last point, I think it's more the current interaction between the regulations and the published financial reports that fees its way into the behavior of market participants.

I just wanted to go back to the issue of what's an appropriate standard on which to value a security that's held for sale, a financial instrument that's held for sale, regardless of the type of financial institution and the FASB, the ISB and their separate pronouncements. And it's come to pretty much the same conclusion, which is the management and its auditors should attempt to figure out what the market would pay for that asset on the statement day.

That's the standard. It doesn't say that they should take a ridiculous mark that to some better offers to them. It doesn't say that they should use an abstract model. It says that they should use reasonable judgment to attempt to value that market price. That is the appropriate price to have from a usefulness standpoint for investors for home financial statements are produced, and if that number is volatile, that number is volatile. But I think to Vin's point, the FASB and the SEC have gone to great lengths here to describe why you don't have to have knee-jerk reactions to uncertain markets. You can use reasonable judgment to try to ascertain what an arms-length price would be for an asset in today's market.

MR. ISAAC: But that presumes that somebody is going to sell the asset, and let's take the third-world debt in the 1980s. Nobody was going to sell it at 10 cents on the dollar. There were transactions at 10 cents on the dollar, but nobody was going to sell it at 10 cents on the dollar and they didn't need to. They had the ability to hold it. And if what you're saying is that we all ought to sit down and use judgment and not just rely on models and last transactions, whatever they are and whatever the circumstances.

If you're saying that you really don't believe that we ought to be doing that, then you and I are in agreement, because I don't think that's appropriate. I think that we ought to be searching for the true, fair value of those assets, and in that in many cases requires an analysis, not just looking at a computer screen.

MR. WHITE: Let's go to Ray, then Aubrey, then Damon. I think all three have been trying to get in here.

MR. BALL: I think there's a large amount of misunderstanding on what the standard calls for and I think the interesting issue is the following. The standard has three levels. You can use prices. You can use indexes, or whatever, or you can use basically judgment, estimate future cash flows and discount them. It probably, of all the accounting standards written in recent decades, brings more judgment into the accounting than any other.

I think the interesting question might be why wasn't that used. In other words, there was some talk around the traps that what happened was that people are faced with unusual circumstances were unwilling to exercise a large amount of judgment. If that's true, we might want to ask why. Is there something in the litigation environment in the U.S., or is it something in fear of action from the Commission itself that caused people to stay at level 2 and not go to level 3.

I think that's an issue that we should be looking at, but if you'd simply look at the standard itself, it is not the way it is not the way it is being characterized by many people on the panel today.

MR. ISAAC: I would just say I agree that there is in the language some flexibility that is permissible, but nobody is going there. Everybody is writing to the models or the indexes, and I think that's largely in reaction to the fear of litigation for the bank management and boards of directors, and for the accountants. And something has to change here.

MR. BALL: Yes, there's litigation and also regulation. You have a 20-year jail sentence hanging over your head under Sarbanes-Oxley certainly makes you act conservatively.

MR. WHITE: Aubrey?

MR. PATTERSON: Just to pick up on that point the move to level three to attempt to determine a reasonable caring value for those securities in an illiquid, frozen, non-functioning market, as I understand it from the responses from FASB, reflect the need for among the normal things you would expect the ability and intent to hold to maturity or for a long term and lack of risk of default that yet also include the demand for a liquidity risk test which gets us right back to the kind of issue that were affected by the basic freezing up of the markets.

So it seems to me to be particularly unhelpful and we've expressed ourselves strongly that we think that needs to be reconsidered. The nature of the model, if you look at a bank's business, a financial services company, you're not just looking at a piece of the asset side and disclosure as I indicated earlier can be in the footnotes in the M&A, an informed reader, which we are entitled to assume, certainly has access to that information to crack into his or her calculus as to the future stream of revenues from this company and future value.

But the fact is that CPA firms for all the reasons previously indicated are inclined to demand a rather severe test even in looking for ways to mitigate current illiquid market exit prices if the intent and ability is there to hold. And I think that's something that specifically and very importantly needs to be reconsidered.

MR. WHITE: Damon next, and then Rick and then Vin, and I'd like to move on after that into some of the operational issues, including OTTI, which I think we're starting to surface through some of the discussions about impairment and the like.

MR. SILVERS: Well, first, I think we need to recognize that the back-drop of credit market freeze-up where assets that I think were previously viewed as liquid in their nature. It all turned out to become illiquid, has its roots in a larger problem of opacity and shadow credit markets, and that it's hard to have this kind of conversation without having at its front-end some admission of the fact that off-balance sheet finance, completely opaque derivatives markets and somewhat unregulated hedge funds have something to do with this. And in that regard I want to acknowledge and compliment the chairman for his suggestion that we do something about those things.

The second point I want to make, because I think that both sides of this argument are in part incorrect, and I think it's worth pointing out why. First, it may be true that there are assets on bank balance sheets where there is a market freeze-up and yet they are fully performing and likely to continue to fully perform. I am in no position to assess what portion that represents at any given bank or in the industry as a whole.

But, what I do know is that the several trillion dollars in mortgage backed securities, which have as their underlying assets subprime loans with the 2 and 28 structures with exploited poor people on the other end of the transaction, are never going to be worth their full value. Pretending that they will be is dragging our economy down, because it is preventing these loans from being restructured. And so if the banking industry wants to pretend that those loans are going to be full value, that those people who are being thrown out of their homes are somehow going to return with a pile of cash that that is really and deeply deluded and continuing to do so is a very pro-cyclical act.

On the other hand, those advocates of the mark to market religion who find themselves without markets to mark to, right, be increasingly turn out to be advocating. And I think people here have been quite clear about it. We ought to take managerial judgment and run it through the income statement. As from an investor perspective, I find that to be a profoundly disturbing thing. That is, you move or down the hierarchy of 157 from actual market prices to increasingly kind of -- manufactured is too harsh a word, too harsh a way of putting it -- constructed mark to model. And I think there's some colloquial term for mark to moosh or something like that that you get into further down the line.

You're actually moving further and further away from the stated justification of the mark to market regime and that strikes me as something that the Commission in this study ought to think real hard about. And this was my comment about scientific theory which was picked up by one of my fellow panelists is that if you have this big idea that sounds very nice, which is that we should have everything mark to real markets, and then our financial statements, instead of being a kind of historical artifact will represent real value today.

If it then turns out we don't really have those markets to mark, except in a very limited set of assets, right, then we move into a more and more baroque set of arrangements that increasingly undermines the very justification for how we started. And I think that we are clearly there, and that there out to then be some really deep thinking about how we get to a system of financial accounting that is less theoretically correct and more tied to economic reality and more workable in circumstances like this.

MR. ISAAC: I would like if I could just say something, because I agree with most everything Damon's been saying this morning. But there is one area where you don't quite have it right. And that is that we aren't arguing -- I'm not arguing -- that these assets should not be marked to their true economic value. I'm arguing that they should, and the question is how do we do that. So I'm not saying that we should pretend like the subprime loans are worth 100 cents on a dollar.

The facts are there's $1.2 trillion in subprime loans -- 75% of them are fully performing -- and we're marking down the 1.2 trillion to about 30 cents on the dollar, and that's just not right. I would argue that the 75% that are fully performing have some loss in them and probably ought to be marked down some, and I would argue that the 25% that are not performing, obviously, need to be marked down a great deal, but not to zero. Maybe it's 50 cents on the dollar. I don't know what it is, but nobody is arguing that if we abandon fair value accounting or mark to market accounting that we should pretend like these assets don't have losses, because they do.

MR. WHITE: Rick?

MR. MURRAY: This section of the discussion, which really raises the question of why didn't the recent guidance accomplish more of what was intended to resolve the problem, I think is a key ingredient for the Commission.

Three quick observations about specific elements of why that may have been. When the SEC guidance was issued it emphasized the importance of the role of judgment in at least three aspects of its comments -- the complimentary FASB guidance did not mention the word judgment, leaving preparers and auditors somewhat at a loss to understand whether there was a full meeting of the minds there.

Also, there is no present guidance available from the PCAOB that would assist auditors in determining what the scope of their legitimate judgment is. We have urged that the PCAOB undertake that to supplement that attention that's received; and, finally, that leads to the I think critical factor of the specter of liability as an inhibitor to having that guidance work in practice. I know the concept of safe harboring is an unpopular phrase in many quarters, but it may be an essential component at least in the short-term of allowing the intended consequence of the guidance to in fact operate in the real world as it was desired to.

MR. WHITE: Tom, you look like you've been -- from a standard setters perspective -- trying to weigh in here.

MR. LINSMEIER: Much of this conversation so far has been one about accounting systems, as if its fair value versus amortized cost and the implications for the problems in our economy at this time. And some of the assertions have been made as if fair value system is widely prevalent and required within our current accounting system. It's not.

The only place where fair values are required are for derivatives through income and trading securities through income. Everyplace else available for sale is fair value on the balance sheet but through other comprehensive income that does not affect regulatory capital. And so some of the assertions are is if the current standards are causing all of these assets to be marked down to fair value where that's just not the case.

And to the extent that it is marked-down it's often to other comprehensive income not affecting regulatory capital, therefore, not requiring banks to sell to meet regulatory capital problems. So I'm not sure that the issue is really one of accounting systems or comparative accounting systems. But, even more importantly, if we were to compare the fair value system to an amortized cost system, present in every amortized cost system is a requirement to write down the lower of cost to market.

In these circumstances, even if we were to move to amortized costs, there would be the necessity in certain circumstances, to write down a market. In an amortized cost system, sometimes those write-downs are less frequent because of impediments to the write-down like other than temporary impairment, but you would still have the write-downs going on. And so to me, although we are couching this whole framework is if it's doing account systems, I don't think that's the real issue.

You have the problems and a requirement to write down under any of the comparative systems. An issue does remain though if those write-downs cause companies to sell and regulators think that the write-downs are really not capturing the economics. The regulators as they do with available for sale securities add back those losses to capital. That's still possible in all circumstances, even if the write-downs go through the income. And I think that's more on-point as to what the issues are than some of the constraints about doing accounting systems.

MR. KROEKER: That's a wonderful segue I think into one thing that I wanted to explore which I don't hear any disagreement about the need to take an impairment or a write-down when there's a decline in credit. So if you're not going to receive your cash-flows, it doesn't seem there's any disagreement. Where there seems to be some tension is what to do with this difference between what some have referred to as fundamental value or the value to hold, and the value that I perceive in the current market place.

Vin had an idea that I would like to explore which was somehow distinguishing for impairment purposes between credit impairment and impairment that is based on liquidity. I think your proposal was to treat those separately and maybe take out the liquidity impairment from income calculations. But I'd like to see people's responses to that.

MR. COLMAN: Thanks Jim. That would be good. Yeah, thanks Jim. Because I was listening to this conversation and where it went to Tom's point is not really on the fundamental values. It's really about impairment and it was raised before the so-called OTTI, other than temporary impairment, and a couple suggestions.

Right now, if you go into the literature, based on the form of some transactions the triggers and how you do it can be different. Right? So if it's in a securitization, that's a set of so-called rules. So there are several places of rules. One would be if we could combine them into one would be very, very helpful and so it's not a form drive other than impairment type test. It's a substance driven, which I think that we would all agree with with respect to some common ground.

Secondly, the suggestion is we've been saying wait a minute I have no problem recording an impairment for the credit losses. Well, we can figure that out. We do that today in certain areas. We can figure out what the credit loss is and charge the income statement for the credit loss under any basic principle of accounting today, because you incurred the loss today, right, in the current market. So you probably have common ground around that.

The difficulty is what are the other aspects that have caused an impairment, and perhaps those aspects come together. We have full transparency for an investor, so it goes through other comprehensive income, which doesn't go against regulatory capital. And we move it to the face of the income statement, not in determination of net income, so that an investor can see what are these other changes, fully transparent with some disclosures, obviously, in the computation of where it goes. So that now you have achieved both objectives, right? We have harmonized the various triggers and application. We have separated credit from liquidity risk and we've kept to the principle of ultimate transparency for investors.

MR. WHITE: Bill, I would love to get input.

MR. ISAAC: I think there is common ground there. I would say I also am concerned, and I'm not sure how you're dealing with it, but we keep on making the distinction between what the regulators can do with capital versus the balance sheet effect. And I think in the world we're in with short-sellers and the rating agencies, and a lot of volatility in the markets, I'm not sure. I guess I'm not sure what you're proposing.

What's the headline number going to be when that statement gets released? In other words, if you were using historical cost-based system you would have in footnotes and tables and it wouldn't be affecting income and it wouldn't be affecting the capital of the consolidated company. I'm not talking about credit losses.

MR. COLMAN: But I just want to clarify. When you say you got to historical cost like Tom just articulated, it always had an impairment test, but we lower cost to market.

MR. ISAAC: But we don't have any argument about permanent impairments, okay?

MR. COLMAN: Or other than temporary impairments, right.

MR. ISAAC: We don't have any argument here at all about permanent impairments, because I think we need to take permanent impairments. But the question is when we have something other than a permanent impairment, what are we doing with that.

I mean, the regulators pretend like it didn't happen, but is that going to be very helpful if the headline when the bank releases its earnings, when Citigroup, the parent company, releases its earnings, what is it going to release and what's it going to show for its capital in the consolidated company. I'm trying to understand your proposal.

MR. COLMAN: I'm with you. Two different points. I'll answer crisply your first one.

What's it going to show in net income? It would show in net income the impairment as it relates to the current, incurred loss relating to credit and not liquidity.

MR. ISAAC: Okay.

MR. COLMAN: Okay. And they liquidity would go into other comprehensive income is the suggestion and it would be moved to the face of the income statement, right? So that would have a charge. It would have a reduction of the equity of, you know, the entity. All right? On the face of the income statement but not in the determination in net income -- to the point about the headlines -- the headlines are generally the determination in net income.

MR. ISAAC: Without this impairment charge Citigroup, let's say, is earning a dollar a share. This temporary impairment charge does what to that number? I mean does it bring it down or are they still announcing a dollar per share?

MR. KROEKER: If I understand your proposal then, you would still come to net income that would only be based on credit losses. Below net income you would have this line that says, you know, the mark to market difference, so the liquidity portion or some other portion and you would come down to a comprehensive income number.

You already have to report comprehensive income that includes that. This would just be moving that from a separate statement up to the income statement. But net income would not include liquidity, if I understand.

MR. COLMAN: That's correct. And the objective is to give more prominence to other comprehensive income.

MR. ISAAC: And I guess I don't understand why you want to do that as opposed to putting it in a separate statement so investors can see it. But they also don't get confused.

MR. WHITE: Scott?

Mr. EVANS: Yeah, I think it's a constructive suggestion, Vin, and I think to the extent that you're clearly parsing a credit-related impairment from liquidity related impairment, it adds to transparency for investors. But as you move from an entity that is primarily in the business of engaging in long-term investments that are held to maturity, two-way entity that is primarily engaged in creating trading profits with, you know, short-term activities, the argument to have it in the prime face of the income statement increases.

And so at some point you reach a tension where you'd have to argue that it should be above the line; and, I don't know how to solve that problem, but I think the direction of your suggestion is a positive one.

MR. COLMAN: Can I just respond to that? I just want to again clarity -- we're talking about an impairment test. The literature, separate, everybody uses 157. Leave 157 for a minute. You put assets in the three categories. To the extent it's trading, because it is the normal churn-type trading, all right. That is a mark to market model irrespective. Impairment generally doesn't matter because you're at a mark to market, because that's the aligned with the business transactions as people were saying. The tension point goes when you start drifting to available for sale and held to maturity.

MR. WHITE: We could just pause for a moment here. I see some of the commissioners leaning forward at different points here. Are there any points, that the commissioners, any questions there or thoughts?

CHAIRMAN COX: Actually, I don't want to interrupt the flow. I think it's going well. I know we're running out of time here, but I'd like to keep this going.

MR. WHITE: Okay. Ray, you had your hand up?

MR. BALL: Yeah, I think Vince's suggestion is interesting. I think it's a fairly complicated issue though for various reasons.

One is, I think it's very difficult, especially in the current circumstances, to sort out the extent to which we have a liquidity problem or a risk and uncertainty problem. And these two are very closely tied. Anna Schwartz had an o-ed piece in the Wall Street Journal last week discussing this. And right now, if you look at the macro sense, the fed is pumping liquidity into the system and is complaining the banks are sitting on it. That tells you something about the uncertainty they face and why they're holding capital rather than liquidity.

A second observation is I'm not too sure that we ought to give the financial institutions incentives to encourage illiquidity by taking the effects of it out of the income statement. One of the things that struck me about the current episode and hasn't been brought up much in the debate is it's remarkable we have a trillion-dollar market in the United States which prides itself on the depth and efficiency of its capital markets and we say it's illiquid.

I mean, that's a problem; maybe we ought to address the issue as to why this is a problem rather than mandating it and saying let's take it out of the income statement. In relation to that, it's worth thinking about what would happen if mortgage-backed securities had not been held iBanks, nBanks, but had been held entirely in pension plans, 401K plans, endowments, sovereign funds, more conservatively managed institutions like Berkshire-Hathoway, we wouldn't have a liquidity problem, because they wouldn't be forced to sell to meet leverage constraints when their asset portfolio hiccupped in value. So I think it's a nice idea, but I'm concerned about the incentives in it, which is to basically, once again, shoot the messenger and ignore the message.

MR. ISAAC: Two quick comments: one is I don't see how you separate an uncertainty problem for a liquidity problem. They are one and the same. If you had certainty, you wouldn't have illiquidity; and I mean they're the same problem. Secondly, I don't know of any banks in a significant way that are forced to sell these assets. They are being marked down anyway.

And I mean there's plenty of liquidity in the banking system, and the Fed is adding more all the time. But banks weren't forced to sell these assets. They didn't want to sell these assets. They won't sell them at 20 cents on the dollar, but we're making a mark there just as if they had sold them.

MR. BALL: You know, I guess the question is whether they're selling. An allegation is they're selling below fundamental value. And the question there is whether that occurs because there's basic illiquidity in the market in absence of buyers, or whether buyers believe that there's so little opacity, so little transparency, that they don't know where the toxic stuff lies. And that's, I think, part of the issue.

MR. WHITE: Damon?

MR. SILVERS: I think that liquidity has been a term that's hidden a lot of other problems. My illiquid market is your market where you won't pay my price, right? And I think we saw this in the discussion about what used to be called the bailout where it appeared as though the notion of liquidity is going to be the cover under which assets were purchased for clearly more than they were worth by the public.

The question that I have about Vin's proposal is there's a mortgage-backed security in the portfolio and the mortgage-backed security represents mortgages that have not reset yet. And the marketplace has looked at those mortgages and said we know they're going to reset. And, in fact, the mortgage-backed security is quite complicated. And, given what we've seen in the last couple of years, we're not comfortable knowing what's really going to happen when they reset, particularly in the context of an economy that is dramatically declined since, say, the last pool reset.

So there's not much liquidity in that security right now and there's a big bid offer spread. But the security is more or less performing today because it hasn't reset yet. How would your proposal handle that situation?

MR. WHITE: Okay, so, looking at my watch here. Aubrey, you have your cared up, so I'll let you comment and then we'll go and we'll do one minute each for I guess we'll call them closing comments or thoughts, but just a minute so we can stay on schedule here. But, Aubry?

MR. PATTERSON: Just to that point, which is a great point, and there's obviously no direct answer, but it still goes back to the fundamental issue that the market has been dysfunctional. It has not been efficient. It has not been effective, and the net result of that is these values, these exit values in the absence of a willing buyer, willing seller market at arms-length are forcing write-downs in many cases that are many times the potential losses that were referred to.

Our thesis is that it doesn't make sense whether the regulators understand it or not. It doesn't make sense to expect the investor public that's relying on this as an indication of the futures stream of earnings of an institution to take a full hit on that impacted value knowing that the more correct economic value is the present value of the future stream of income of the securities, 80% of which are more likely to perform than not.

So we continue to support the concept that there has to be a rational approach to credit default as a determinant, but the liquidity risk test which continues to be supported by FASB, takes you right back to the current illiquid market. And, that to me is the circle that has to be broken.

MR. WHITE: Okay. So, Damon, we'll start with you, one minute.

MR. SILVERS: Going the other direction?

MR. WHITE: I wasn't going to give you enough time to really prepare more than enough.

(Laughter.)

MR. SILVERS: If you give me enough time, I'll use it!

I hope that the Commission and our guests here from the other regulators take one thing away from this conversation, which is that both sides of the argument have some valid points and that the issue of pro-cyclicality is more complex than one system drives one way and one drives the other.

On the other hand I think it should be quite clear that we are not in any sense at this point in relation to these issues and financial institutions talking about a mark to market system. All right. We are having an argument about which administratively derived values are going to be used and under what rules. And there are a series set of competing considerations here that I think regulators need to look at, and I would reiterate.

And I think Vin's proposal has this quality to it, but I'm concerned about the details as my question indicated. I would reiterate that I think that one way of acting carefully in this situation is the sort of approach that tries not to make two big changes today in this environment in the accounting and disclosure regime looks to counteract the pro-cyclicality through the safety and soundness regulatory structure, uses the opportunity the Commission has here to look at some of the deep conceptual problems that the increasingly universal move to a mark to market system seems to be bringing up.

And, finally, that all aspects of the government be serious about what is really the underlying drivers of the financial crisis, which my questions today have tried to point to, which is that our financial institutions and home mortgage financing structure have not restructured these loans in a way that will undue the downward spiral and provide relief to Main Street, to America's communities; that we have not yet, despite Chairman Cox's urging, passed the necessary statutes to empower the Commission to shine a light on the shadow credit markets.

And, finally and most fundamentally we have not dealt with the fact that our economy is not a sustainable thing when 40% of its corporate profits come from the financial sector as was true in 2006, and we need to do some more real things and less shuffling of paper.

Thank you.

MR. WHITE: Rick?

MR. MURRAY: We anticipate that the Commission's conclusions will be crafted more by the use of scalpel-like instruments than blunt instruments. And we also urge that in doing so the Commission pay careful attention to the implementation inhibitors that could cause a well-designed solution to fail to achieve its goals.

MR. WHITE: Aubrey?

MR. PATTERSON: Just a word of thanks for allowing us to express our opinions and have this discussion. We appreciate the opportunity to put forth our views and look forward to hearing the Commission's response.

MR. WHITE: Bill?

MR. ISAAC: I can't be as brief as either one of them, but I'll try to be. I'll try to be brief.

First of all, I would point out that FAS 157, as I understand it, came into being in 2006. So it's not as if I'm asking that we change the whole system of accounting that has been developed for centuries. I'm asking for a very bad rule to be suspended until we can think about this some more and stop destroying so much capital in our financial system.

I think that's a basic step that needs to be taken immediately. And then I want to pose a question for everybody to think about. I think that at the beginning of this period we're in, inflation was under control. Economic growth was good. Unemployment was low and there were no major problems in the banking system. And then when this subprime thing develops, it's a $1.2 trillion of subprime mortgages. About 2 to 300 billion of it was estimated by the FDIC to be in the banking system in FDIC-insured banks, 2 to 300 billion.

Let's say 300 billion, and the rest was spread out all over the world. The likely losses were estimated to be roughly 20%. So 20% of 300 billion is 60 billion, and the banking industry in 2006 had $150 billion of earnings after tax, and $1.4 trillion of capital. So how did we let that little bitty problem, and I don't mean to minimize it, but it's not a big problem in the scheme of things. How did we let that get so big?

And then I take us back to the 1980s. We had our money center banks were overwhelmed with third-world debt that would have driven them insolvent if we had marked to that arbitrary market. We had a deep recession in the agricultural sector. We had a rolling real estate recession. I mean, we had a deep recession in the economy as a whole in 1981-82. We had a 21-1/2% prime rate. We had an agricultural depression and we had a rolling real estate recession that eliminated many of the regional banks including nine of the ten largest in Texas. And, we had 3,000 bank and thrift failures during that decade.

Now, how did we get through all that? And once you get past 19821, you have one of the strongest economies in the history of the world. How did we get through all those problems and still have one of the strongest economies the world has ever seen for the next two decades almost in the face of all those problems?

I've got to tell you I can't come up with any other answer than that the accounting system is destroying too much capital and therefore diminishing bank lending capacity by some $5 trillion. And, that's why we're in deep trouble in the economy right now. It's due to the accounting system, and I can't come up with any other explanation.

By the way, thank you very much for having me here. I mean, I really think this is helpful and I think we have some common ground as near as I can tell.

MR. WHITE: Scott?

MR. EVANS: Thanks very much. I'd like to add my thanks to the Commission for my opportunity to express my views today.

I don't agree with Bill as we've discovered. I'll state very succinctly I think that the fair value standard is appropriate for assets that are in the trading portfolio or held for sale. I think the process that the standard setters have come up with, the FASB, the ISB, the SEC, has enhanced transparency to investors and helped to serve the primary role, as Chairman Cox outlined, of financial reporting, which is to inform investors; and, as such, fair value is a good thing.

The thing to focus on right now is that the problems we're having is the use of the standards and the ability of preparers to communicate with investors in a consistent fashion. That's what FAS 157 is all about is communicating in a consistent fashion in a standardized way, and there are some problems with that. And that really, if you look underneath the arguments, the common ground is that this still is problematic.

However, I think we can all feel good about the fact that the SEC, the FASB and the ISB, are all on the case. They've released a number of pro-active comments recently giving preparers and auditors guidance on how they can make fair value assessments in a consistent matter that enhances transparency rather than provides confusion to investors. And I think it would be a serious mistake for us to retrace our steps and abandon this progressive step of FAS 157.

MR. WHITE: Vin?

MR. COLMAN: Thanks for having me also. I really do appreciate it. I just lead with perhaps a couple comments.

One is and some of them is may be a summary of what's been said here. I really ask that we separate the accounting from the root causes, because when we say the accounting has caused this, you know, there are debates around pro-cyclicality. I think those debates are fair, but there are some other root causes here. And I just hope that, you know, to the suggestion that somebody made about broaden the scope of what you're looking at beyond the accounting so we don't try to have accounting be the answer to some issues that I think go beyond that.

Secondly, to ensure that we do continue to try and separate the objective of regulatory capital and safety and soundness with the objective of the principles of financial reporting, because they're different for investors. I would also ask that we keep a principle in mind for the next 90 days that you're thinking about, and one is around transparency for investors. As I think we just stated, is the fair value model, does it have imperfections?

Of course, somebody can assert there's imperfections and we can work on those imperfections, but to have a fundamental change I think could have serious consequences. And we've offered some ideas that we'd like to pursue going forward that perhaps can help the system without undermining some of the principles that we have.

So thanks again for having me.

MR. WHITE: Ray?

MR. BALL: I think there's plenty of blame to throw around in this episode. We haven't addressed the people who, institutions who created these toxic assets and their behavior. We've been talking about blame on the accountants.

I'd like to just simply say that affair value is not an accounting term. It's a legal term. It means the amount that a willing buyer would pay in a market transaction. And if the United States, which has the deepest, best capital markets in the world and all of the bodies regulating those capital markets can't make that concept work in the United States, then we have a problem.

What's necessary to make it work? I think the issue was structural issues in the market rather than recording what markets do on balance sheets.

MR. WHITE: Okay. Jim and I would like to thank each of the panelists for very helpful input and thank all of the observers for being here. This is going to be very helpful for us as well work on the study. We're going to resume again very shortly, but Chairman Cox, do you want to give us a couple of closing words?

CHAIRMAN COX: I just want to add my appreciation to that that's been expressed by John and by Jim to each of you. This has been by our own standards -- we have many of these roundtables -- absolutely superb.

All our roundtables we get a lot out of them, but particularly I want to compliment this panel and the depth of this discussion and the interaction. It's been hugely helpful, and obviously we'll be on a continuing basis interested in consulting with you and hearing your views.

Thanks very much for what you've devoted in preparation of being here and the time that you've given us this morning.

MR. WHITE: Okay. We'll resume in about five or six minutes.

(A brief recess was taken.)

MR. HEWITT: We'll go ahead and get started if everybody will take their seats please. And, good morning again.

I am Conrad Hewitt, Chief Accountant of the SEC. I am also again pleased to welcome everyone, the Commissioners and the observers and the panelists that are here with us today on this Commission's roundtable on mark to market accounting.

Joining me as a moderator on this panel is Wayne Carnall. Wayne is the chief accountant for the Division of Corporation Finance, and I thank Wayne for joining me and helping me today. I need a lot of help sometimes.

The requirements to use fair value or current market price particularly for brokers and dealers in securities-impaired investments have been around for many decades. I can personally attest to that because I was an auditor in the mid-60s, auditing fair value for brokers and dealers, investment companies, and mutual funds. In about 1970 the banks wanted to be able to reclassify their mortgages into two categories available for sale and held to maturity.

And at that time, the fair market value concept on mortgage securities came into being. So that's been a few years ago. Fair value has seemed to work very well over many years; however, recently, as we all know in the financial crisis we have here and worldwide, there seems to be some problems and doubts about fair value. The extent to which the U.S. GAAP requires financial institutions to present at fair value changes in fair value recognizing income statement, which is really the specific meaning of mark to market accounting.

That really depends on the characteristics of the financial instruments, its legal form and how the company intends to use the financial instrument. And, again, I think as in the previous panel the fair value usage and application really revolves around basically financial instruments. For many months now there've been numerous events that have caused large disruptions in both the credit and equity markets around the globe. These events resulted in some markets become inactive or having significant declines in liquidity, which in turn have led to challenges for registrants and their auditors in applying GAAP, and also challenges for investors and other users of financial statements in analyzing financial statements impacted by fair value accounting.

To assist in meeting these challenges, my office in conjunction with FASB staff issued a letter on September

30th, not to long ago, on the application of fair value measurements in our current market environment. Additionally, on October 14th, I issued a letter to FASB chairman Bob Hirst regarding the application other than temporary impairment model to perpetual preferred securities. Now both of these letters were intended to clarify the application of fair value measurements and to emphasize the need to use reasonable judgment.

And as with the first panel, we have a number of questions for this panel and we anticipate that Commissioner's observers from the FASB PCOB ISB, Federal Reserve and Treasury may from time to time participate with questions for the panelists as well. And we'll certainly just raise your hand or turn your timecard over and we'll be sure to accommodate you and recognize you.

At this time I want to introduce our distinguished panel starting with Randy way over on my left. Randy Ferrell is with the Ficara Bankshares Inc., and he's the CEO. Next to Randy is Patrick Finnegan from the CFA institute. He is the Director of Financial Reporting Policy Group. Next to Patrick is Bradley Hunkler, Western Southern Life. He is the VP and controller.

And then we have Lisa Lindsley, with the CTW Investment Group, Managing Director. Cindy Ma, Houlihan, Lokey, Howard and Zukin, the managing director; Chuck

Maimbourg, Key Bank, Senior Vice President, Accounting Policy; Richard Ramsden, Goldman Sachs, Managing Director; and, Russell Wieman, Grant Thornton, National Managing Partner.

So Wayne and I have kind of divided. I mean, I don't think we'll have time for all of these topics, but we'll try to limit maybe one question to each of the topics, like the pro-cyclical situation that we have, active versus inactive markets, the application of 157 disclosures, and then maybe we have time OTTI, other than temporary impairment. So let's kick it off.

I'm going to kick it off with Randy. I said do you believe that the application of fair value accounting is pro-cyclical? That is, does the application of fair value accounting lead to increasing breakdowns and declining markets in leading to increasing write-ups and good markets. In other words, we've had tremendous, high, very positive markets; and, now, when everything is going down, nobody likes 157. So, Randy, what are your comments on that?

MR. FERRELL: My thought is definitely in declining markets, 157 or fair mark to market, would lead to writing assets down and showing them as being under-valued, whether it's on the income statement balance sheet in whatever form. And it would have the opposite effect in increasing market.

MR. HEWITT: Chuck, do you have any comments on that?

MR. MAIMBOURG: Well, I think it's interesting, the fact that I was thinking during observing the last panel that, you know, we've changed the definition with 157. That's what's changed, because we've gone from willing buyer/willing seller to an exit price. And I think a lot of times we're trying to portray to investors in giving a value that we're going to sell it for, when in fact there's no intention whatsoever to sell it. I think if things are in held for sale, that's one issue. But, we're unfortunately getting into a lot of other assets that are not going to be sold, and therefore we're giving an artificially low value given the current markets.

MR. HEWITT: Any other commenters on pro-cyclical?

MR. FINNEGAN: Con, this is the view that I'm going to express I think is widely held among investors and certainly my colleagues at the CFA Institute. Pro-cyclicality is something that exists in good times and in bad. I don't think it's something that you could say is only an impact or an effect the exists in bad markets. But I don't think it impairs the relevance of fair value reporting for investors, at least in general purpose financial statements.

So I think a distinction that I heard discussed this morning -- it got some attention -- is that we have to distinguish between the role of financial reporting for prudential requirements for regulatory and capital adequacy purposes, and financial reporting for purposes of investment decisionmaking purposes. So pro-cyclicality is a consequence.

However, I think one of the things that we also have to keep in mind is that if managers in the evaluation of assets in rising markets adequately take into consideration things like liquidity risk, model risk, and the like, perhaps that would temper some of their enthusiasm for leveraging their balance sheets the way they did.

MR. HEWITT: Brad, I believe?

MR. HUNKLER: Yes. I guess the pro-cyclicality effect I would say is a good indication why we don't believe that fair value should be a significant component, one, of regulatory capital, or two, the balance sheet and the income statement.

We do, however, recognize that it does provide valuable information to investors and do not oppose disclosing that information in the notes to the financial statements or the MD&A in a way that it can be transparent and usable by the investor groups. But what happens in the positive markets, I don't think companies get credit for the pro-cyclicality of facts. Instead, it's easier to ignore when it's a positive impact. When it's a negative impact then it becomes an issue.

So I don't think that companies have been touting their unrealized gains and losses in the market place. Over the last two or three years, I represent an insurance company. We certainly have significant unrealized gains and losses due to market movements. We don't tout those unrealized gains and the good times, and we certainly don't necessarily respond in a significant way when those unrealized losses are emerging due to market effects during times of crisis like we have today. We make our decisions based upon economic valuations, based upon the expected cash flows of securities that underlie our portfolios.

MR. HEWITT: Any other comments on that topic? I must apologize. I need to back up for a moment. I forgot to offer each of you your opening statements. So that we can keep them brief, I will do that at this time. I'll start with you, Russ.

MR. WIEMAN: Well, I can certainly meet your brief requirements here.

First of all, I'd like to thank the Chairman and the Commissioners and the staff for an opportunity to speak today. I just have a couple of things from an opening remark perspective in that the fair value reporting, personally for me and my firm, that we strongly support the fair value reporting. As we heard in the first panel, it's certainly not perfect.

There are a lot of judgments that need to be made, and perhaps we could look at certain things on how we might be able to get a better answer than we have today. But, right now, it's the method that provides most transparency for investors and we strongly support that. We also believe from what's gone on in the past months and weeks relative to the markets, if anybody doubted the world global market, they can have no doubts about that any more. And we think it's important that the standard setters and the regulators in all these markets get together and make sure that we have some kind of standard that we can all live with so that one jurisdiction doesn't get an advantage over another or another with a disadvantage.

We also need to have the investors be able to have comparability and consistency. So we strongly urge all the regulators to have a global answer, not a U.S. answer, not an E.C. answer. It needs to be the same. We also believe, as long as I'm on standard setting that we believe that standard setting in the U.S. and elsewhere needs to remain independent, and to the extent that the political atmosphere gets into it, I don't think we ever get the best answer.

At least that's what we believe. And, again, on something that was discussed a lot at the last panel relative to the differences in what the regulators see from a safety and soundness perspective and the transparent reporting that you need from financial reporting, we think that some consideration should be given to the extent that it can to give the fair market value transparency for the investors and some solution relative to the capital situation for the banks.

Thank you.

MR. HEWITT: Thank you, Russ.

Richard?

MR. RAMSDEN: Yes, first again, I'd like to thank you for giving me the opportunity to present here today. Just by way of background, I'm an equity analyst covering U.S. banks. So my role is to analyze financial statements and make investment recommendations on the back of that. And I really would like to make four comments; and, again, I'm going to keep these very brief.

The first point is that I do think that analyzing financial statements as an investor requires transparency of information, but also, importantly, comparability of information between firms. And in my view mark to market accounting provides the most accurate representation of what the true financial position of a firm is at any given point in time.

And that is central in my mind to understanding both its capital position at that point, but ultimately it's value. So I do believe that mark to market accounting is probably the best alternative we have, both in terms of comparability of information, but also in terms of transparency.

The second component, I would say, is that I do think today in particular that transparency is going to be critical in restoring investors' confidence in the financial services sector. And I think investors understanding enhance ability to price risk and provide capital to the industry would again in my mind be negatively impacted by any move away from mark to market or fair value methodologies. I think that's particular true given the uncertain economic environment that we have today.

The third point I would make is that I don't believe that changes in mark to market accounting rules would actually alter investors' perception of risk in these companies. Rather, I think what it would do is lead investors to impute market values based on other input, and I think in turn that could actually lead to inaccurate conclusions. So I don't think it is going to impact really the way in which investors view financial institutions.

And then I would say the fourth point, which I think we have heard before is I think it's just critical that we differentiate cause from a fact, because in my mind I don't think that mark to market accounting has been the cause of this crisis. It clearly has been banks granting loans and holding securities that haven't incurred real losses. And I think really what the mark to market rules have done is just reflected that deterioration.

The one point I would add to that is I do think it is very important to take the $750 billion of losses that the financial industry has incurred both here, but also abroad, and disaggregate it into losses that frankly have been incurred because of credit deterioration, losses that have been incurred because of liquidity insofar as that can be measured. But also losses that have been incurred because of changes in the required rate of return that investors have for holding those instruments today.

MR. HEWITT: Chuck, please?

MR. MAIMBOURG: Good morning to all. My thanks also to the Securities and Exchange Commission for hosting the roundtable this morning on fair value and FAS 157. I appreciate the opportunity to participate.

I am the Director of Accounting Policy and Research and Key Bank, which is a 100-billion-dollar bank, located and headquartered in Cleveland, Ohio. Key adopted FAS 157 for both financial and non-financial assets and liabilities as of January 1, 2008.

Based on our most recent filing, form 10Q as of the quarter ended June 30, 2008, we had approximately 12% of our assets were fair-valued on a recurring basis. Approximately 96% of these were categorized as either level 1 or level 2 assets under 157. Only about 1% of our liabilities are fair-valued on a recurring basis.

We have certainly had our issues and challenges with fair value accounting, particularly in the areas of commercial real estate and private equity investments as the financial markets have continued to deteriorate. However, our biggest challenge has been with the intersection of FAS 141R and FAS 157.

In April 2008 Key was considering the acquisition of another bank. During our preliminary due diligence process, we were informed by our auditors that as a result of FAS 157 and the continuing market turmoil, that when valuing portfolio loans, those are ones that will be held after the acquisition. All aspects of value had to be considered, including credit, liquidity, and interest, because the loans acquired for portfolio must be valued at fair value at the acquisition date in accordance with FAS 141R.

Based on our various discussions at that time, it was our understanding that the other "Big Four" firms and the SEC had concurred with that conclusion. The capital, ratio and other transaction ramifications of this accounting conclusion caused Key to not pursue this particular acquisition as well as others throughout the balance of the year. I believe our experience with FAS 141R and FAS 157 highlights the fact that there are more consequences of 157 that have not been felt by the financial markets at this time.

Therefore, our discussions today and the SEC's fair value study are critical in determining the best path forward for fair value accounting in FAS 157.

Thank you.

MR. HEWITT: Thank you, Chuck.

Cindy?

MS. MA: Good morning.

Many opinions on fair value have been offered, and I am really honored to be able to be here to add my voice to the chorus. As a background, I am evaluation professional, having been doing valuation on various types of level 3 financial assets since the global crisis started in July 2007.

While many people recognize that FAS 157 does not represent a fundamental shift in the application of fair value accounting, FAS has called for the repeal of the standard in hopes of soothing recent market chaos. I believe that this debate may have been caused by the misconception that mark to market automatically equates to fair value, which is not the case. While mark to market accounting is an important indicator of fair value for regulators and investors, FAS 157 does provide the flexibility to consider a wider range of valuation techniques to deal with situations when market prices are distressed and not representative of fair value.

Fair value accounting should not be suspended or eliminated. Investors must have confidence in the reliability of the financial statements. Without that confidence, there would be no investment. It would be pure speculation. With the level, focus and attention drawn to fair value accounting, changing the rules in the current market conditions would only diminish investor confidence.

Many helpful statements have already been issued to try to clear up the confusions, but more clear guidance is needed to address incorrect interpretation and to communicate the intent of the standards. Some opponents of FAS 157 claim that companies may be required to mark position to market based on distress transactions. However, as already clarified by FASB, FAS 157 does allow for the use of mark to model when observed transactions are distressed.

Granted that, recognizing those distress situations is a challenge. In equity markets, indicators of market activities, like trading volume and bid/ask spreads, I easily observed. However, for the financial asset classes that had been making headlines such as the RNBS, the CDOs, the CLOs, the credit default swaps, there was really no exchange and no centralized data source to tell people to price the transactions.

But, let's understand a fact, okay? Many of those structured investments were created to be bought and held. They were not created for day-to-day trading. And even under normal market condition, many of those instruments were transacted what I call "by appointment only." And therefore in the current market conditions it's just really no surprise that we didn't see that many transactions in those instruments. And when the transaction occurred, they occurred at very wide and disbursed price levels.

Since it's really impossible to really read the mind of the parties involved in the transactions, clear guidance is really needed as how to incorporate or consider those market data in a fair value analysis. However, it is important to note that consideration does not mean 100% reliance. And I also would like to make a distinction between illiquid and distress assets. Or, correspondingly, that's what I will call "volume illiquidity discount" and "funding illiquidity discount." Think about it.

Even in less troubled times, different markets will exceed different levels of liquidity. And there is a body of research, generally support a discount on securities that are less liquid. For example, even in normal market, there is a liquidity premium between the on-the-run and off-the-run treasuries. Even your normal audit transactions, there is a difference in bid/ask spread between agency paper and subprime mortgage bonds. And, therefore, it is appropriate to include a volume liquidity premium in valuing a level 3 asset.

However, many market participants including the structure investment, via Co-s the SITH hedge funds and financial institutions, have recently been forced to sell assets at prices they considered too low. This is actually caused by what I call funding illiquidity or liquidity driven by certain market participants' need for immediate capital or cash. In my opinion it may not be appropriate to include a funding liquidity premium in valuing the level 3 assets, especially when investors have abundant financial resources to hold those assets in the foreseeable future.

Calibrating valuation input for level 3 models using distress or fire sale prices will certainly result in liquidity premium, far in excess of a reasonable level for fair value purposes. Market participants should really work toward a more comprehensive, economic base, liquidity premium model that incorporate orderly market transactions. I believe this point has been confused by market participants and in the time when the liquidity of many instruments has declined so much, it is important that this factor is well understood by the preparers as well as the users of the financial statements.

The bottom line is sometimes a market price is a fair value. Sometimes a model price is a fair value, but fire sale prices are never fair values.

Thank you.

MR. HEWITT: Thank you, Cindy.

Lisa?

MS. LINDSLEY: I would like to thank the Commission for the opportunity to participate on its panel.

I represent the CTW Investment Group which works with pension funds sponsored by unions affiliated with Change To Win to enhance long-term shareholder returns through active ownership. Change To Win is a federation of unions representing nearly six million members, and its affiliates participate in both public pension funds and Taft-Hartley plans. We estimate that since the beginning of the year the retirement funds of U.S. workers have lost over 1.5 trillion just through the decline in the value of their share of U.S. equity markets, not counting the decline in the value of their bond and mutual fund investments.

As a result of our work on behalf of pensions, we have a unique perspective on the financial crisis that's relevant to today's discussion. Beginning in January of this year, we engage the boards of directors of the six banks that had suffered the largest subprime losses, of which three continue to exist today. We wanted to know what the boards of these firms had done to oversee risk management. We learned that many of these large banks did not monitor the underlining credit risk of their MBS portfolios and that they focused on the interest rate risk related to CDOs, not the credit risk of the underlying assets.

Directors came to understand too late that the complex nature of the products their institutions were originating and investing in that banks continued to increase their risk profile with no regulatory mechanisms to stop them. This dynamic was not caused by a mark to market accounting. Our experience with the banks has reinforced our view that more robust regulation by a stronger SEC is necessary. The SEC should have comprehensive jurisdiction, both over securities linked to currently registered securities, such as credit default swaps and other derivatives, and the currently unregulated actors who have contributed to the crisis.

Our pension funds have very conservative investors with little direct exposure to the toxic securities at the epicenter of this crisis, but they've been aversely affected by the actions of credit rating agencies, hedge funds, private equity funds, and other unregulated actors. We support the concept of fair value accounting where it provides greater transparency and uniformity to readers of financial statements such as our funds.

We recognize that mark to market is not the greatest indicator of intrinsic value for all asset classes. We also believe that it's very important to take into account the liability profile of various non-bank financial institutions before applying fair value accounting to any of them.

The current, mixed attribute system could be improved by providing further guidance in limiting the discretion of issuers as to which accounting method applies.

Thank you.

MR. HEWITT: Thank you, Lisa.

Brad?

MR. HUNKLER: Yes, thank you.

I come today from the perspective of a well-capitalized, stable, life insurance company. I also try to bring forward the perspective of the life insurance industry, which I have obtained through my role as chair to the GAAP accounting committee for the American Council of Life Insurers, ACLI.

Fair value has been credited by some as a significant factor in the current credit crisis. It's been cheered by others as an early detection system that will prevent a prolonged downturn in the economy. I think potentially both parties have given more credit than fair value deserves on both accounts. While some might not like the reality of where currently priced, it is a reality and it should be disclosed and understood by investors and regulators.

I am not convinced, though, that fair value should have the impact that it's currently having on income statements, balance sheets and regulatory capital. While I do not support the view that fair value accounting has caused all the problems that we face today, I do believe that the problems we faced today have illuminated some inherent weaknesses in fair value accounting that should be addressed.

FAS 157 is at the epicenter of fair value issues. FAS 157 changed the definition of fair value to exit value. Prior to FAS 157, fair value was used in varying degrees throughout GAAP. It's not certain though that the exist value definition is necessarily the most appropriate measurement basis for all situations where GAAP requires fair value though. I support the use of exit value concept, for example, for equity securities and for debt securities that trade in active markets.

I question the usefulness, though, of exit values for liabilities and assets that trade in inactive markets. I think it's na‹ve to believe that market prices provided by inactive markets provide transparency. Granted it comes from a third party, but it is neither objective nor transparent. Many times, these prices are determined by inefficient markets.  There is a lack of transparency around trade activity and trade volume.

In many cases companies are forced to rely on pricing services that work largely in a black box.  Many times, pricing services used brokers to assist in the pricing.  Brokers are often motivated to reduce prices as much as companies may be motivated to increase them in terms of using a mark to model, so we don't believe that it necessarily represents a more transparent value.

While FAS 157 in a recently issued interpretation attempted to clarify that a departure from market prices driven by distress sales is permitted.  It falls short of overcoming the exit value premise of FAS 157, thereby resulting in very  little change in practice.  For this reason, we believe that the standard needs to be revised, not interpreted.  We also believe that a thorough review of the standards of required fair value should be reviewed and that review would lead to the logical conclusion that FAS 115 needs to be examined as well.

We believe that there's an opportunity to align FAS 115 with some of the provisions of IS 39.  Given the recent change in reclassification permitted by the ISB through IS39, we believe it offers a significant advantage to IFRS filers in the U.S. as compared to GAAP. We believe that it should be looked at in terms of the addition of the loans and receivables category.

Or at a minimum, I think that would be difficult to apply that category within current U.S. GAAP, perhaps loosening some of the tainting restrictions of the held to maturity category and also the adoption of some of the other temporary impairment guidelines and IFRS which we believe to be superior to GAAP. We hope these changes can be made in the short-term with some of the favorable transition options similar to that done by the ISB.

Thank you.

MR. HEWITT: Thank you, Brad.

Patrick?

MR. FINNEGAN: Thank you, Chairman Cox and other Commissioners, Chief Accountant Hewitt and members of the staff, for the opportunity to visit with you today.

I am here representing the CFA institute; and as you know that body is an organization representing roughly 100,000 investment professionals around the globe. In my role as a member and an employee of the CFA Institute, I head the financial reporting policy group, and in that regard had responsibilities for interfacing and working with the standard setting organizations, the FASB, the ISB, and the SEC as well.

I would like to, I guess, make it very clear, unequivocal, what our views are at the CFA Institute with respect to fair value reporting. In case some of you have not been reading the financial press or perhaps some of the letters that we've been writing to Chairman Cox, and that is that simply fair value provides the best measurement of economic reality of at any given reporting date, and I will come back to that. So we are staunchly in favor of the use of fair value reporting as the single, best measurement attribute for financial assets and financial liabilities.

I would like to pick up on some of the recommendations and topics that have been discussed not only by this panel but also by some of the members of the prior panel, and talk a little bit about one item, which I think needs to be given due consideration in this whole debate. And that is the need to let accounting standard setting, the process, proceed unfettered and without political interference.

Without that process, we will not be able to derive and produce reliable financial information for investment decisionmaking purposes. And to allow political interference to continue will just erode investor confidence in the signals and the messages that are published by the standard-setting bodies.

Second, I would encourage the staff of the SEC to continue to work very closely with the FASB and their colleagues as well at the IASB with the accounting profession, with investors, and preparers alike, to continue to develop guidance around two very important areas: one, the exposures that financial institutions have in this place, the depth of them, the nature of them, the extent of them; and two, the valuation techniques that are being used to come up with fair values, in particular the often criticized values of mark to model.

With respect to the issue of pro-cyclicality that Chief Accountant Hewitt has already raised this morning, we believe there's a distinction that needs to be made between information needs of investors and those used to set prudential requirements for capital adequacy and regulatory reporting purposes. We would not argue that fair value has pro-cyclical effects, but they exist in good times and in bad. That, however, does not impair the relevance of fair value for purposes of assessing economic reality at any given point in time.

It is precisely in periods in which managers act with excessive optimism that regulators and risk managers need to ensure that fair value adequately captures elements known as liquidity risk, credit risk, and model risk. But we should not confuse the reporting needs of investors with those of regulators or even boards of directors. Eliminating fair value would create irreparable damage to our fragile system. It would remove critical information in a time where more transparency is needed, not less.

Markets would not suddenly be restored to confidence. One only needs to look at the lessons from the regulatory oversight in Japan during the 1990s to see that artificial rules or measures do not fool the marketplace. Historical costs or hybrids of historical cost and fair value offer less relevance over time. And, it is insensitive to the signals that market prices emit.

MR. HEWITT: thank you, Patrick.

Randy?

MR. FERRELL: Good morning. I am Randy Ferrell, CEO of the Fauquier Bank. We are a $500 million-bank headquartered in Warrenton, Virginia, with eight branches and 145 employees.

I would like to add my thanks to the SEC for holding this roundtable on a topic that is important to bankers of all sizes as well as other industries. I would like to cover three areas: the community bank business model, community bankers' views on fair value, and other than temporary impairment or OTTI.

First, the community bank business model: over 97% of the industry is classified as small businesses; and 41% have fewer than 30 employees. Community banks have been an integral part of their communities for decades, some for more than a century, and we all intend to be there for many more to come. The business model of most community banks is not based on fair value. Instead, our business models are typically traditional, commercial, and retail banking designed to fit the needs of our customers.

There are very few community banks that have derivatives. We gather deposits, we make loans, and our income is primarily based on established interest rate spreads and fee-based income. Community banks are not mark to market jobs. Next, I'd like to cover community bankers' views on fair value.

Community bankers I serve with on the ABA's community bankers council cringe when the topic of fair value is discussed, particularly, when there is discussion about any further efforts to fair value loans and other financial assets and liabilities. Community bankers are very concerned about the complexity of fair value and about moving any further toward fair value for all financial instruments for the following reasons.

Estimating fair values is almost impossible to do with a sufficient level of reliability in a community bank. Few community banks have the necessary accounting expertise. Marking loans to market could dramatically change the products we provide in our communities and could place us at a competitive disadvantage to banks that utilize hedging strategies.

If a fair value model is used for financial instruments making liabilities to market is very difficult, but it is illogical not to fair value them because they are the source of funding for the assets that would be fair value. Fair value creates difficulties in differentiating between how the bank is performing under its traditional business lines and making its business decisions versus how the market would value those assets and liabilities. The market's valuation does not correlate with our business decisions. This makes it difficult to explain their performance to existing and potential shareholders, customers, the media and regulators on an ongoing basis.

Last, the topic of OTTI is probably the biggest concern among community banks as it relates to fair value and its application in the held to maturity and available for sale categories for debt securities. If the fair value of an instrument is less than its book value, then OTTI may exist. If so, the instrument must be written down to fair value. For community banks this process is particularly troublesome for debt securities and pool trust preferred securities that have experienced no credit problems.

That is, if the cash flows are equal to the book values, then how can there be OTTI? Because fair value is the basis for determining if OTTI exists, this can result in marking down assets permanently through earnings that should not be marked down. This makes the real value of assets more judgmental and less transparent.

In conclusion, my suggestions for the next steps are, number one, reconsider any further moves to fair value. The accounting model should be such that a reporting entity can prepare its own financial statements. Number two, as the Commission has already requested, expeditiously examine the accounting guidance for OTTI. And, number three, take a fresh look at the definition of fair value to help reduce complexity in estimating fair values.

I want to thank the Commission for the opportunity to share my views with you and I look forward to our panel discussion.

MR. HEWITT: Well, thank you, Randy, and thank all the panelists.

We are going to move into a new, easy topic: active versus inactive markets, and Wayne will have a couple questions in there.

MR. CARNALL: Thank you very much, Con.

First of all, we can tell that we already have diverse views, and I think that's fantastic. We're asking you questions. If you have differing views and if you want to share your views and question other panelists, please do so. I think this morning, so the earlier session was very informative to all of us in terms of when people had shared different perspectives. So if one of the panelists is expressing a view and you'd like to share a differing view, please do so. We would encourage you.

As Con mentioned, we do have a number of questions that we are going to ask about accounting, and obviously we'll get into a little bit on disclosure. But, actually, before we do that, Chuck, I just wanted to ask actually a follow-up question if I may to one of your points. I want to make sure I understood your observation about the interaction of 141R and FAS 157. Did I understand that you did not complete an acquisition because of the accounting?

MR. MAIMBOURG: That's correct, because of the loans that we would have been purchasing. We would have to fair value, and if we had to mark those loans down, you know, the bank we were acquiring had them on the books at whatever the original, amortized cost was, because they were held to maturity loans. All of a sudden, when we have to fair value them and we look to the market and the way that it's currently being interpreted in a lot of circles is that, you know, you have to look to market sales. Those marks could be as deep as 20 or 30 cents on the dollar that they were worth.

That's a huge amount to make up when you're trying to buy a company and you're having to fund that sort of capital to get into that business, and we just couldn't make it work. The tangible equity ratios were all over the map and it didn't work.

MR. CARNALL: So even though the economics weren't impacted by the accounting, the accounting drove that determination?

MR. MAIMBOURG: Yes, and I hear about it every week from our corporate development director.

MR. CARNALL: Okay. Thank you.

Actually, before we get into whether we have an active or an inactive market, I just wanted to actually ask a question that we were actually going to ask the first panel group, but we didn't have a chance. And, actually, Randy, if I could start with you on this issue and also ask Cindy's perspective, and that's that FAS 157 contains the principle that one could look to as to what a market participant would consider when valuing a financial instrument, not the holder's intent with regards to the financial instrument. And this is actually a point that Brad was talking about a little bit. But should management's intent with regard to investments and financial instruments matter when determining the fair value of the financial instrument?

MR. FERRELL: Wayne, I want to make sure I understand the question. Would you repeat the last part?

MR. CARNALL: Sure, sure. I'm sorry. I'll paraphrase it. What FAS 157 requires is that you look to what a market participant would consider when valuing a financial instrument. And so basically it was looking at what could you sell that instrument today, not whether you would have the intent to let's say hold that for a period of time in determining the fair value. So your management's intent does not impact your ability how you're going to valuate. The question was should that be a factor in determining the fair value of a financial instrument.

MR. FERRELL: Wayne, in my opinion it should. I mean in our business model when we purchase an investment, we look to not only the price that it may sell for today, but the duration, any number of different things in determining how we intend to use that asset over a period of time. So in my opinion, yes, it should.

MR. CARNALL: Okay. Brad, actually, you commented on that originally. I was wondering if you wanted to expand on that.

MR. HUNKLER: Yeah, I think I would. I think there's a difference between a cash flow investor and a trader, total return investor, or a money manager that uses investments for purposes of, you know, holding those assets and trading those assets.

What I would suggest as an insurance company is we use the cash flows off of those assets to immunique our liabilities and the interest credited on those liabilities, and it's the most important element of understanding our financial statements and our financial health is understanding the ability for us to collect those cash flows on an ongoing basis.

I do think and I think to Pat's point I don't want to deny investors information about what type of a loss we would incur in the event we were required to or needed to sell those assets. But I do not believe that that should be the basis for the preparation of our financial statements. I believe that should be disclosed in the footnotes or in the MD&A.

So I do believe there's a difference. I think a trader should be looking more towards current market price. And I think a buy and hold investor should be looking more towards cash flows. I think FAS 115 recognizes that and the different categories. Unfortunately, the restrictions around the held to maturity category is such that someone trying to manage a portfolio to provide a reasonable return for investors can't do that within the trading restrictions of the held to maturity category in FAS 115. Thereby, we see it used very rarely in the insurance industry, even though turnover rates and portfolios could be 10 to 15 percent.

MR. CARNALL: Okay. Cindy?

MS. MA: I think the answer actually depends on where is the source of your market price, because the sources of the stress market price, then one would have to think about what does the management intend. Because if the management basically has no capital to really light all resources to hold the instrument, then they should actually market to that distress price, because that is a price they would be able to raise the needed capital and cash.

But if the price that we are talking is that you come out from a level 3 model and then the level 3 model basically should capture the market illiquidity due to volume restrictions, but it should not have like capture what I call earlier, illiquidity funding discount. Then that price will not have to be adjusted for the management intent.

And, also, it's based on the current interpretation of the FAS 157. We are doing valuation based on what market participants will be doing, not like in the individual company, unless it gets to the level 3 situation. But we do look into the management intent when we get down to considering the OTTI issue.

MR. HEWITT: Thank you.

Yes, Richard?

MR. RAMSDEN: I mean, to just echo one comment that was made and just a second one, the first is that I think it's debatable that intent as a concept is sufficient to base an accounting policy on, which I think we've heard. But the second is in an environment that's incredibly uncertain and volatile, such as the current one. I think intent can change and I do think that that can be to a lot of confusion and a lack of comparability between financial statements given that you are likely to see changes in intent given how rapidly the values of securities are changing.

MR. HEWITT: Russ?

MR. WIEMAN: I was just going to add one thing, and Richard kind of said it. I think we often times talk about intent by itself, but you also have to look at the ability and you can't have one without the other.

MR. HEWITT: Patrick?

MR. FINNEGAN: Wayne, I guess it probably doesn't come as any surprise to you to know that investors as a whole are not in favor of accounting by management intent for the simple reason is it allows the issue of moral hazard to creep into the preparation of financial statements. Users are interested in understanding how the economic activities in which the businesses are engaged flow through and affect the reported accounts, and they're not interested in how management might be able to adjust economic activities to paint a picture that they think is more representative of their performance as opposed to what actually occurred. So management intent, in fact, I think is an insidious idea in financial reporting and our view, you know, at least from the

CFA Institute's perspective, is that we should let all changes and net assets occur as they occur in the balance sheet and in the income statement.

MR. HEWITT: Any other observations on that point?

MR. MAIMBOURG: And I think you have to include management intent. I mean, management is running the company and they certainly have opinions, and they're the ones that are in the best position to do that. I don't think you can just totally ignore it, because if we didn't include management intent we wouldn't need management. We could just put everything on audit pilot and act like we're going to sell everything tomorrow. And that's just not the case.

You know, there are loans that banks hold and intend to hold, and that's the reason we make the loan is because we want to hold it and make the money off of it. And the fact that the market will only pay us 20 cents because the market's down is not I don't believe is a reason to mark it down to 20 cents on the dollar.

MR. HEWITT: Cindy?

MS. MA: Yeah, I just want to add one more comment. I think the reason we're having this debate is due to the fact that we have active rules in active markets. We are in a really liquid, active market, would not be debating. Yes, we mark everything to market, and given the fact we are in the current situation, and then there are different liquidity among different asset classes and, therefore, I think we need to like give some guidance to specific asset classes who are like particularly frozen and/or liquid. And rather than try to come out with rules that generalize and apply to our asset class.

MR. CARNALL: Actually, Cindy, that's a great segue into my next question, and that's about active and inactive markets. And the question is should fair value be limited to situations where there's an active market. If there's not active market, should companies be allowed to base their fair value estimate completely on an internal model.

MS. MA: A question, please.

MR. CARNALL: Yes.

MS. MA: I actually believe that FAS 157 provides a lot of guidance from that standpoint. In an active market, you basically can get the transaction prices from level 1. And then in an inactive market, it basically is you market to model. And I actually would like to give some justice back to the term mark to model, because I was sitting in the audience this morning. I heard a lot of criticism saying mark to model, mark to moosh, mark to something else, but indirectly then the panelists also said, oh, well, we actually had to do fair value. Now, how do you do fair value? And the panelists said, well, we look at the cash flows. We look at the discount rate. We look at the wrong factors. But, in fact, those factors won't sit on the desk and stare at you, right? You have to build a model and put it into the computer.

Remember, when we talk about mark to model, it's I think the market has the wrong conception to think that this is a black box. It seems like an ET coming up from outer space, but that's absolutely not true, okay. Most of the models that we use are really fundamental economic models and I know a lot of people are talking about it's so difficult to really value the mortgage backed securities, some of the complex instruments. But at the end of the day -- we are trained as economists -- we do look at cash flows.

And, therefore, we look at factors that like what factor cash flows and the expected default rate, delinquency rate, recovery rate. All of those are economic factors that go into the model. And then we'll determine what will be the appropriate discount rate to come out with a value. Yes, it may not be the value that people will be like readily buy and sell. But it is a value coming out from a fundamental, economic model.

That's why I was sitting in the audience kind of saying, actually, that's no conflict. On the one hand, people support fair value. They actually just say fair value coming from an economic model. And on the other hand, they keep attacking a level 3 methodology, mark to model, and that's why I say it's just actually more due to like people actually do not fully understand all these terms. And I think if there's more guidance, more examples, provide the people to try to reconcile this misconception, I believe it will reduce a lot of the debated issues.

MR. CARNALL: Yes, first Richard.

MR. RAMSDEN: Just a couple of comments. The first is I do think investors would be somewhat sympathetic to the idea of disaggregating where the losses have come from. How much of it has come from true credit events and how much of it has come from liquidity. And, I guess thirdly, how much of it has come just due to a higher rate of required return for investors to buy that security today compared to a year ago.

My concern, however, is it's extremely difficult in my mind to single out how much of the decline in value is because of liquidity, and how much of it is because of credit. And I'll give you an example. A year ago, if we looked at say the CMBX index, which is an index of commercial real estate related assets, we would have estimated that the market was building in aggregate losses of around 800 basis points. Now, that would compare to our estimate of around 500 basis points, so we would attribute that gap to liquidity. However, the recent data that's coming out suggests in actual fact that the credit market was just frankly more accurate at foreseeing what we think the ultimate peak losses will be in that asset class.

So, I do think if there is going to be a move to disaggregating losses between liquidity and credit it needs to be very, very clearly defined. And I think it needs to be very carefully disclosed. Otherwise, I do think it would lead to additional confusion and a lack of comparability between institutions, who clearly will have a different view on where the losses ultimately are going to be.

MR. CARNALL: Actually, before I get to you, Lisa, let's go back to Cindy as a valuation expert. \

Do you think that distinction can be made and would you be comfortable if a company actually disclosed that distinction and financial statements?

MS. MA: I think from their standpoint it makes sense, but I will be scared to do the implementation. And I would be very sympathetic to the auditors if they had to review that, because you basically, totally control with the early panelists. It's because to try to make that artificial segregation, guess what? You're not going to get market prices. Nobody is going to say go and get a market quote for liquidity. Go and get a market quote for credit and then separate it. Then what happened?

You begin you build a model to it; and therefore, when you build a model, I'll be honest with you. It could be subject to manipulation. It's just like statistics. It can be manipulated and it will be created auditing nightmare. Therefore, I was a little bit surprised that it was a recommendation from an accounting firm. I would actually think it would be very difficult to do, but if guidance set out that we have to do it and therefore there's nothing that we cannot construct, therefore we will build a model and try to like do our best job to allocate the two parts. But, I would not recommend that.

MR. CARNALL: Okay. Cindy, I have a related question to your model, inactive market for giving the auditors that would have to audit the model and so forth.

How would you describe this model to investors so they could understand it in a footnote? How would you describe the model?

MS. MA: Oh, okay.

MR. CARNALL: Would you use the assumptions that you used into the model, less those? I mean, how would the investor understand how this model is being used?

MS. MA: Essentially, I think people, as I said, it's some kind of scare. When people think model, they think it's very complex, and model is actually really not that complex. It's just like little puzzles, because right now the sector is really frozen, the debt market, the fixed income market. So that in part the fixed income market is frozen, when you think about fixed income, it's like the thing has any assets we are dealing with. It's what is a cash flow, and therefore we have to explain what the model is. First, we have to explain what is the economics behind that instrument, okay?

And what kind of expected return and expected risk related to instrument, that's our first part. And the second part is we will have to try to explain what will be the factors driving the cash flows. And those are the things that need to go into the valuation. I give you a good example will be we are totally aware of the fact that the auction rate securities is a frozen market, totally frozen, okay? And we have a lot of clients coming to us and say, we're holding a couple hundred million dollars of student loans, auction rate securities. How do you value this?

And further, they said there is a secondary trading, and marking at 70%. Should we market that? And I said, well, let's don't talk about that first. We'll consider that's a data point, but what we should do is look at how we build a fundamental model to address that issue. And first is as we look at this student loans are auction rate securities. And, take the best one, okay? Most of them are actually backed by federal government. And your client again says, well, they're backed by federal government, and t-bill is backed by federal government.

And how come mine is frozen, and how come mine is not a par value? And because there's no credit risk, my answer to them is that means there are other factors driving that value, because if there is no credit risk, you're right. They should be a par value, and the fact that the auction failed, they are not at par value. There are other factors. The other factor is because there is an illiquidity premium at the moment the market that's not one to touch this type of asset.

The investor reveals a preference that they don't want that asset for whatever reason, and then in our valuation we will have to capture that illiquidity. But going back to the question, the model will be, say, okay. This is a fixed income instrument. What will be the driving factors for the instrument? What is the expected coupon rate? When is the auction rate security failed? You need to review the offering memorandum. It would tell you what penalty rate the investor would get as long as the auction is failed. That is a key factor for valuation. You have to disclose that.

And then the second part you would have to look into is well, the offering memorandum says that the statement is 20 years, but am I going to really value this instrument in 20 years? Not necessarily, because you really have to go back to look into the structure of the instrument. And, given the fact that most of the issue already, like doing redemption, and with the attorney general looking at the student loan market, therefore expected time going back to par value will be a lot shorter than 20 years.  It may be four years.  It may be five years.

Those are the factors that we have to take into consideration.  And then the next factor will be what would be the correct adjusted discount rate.  And then you would have to factor into the credit quality illiquidity premium and a lot of other factors.  Therefore, all those kind of things, if I would be doing the footnote disclosure explaining the model and all that will go into that footnote. And, therefore, when we do reports for our clients, actually the report will clearly lay out the methodology, the assumptions.

And then because 157 says assumptions are not management assumptions, that you basically should use market participants' assumptions, and therefore we will be going out to look into like what type of research was being published by different financial institutions, and what kind of data they use.  This is what we come out with the assumptions.

I know I took too long, but it just got a little bit carried away.  Sorry about that.

(Laughter.)

MR. CARNALL:  No, thank you very much, Cindy.

Lisa, I'm not sure if you had an observation before, then we'll get to Brad. So let's go down the line until everybody's covered. Lisa?

MS. LINDSLEY: Okay. As a user of financial statements, I just wanted to make two observations. One is that we really could use additional disclosure regarding the models that are used in the case of mark to model. For example, in our discussions with a couple of the banks at the epicenter of the subprime meltdown we found out that senior management was not using the Case Shiller housing price index, which is adjusted for inflation. Rather, they were using a nominal housing price index that did not reflect the historical asset price bubbles in real estate.

And one other suggestion is which was commented on in the last panel is the need to provide further guidance on when a market is sufficiently illiquid, such that level 2 inputs are not indicative of fair value and issuers moved to level 3. It has been suggested that the FASB could use indicators such as the bid-ask spread and relative to normal levels. As was mentioned in the last panel, the September 30 joint release between the SEC and FASB relied, we think, too much on the word "judgment."

MR. CARNALL: Brad?

MR. HUNKLER: Thank you. You know, Cindy talked about kind of the negative connotation and the negative image of mark to model, and I think that that's largely fueled out of a concern around management bias and the introduction of management bias into that model. And I think when you talk to the investor community and you talk to the auditing community, I think it's important that they have professional skepticism in what they do and challenge management and management's assumptions.

And they need to be given the tools to do that, and that's what I think a big part of the footnote disclosure should provide them. But I think in setting accounting standards, when we come here to talk about setting the standards, I think there needs to be a presumption of management integrity in how financial statements are set in auditor capabilities. And you don't always talk about that, but when we're here today and we talk about the use of mark to models, we shouldn't allow a fear that management is going to introduce bias and introduce techniques to delay the recognition of losses into that. We should base it off the conceptual approach and I think auditor bias gets us back into FAS 157.

I think, you know, Tom representing the FASB is here. And I think the FASB is kind of scratching their head saying for all these people who want to throw 157 under the bus where were you for the multiple years, two, three years, we debated FASB statement 157 and the extensive due process around the issuance of that standard. And I was one of the folks drafting comment letters on FAS 157, largely supportive.

I think the issue is we largely read FAS 157 as many people talk about it in here today is providing the flexibility necessary to accommodate the situations that we have today. The reality though is that through interpretation, and this has emerged subsequent to the issuance of the statement, that the exit value bias, and maybe to a certain extent the auditor bias to use independent information as opposed to management information, has not allowed companies the flexibility that I believe 157 was originally intended to provide to move away from distress sale markets.

I talked to a couple of dealers prior to coming here to talk to them a little bit about the non-agency, mortgage-backed, security market. And these are large dealers that represent large insurance companies and banks. And, I say, do you see any transactions in this market that you would not qualify as forced sale transactions. And they answer is, very, very few, almost none. Banks are not selling; insurance companies are not selling into this market. The reason: they're basically on the sidelines; the folks that are selling are money managers, hedge funds, folks that are forced to delever, or folks that are forced to sell in order to fund liquidations, distributions out of funds. Those are the sellers in this market.

That is not a functional market. And so it doesn't mean it shouldn't be disclosed and understood, because it is a reality, and people need to understand it. If we are forced to sell these assets, we will incur a loss, but on a proponent of providing an economic value in the financial statements and disclosing the fact that if these securities were sold, they would be sold for a value less than the economic value and providing some parameters and some sensitivity analysis around what values those would be. I think that's a footnote. I don't think that's the basis for the financial statements.

Thank you:

MR. CARNALL: Any other observations on that point? Chuck?

MR. MAIMBOURG: One quick point. I was going to echo what Brad said in terms of I think a lot of this has gotten into a debate. We keep talking about 157, and I think the fact of the matter is that 157 is sort of behind us, because as Cindy said, a lot of times we have to go back and reread it. Because if you read the definition of fair value on 157, it talks about an inorderly transaction with market participants. Well, I think the problem is we have been swept down this interpretive path that basically has taken us to a definition that says, you know, go out into the market and find the lowest possible price you can find in market to that.

And that was not the purpose of 157. So I think a lot of that has happened, and I do have to report back that at least from my observations, and I've talked to several of the banks that are larger than us, their controllers and accounting policy folks, and I know within our bank and I've talked to our auditor the 157-3 guidance and FSP, and the guidance from the SEC really had no impact whatsoever on any of the interpretations related to 157 in a way that it's applied currently. So that's based on my informal surveying of some of the other banks.

MR. CARNALL: Russ?

MR. WIEMAN: I don't want to sound defensive, but I think the auditor committee needs to stand up here a bit. I think one thing, when we talk about auditor bias relative to third parties, I don't know if that's auditor bias. But that's the standard and typically over time that's been our best source of information. As it relates to the guidance that's come out, while I would say perhaps that if someone had an expectation that it was going to be a landslide change in terms of what people were going to go to, it was not that. But I believe it was extremely helpful guidance, and it all gets down to the words "judgment," in terms of what you use.

We've used judgment a lot. Cypher talked about judgment, and that's something that someone needs to look at in terms of what characteristics you use when you're doing judgment. But I think if there was a bias, I think maybe we did get swept down a path, perhaps. I don't think it was necessarily the lowest, but it's like a market value, and that's from an audit perspective. That's preferable than anything else, and I think the guidance that's come out is certainly that our firm has made us think about a lot of different things. You may not get a different answer, but it's made us think about different things.

MR. CARNALL: Actually, if we could move on to the next item, and again I just want to indicate to everybody we'll have a short minute at the very end to make closing remarks, but if we could just go to changing from accounting to disclosure, I'll ask a fairly simple question. I'll direct it to the financial analyst for Patrick and Richard.

How could disclosures related to fair values be improved from an investors perspective? In other words, what information could they be receiving that they're not currently receiving? Are there changes to FAS 157 that could be made that could improve disclosure? Are there items that we should require through the MD&A that would help people understand more about fair values.

We have issued to dear CFO letters. That's what we refer to them as, that we have placed on our web-site back in March and then September to try to encourage and maybe make recommendations about disclosures in the MD&A. And I was wondering from your perspective are there other items that you think should be disclosed that are not currently be disclosed. Are there ways that we can improve that communication to investors?

MR. RAMSDEN: A couple of things I would say, the first is I do think some attempt to try and disaggregate where the losses are coming from would be quite helpful. And I fully accept that there is a judgment component to it, but to try and understand a little bit better what type of loss expectations management is using in valuing some illiquid instruments, what type of return assumptions they're using and also just the basics of what the underlying cash flow assumptions are where there is no market prices.

You know, the second is I do think the investment community would pay some attention to management saying, look. This is what we think the economic value of this instrument is, and this is what the mark to market value is. And this is what we would attribute to the liquidity discount. I do think that that would be helpful in particular if there could be quite clear guidance given on how we calculate those.

I think on the modeling issue it is complicated;

and, again, I do think that the analyst community is always going to rely quite heavily on the auditors as well as on the management to ensure that the inputs that are going into those models are reasonable. Having said that I do think that critical assumptions in particular about forecast house price declines for some of the mortgage-based securities, again, would be very helpful. So those are the things I would say would be useful.

MR. FINNEGAN: Wayne, thank you. I guess I was picking up along the lines of the question that Con had raised. And I think your question ties right into it.

We, the CFA Institute has offered comments to the FASB, on 157 in connection with its development of the FSP 1573, and we echoed in that comment letter the suggestions that you developed here at the SEC, their CFO letters that were developed in March and in September.

In addition, we also think a lot of the disclosure examples and suggestions developed by the ISB's expert advisory panel would go a long way as well to enhancing the understanding of users or investors' use of mark to model techniques. There is absolutely no question. I think that investors need to understand the assumptions, the inputs in these models; and, they also have to have an appreciation of the range of outcomes that can be derived from these models.

But, I think one of the things that doesn't come through loud and clear when a user puts up a set of financial statements is the fragility, if you will, of the numbers that these models produce, and that's where management has the opportunity to tell the story the way it really is, and to explain that fragility. So, to Cindy's point around understanding the assumptions with respect to which housing price index you're using, absolutely that has to be discussed. But I think the notes also have to provide some sense as to how the models are being used from a risk management perspective and the fragility of the outcomes from these models. Otherwise, the users cannot take away any degree of confidence around the numbers.

MR. CARNALL: Any other observations or anybody want to add anything in terms of the disclosures? Tom?

MR.LINSMEIER: I did want to make a point that the FASB will be making an agenda decision in the very short term about what potential disclosures we could add to the package that's required to facilitate the use of fair values in these markets; and, of course, we will do every effort to coordinate our response with the ISB so that we have identical sorts of disclosure rules. But this is a very pertinent question and something that I wanted to make sure everyone knew is on the radar screen for us.

MR. RAMSDEN: One thing I would add as just taking on board that earlier comment I think some type of sensitivity analysis about how values change as you change key input assumptions is critical. Because I do think investors recognize that no one has the right answer about where some of the key assumptions are going to go both in terms of house prices and loss assumptions. But I do think a sensitivity analysis would help highlight some of the fragility issues. But I think it will also help just size. What is the impact if one of those key assumptions is wrong?

MR. CARNALL: Richard, that's actually an interesting observation. In our March 'Dear CFO' letter we did actually encourage that type of disclosure that companies do provide sensitivity analysis, close ranges of differing values. And one of the reasons that we hard that we heard that companies were not providing that information was one is the fear of being called the litigation fear. The fear of actually being wrong, and then someone second guessing that if you recorded it in 50 and you disclosed a range of let's say 30 to 60, why didn't you record it at 30.

And I just was wondering. I've just got the perspective of perhaps the preparers and the auditors. If there was a safe harbor protection on that disclosure. If you had that in terms of like the market risk disclosure information that we currently require, there is a safe harbor protection. I was wondering if that would encourage more companies to provide that disclosure in, let's say, their

MD&A.

I guess, Chuck, if I could ask you that from your perspective?

MR. MAIMBOURG: I'm happy to say we don't have any subprime loans, so this has not been a big issue for us. I mean, there is sensitivity analysis that's provided in other areas. We provide that related to servicing assets and also a securitization assets. So it's not uncalled for in the accounting guidance, but I do understand the litigation issue.

Because I think the earlier comment, I think that's part of what's driving these interpretive guidance issues that we have with 157 now is sort of the fear of litigation, because you know if anybody makes the wrong decision they're going to pay for it.

MR. CARNALL: Randy, I was wondering if you have any perspective. Do you think people would disclose more if they could be protected from that risk or at least minimized?

MR. FERRELL: Well, first I'd like to add that we don't have any subprime loan exposure either, and to be perfectly honest, that question could better be answered by my CFO.

MR. CARNALL: Fair enough, thank you.

Any other questions or observations on that?

MR. FINNEGAN: Wayne, I would just say that anytime you encourage but do not require disclosure, you're generally going to get it. I think Tom knows that very well.

MR. CARNALL: You know, actually, that's an interesting observation; and, one of the things that we are very anxiously waiting for is the Qs that for the quarter just ended will be due in the next 10 days, or so. Because you know we issued the September letter right at the very end of September or certainly in time for people to consider for their 10Qs, and it was more of an encouraging. Obviously, the rules do require certain information, but we are actually very anxiously looking forward to seeing what companies did do in response to that letter.

CHAIRMAN COX: Well, if I might just jump in on that point, I mean, people are rather rapidly going past the 'Dear CFO' letter that the SEC sent out. How is it that for some institutions there can be such passion about how wrong the numbers are that mark to market forces them to use and yet such comfort that discussing that with investors is not material?

MR. HUNKLER: I think there is a little bit of a practicability issue in the availability of the data within the timeframe necessary to get it done and the disclosure burden that exists today is sufficient. I think also the litigation considerations are certainly part of the landscape that prevents companies from disclosure beyond what's required. I do think that companies have some of these conversations with credit analysts and others to go into some of these topics but are reluctant to put it in regulatory filings.

MR. FINNEGAN: Chairman Cox, I would add that I think this whole illiquidity situation that we've seen around these very complex financial instruments has underscored the fact that the risk management systems of many of these organizations have not allowed them to provide the kind of disclosures that really investors are looking for. I think there's been a whole breakdown in the governance, frankly, of financial institutions. They weren't prepared to make these kinds of disclosures. They didn't have the system in place to make these kinds of disclosures. They were relying too much on other market makers, brokers, and other services for the valuation of any securities.

MR. HEWITT: Thank you. We'll move on to our last question. We are running out of time, unfortunately, and this question really revolves around the application of fair value standards, and I am going to ask Lisa the question and two or three others involved in this particular item.

Now, some have questioned whether fair value measurement guidance has been applied consistently in the current conditions. Are you concerned about the amount of diversity that exists related to estimating fair value for instruments that do not trade actively. That's the first question. The second related question is, if so, what steps do you think should be taken to minimize this diversity.

Lisa, do you want to kick it off?

MS. LINDSLEY: Thanks. I think I answered this a bit in my earlier comment. Yes, I am concerned about the diversity and I'm concerned about the discretion that's given to management in terms of which method to apply. And I think that we would like to see more direction be given in terms of when to move to mark to model, how management determines that a market is illiquid.

MR. HEWITT: Any others have comments on diversity? Does it bother you that one financial institution uses a different method than another?

MR. HUNKLER: My comment on that would be I think one of the issues is not so much diversity and practice around similar valuation approaches, but diversity and how different instruments are accounted for under U.S. GAAP. For example, you know, we are an investor in CMBS, commercial mortgage-backed securities. We also invest directly in whole commercial loans that we hold on our balance sheet.

You know, one of them is fair valued through the income statement or through the balance sheet with some fairly punitive marks right now in the CMBS market. The other is carried at cost and, you know, you put loss reserves up to the extent that you view a concern with the collectibility cash flows. You see the situation emerge across a lot of financial institutions where very similar assets are receiving significantly different treatment under the current accounting standards. You're going to guess I'm not an advocate of fair value and direct whole loans, but rather changing valuation and impairment criteria for securities backed by comparable collateral.

MR. HEWITT: Yes, Chuck?

MR. MAIMBOURG: I think there's definitely diversity, and I think a lot of it depends. You know, going back to some of the things we've talked about, which is different management teams at different places. They have different judgments and interpretations. They have different auditors who have different interpretations. Companies have different interactions with the SEC as to where they're at with how often they get reviewed and those sorts of things, so there's a lot of variables that come into play here.

And, I'm always interested, as I sort of think about this, is we try to move to principles-based accounting, because I just continue to sit back and scratch my head as to how we're going to allow everybody to use their judgment, but everybody sort of come to a consensus that everybody likes. I think it's going to continue to be a challenge going forward?

MR. HEWITT: Any other comments and observers? I know that Chairman Cox and Tom. Go ahead Tom.

MR. LINSMEIER: It's a slippery slope to think about providing guidance for specific financial instruments when there are so great variation in those instruments. It is absolutely a common belief that one of the worst things the FASB ever did was build 800 pages of derivatives hedging accounting guidance that caused rules and specific guidance for the various different types of instruments, hedging transactions and relationships.

Once we start going down that slope in terms of financial instruments and valuation, we could very easily get to the same sort of massive rules and guidance that we have in 133 as we would in 157. And that was the intent of the FASB to try to avoid that when putting together a valuation resource group to be able to identify circumstances where we thought there was enough variation and practice that we ought to augment the guidance to deal with significant variation, but allow the necessary judgment because of the diversity in financial instruments to allow some variation within bounds, within the standard. And so it's a real slippery slope if we get too far. We could very easily get to 800 pages, and I don't think that's the right answer.

MR. HEWITT: Okay. I think I'll allow one more.

Cindy?

MS. MA: Just along that line is the same thing in the valuation community. I mean if you look across different valuation firms, we may not be using the same methodology in terms of valuing the same type of assets. And, therefore, the burden actually rests upon the auditors, and you are hoping that the auditors actually have like a national framework to review those valuation models to make sure the methodology, assumptions, and approach are consistent. And, therefore, I think another way to put this, besides putting the burden of FASB on the uses, may be also the valuation community needs to take certain steps to try to come up with more standardized approaches or models and a standard way to derive assumptions.

MR. HEWITT: Okay, thank you. We are entering the closing arena now. And I know that Chairman Cox and Commissioner Casey have to leave, but I'll ask if there's any observations or questions from any of the commissioners at this time. Then I'll give Chairman Cox that opportunity to give the first closing comments, if you will.

CHAIRMAN COX: Well, in fact, why don't I defer and give the last closing comments, simply because of the burden of my brief remarks will be to thank and congratulate all of you for what you provided, but I'm interested in hearing the last ounce of it.

MR. HEWITT: Randy, we'll let you start with your closing comments.

MR. FERRELL: First, I'd like to say that I feel that I would be remiss if we didn't discuss one section that I hoped we would talk about today, and that's the smaller end of the publicly registered SEC companies.

MR. HEWITT: That was my last question.

MR. FERRELL: Well, I'll be brief, but I'll just say that new changes concern me, because they're going to add expense, expense in terms of personnel, additional expertise, time, which is already tough at reporting time, quarterly and at the end of the year, external audit expense. There are any number of different issues that do concern me about the smaller end of the publicly held companies.

Financial reporting no doubt will be more complicated, will be more subject to judgment, and therefore in my opinion less transparent. It will be much harder to explain to our shareholders, to the press, to the media, to the analysts, and one of the biggest issues in my mind is how do we separate and explain on an ongoing basis our profitability from the traditional banking activities that we do from the mark to market or fair value.

There's no doubt that it will increase earnings volatility, which is something that management will e expected to have to explain to its very constituencies.

Those are just a few of the issues that I think are on the table, and would be from I guess the community banking end of the spectrum. And I think there are about 8,000 of us out there, if I remember correctly.

Thank you.

MR. HEWITT: Thank you, Randy.

Patrick?

MR. FINNEGAN: Well, I'd like to thank the Commission and obviously the staff for the opportunity to visit with you today and share our thoughts. A vigorous debate around fair value, essentially, has been made necessary by virtue of the events in the last year and I think we have to take stock of those events and we have to be mindful of the fact that financial reporting is not at the core or the cause of this, essentially illuminated many of the issues that we're coming to grapple with today.

So as one of my colleagues in the financial reporting world has written recently, "Breaking or tweaking the financial accounting thermometer will not improve the health of the patient. It will only make the doctor's task a bit harder." So I would ask the Commission not to repeal or suspend fair value reporting, but help to improve fair value reporting.

MR. HEWITT: Thank you, Patrick.

Brad?

MR. HUNKLER: Well, again, I would echo my thanks for the invitation to be here to the Commission. I think my closing comments, I would recommend that the Commission take a two-tired or two-staged approach to addressing this issue. The first stage would be to address short-term opportunities to respond to what's happening right now in the market place.

That would include revisiting FAS 157 as much as I hate to admit that it needs to occur. I think that that is the level of change that would need to occur to actually get back to what may have been the original intent of the standard, but to be able to depart from mark to market accounting when it does not provide decision useful information. And then also to adopt some similar provisions of IS39 in the FAS 115 as it relates to other than temporary impairments and the use of the loans and receivables category.

On a longer-term basis though I believe the Commission should look towards, or the second step is to look towards a longer term view of the world. And, in fact, where fair value belongs in the financial accounting framework, I do believe it belongs somewhere. I am not an advocate for eliminating it, but in the current financial statements, I am not sure it belongs in the balance sheet on the income statement. Clearly, this can be addressed in the FASB's financial statement presentation project and there could be a happy home for fair value at that time.

But in the current financial statement framework, I'm not sure I understand exactly the right place for fair value. The way it's being implemented today on a mixed attribute basis doesn't seem to accomplish the objectives of providing meaningful financial information, and so I believe that there's an opportunity to revisit fair value accounting, understand its place in the financial statements, whether it be in the footnotes or in a new place in a new financial statement presentation model.

But understanding that, I think, is going to be critical to how we move forward from this situation. I appreciate the invitation to be here. Thank you.

MR. HEWITT: Thank you, Brad.

Lisa?

MS. LINDSLEY: Thank you. I'd like to also add my thanks to the Commission and the staff for the opportunity to speak today. I think that we recognize that fair value accounting is pro-cyclical, but it's not the root cause of this crisis and the SEC's activities in the future to prevent another crisis of this time can be much more effective in regulating the currently unregulated actors, the intermediaries who didn't perceive or exercise any fiduciary duty unless you have credit markets and other unregulated securities. And we think that the suspension of fair value would not be any kind of cure for an over-leveraged financial system.

We also hope that, you know, in the future we'll get what's really needed, which are strength in corporate governance reforms to ensure shareholders are protected, including proxy access possibly, separation of chairman and CEO in boards, and enabling shareholders to have a voice on executive compensation, which encourages excessive risk taking.

Thank you.

MR. HEWITT: Thank you, Lisa.

Cindy?

MS. MA: I think we want to keep fair value standards as they are, but use your additional guidance and increase disclosure requirements. But we know that as coming from FASB, and then use your guidance to address market illiquidity to make it clear the intent and the principles behind the standard, so a judgment call can be made more easily. And the last one will be issue more guidance to address how to judge whether a market is active or inactive with specific sample sites especially in certain asset classes that are literally frozen at the moment. And at the end, thank you for giving me this opportunity. Thanks.

MR. HEWITT: Thank you, Cindy.

Chuck?

MR. MAIMBOURG: Thank you for the opportunity to be with you this morning, and early afternoon, I guess, we're into now. I appreciate being able to share my views. I don't think we can put the fair value genie back in the bottle, so I think we're going to have fair value going forward.

What I would ask the Commission as they put together the study is to think about some of the economic impacts that are occurring as a result of fair value. I'm a firm believer in that. I think I highlighted one earlier in my comments, but it is having an impact. And I don't think we've seen the full impact of that yet, because I think we'll see that after 141 R officially comes into play and people are having the fair value things that really they have no intent to sell. So why should they be asked to mark to a price where they have no intention of selling. Because again going back to one of Randy's earlier, or someone on the previous panel said, you know, we're talking about a going concern.

We're not talking about an acquisition where we're going to sell off everything tomorrow. We're going to buy the business. We're going to run the business. We're going to add it to our existing business, so I'd ask that you'd consider that going forward.

Thanks again.

MR. HEWITT: Thank you, Chuck.

Richard?

MR. RAMSDEN: Thank you. Three points I would make, and the first, and it has come up several times, I think, cause and effect is critical. And, again, I don't think that mark to market accounting has been the cause. I actually seeing that as being loans that were granted or securities that bought that ultimately lost value.

I think the second point, again, which I think is extremely important is to try and desegregate really how much of the problem is mark to market and how much of it is credit related. Because I do think what the data will show is that the majority of losses that financial institutions have incurred, are actually a direct result of credit issues. Clearly, there are some mark to market losses, but I don't think it's the majority of them.

And then the third point which I think is extremely important to think about to try and reduce the cyclicality of the industry is to really think about reserve requirements and how reserve requirements are sat when the economy is in good shape and how banks have been forced both to provide for loans as well as build reserves during this current crisis.

I do think there's a very strong argument to be made about coming up with counter-cyclical reserving requirements. And I think that would actually have a bigger impact on insuring stability, at least of availability of credit over the cycle than changing the accounting rules.

MR. HEWITT: Thank you, Richard.

Russ? You're last.

MR. WIEMAN: Well, as the last person here I'll try to make my comments brief. I think certainly suspension of fair value accounting, I think, would be inappropriate at this point in time, as I think many people have said. One of the things that was encouraging to me about being here, both for the first panel and this panel, is that there might actually be hope, because I don't think the proponents and the opponents are as far apart as I thought perhaps they were as we started today.

So I think there is some common ground. I think that we all realize that it's not perfect. We might need some more guidance. I think also FAS 157 is misunderstood by a lot of people in terms of how it fits into this whole process; and, everybody wants easy answers and easy guidance so we all know exactly what bucket to put things in. And I guess I would say I don't think that's possible, because we're not dealing with an easy situation.

So there aren't many bright lines here, and all the guidance that's come out so far has been judgment. And I think that's what we have to look towards, and I think we keep talking about the fact and a lot of comments today that we have to have a bias so that there is no bias from management. Well, we're talking about financial instruments, but management has a bias review on the valuation of every asset on the balance sheet, so this is really no different, just a bit more complicated.

MR. HEWITT: Thank you, Russ. Well, we've had an outstanding, informative roundtable today, and some special thanks to the Commissioners, to the observers, to the panelists, to my fellow moderator Wayne, and to my OCA staff who put the roundtable together and also to the audience for all of you who are paying attention to a very important subject called "fair value."

The roundtable is adjourned. Thank you very much.

CHAIRMAN COX: Well, not quite. It's almost adjourned.

(Laughter.)

CHAIRMAN COX: I just want to first of all thank Con and Wayne, because if I didn't speak, there would be no one to thank you for the outstanding job that you've done moderating.

I want to thank our observers who have been here for the entire time. We are looking very, very closely to coordinating with you and value very much that partnership. And I want to thank our second panel. You've done an exceptional job of laying bare some of the very difficult issues that we're challenged with.

On the second day of the new year we will report to the Congress the results of this three-month study that will include in significant part the input that you provided today and the comments that you provided in writing; and, then, undoubtedly some of you will provide between now and the end of the year.

As has been pointed out a few times during these proceedings today it is possible and indeed encouraged for anyone who is interested to submit comments to the SEC's website. The closing date Con or Wayne on the comments John mentioned this morning, it is some time in the third week or so of November.

MR. HEWITT: Yeah, there's an opening comment period on our fair value study. I believe it ends in about two weeks. It's on our website.

MR. CARNALL: November 13.

CHAIRMAN COX: November 13, so it's right in the middle of the month.

MR. HEWITT: That's in about two weeks.

CHAIRMAN COX: It is very easy to submit comments on the web and we encourage you to do so.

Our next roundtable will be on November 21st. I know many of you will be here with us then as well, and so we look forward to seeing you and until then, we are indeed adjourned.

(Whereupon, at 1:06 p.m., the meeting was concluded.)

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