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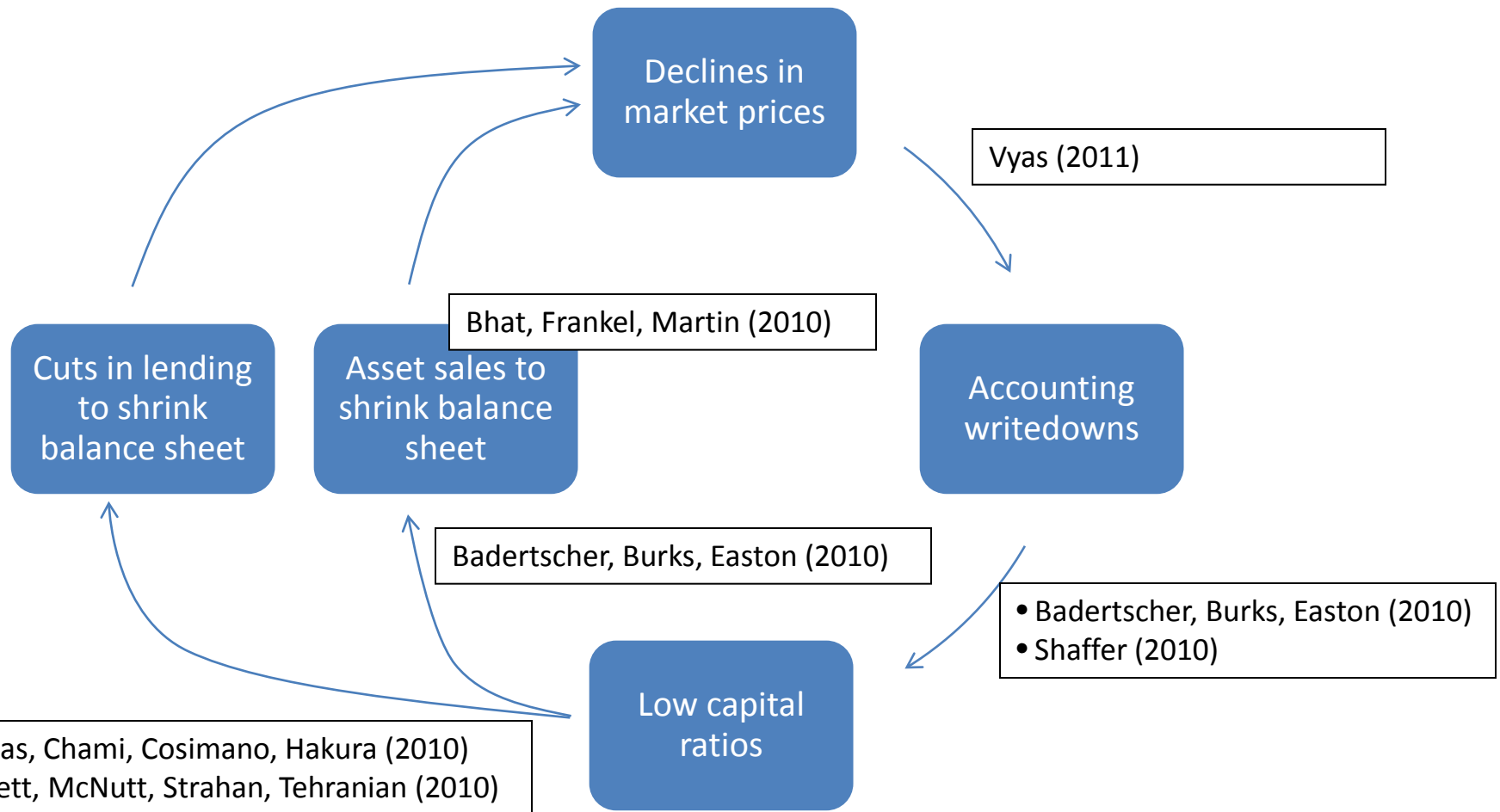
Mendoza College of Business

**Remarks on
Fair Value Accounting and Cyclicity
Involving Commercial Banks**

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Fair Value Accounting and Cyclicity



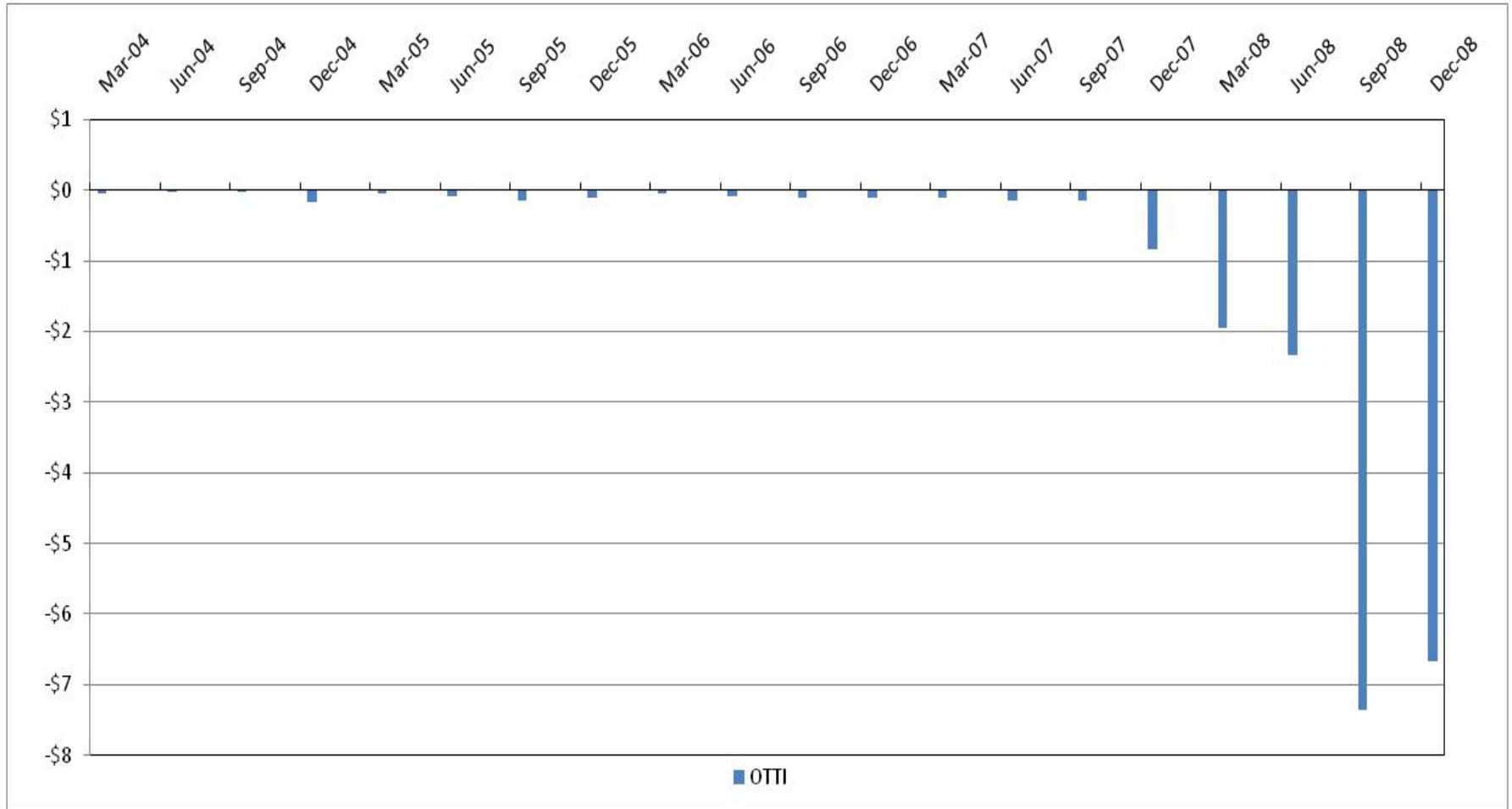
Fair Value Writedowns → Regulatory Capital

For most assets, fair value accounting has little effect on regulatory capital

- Loans held for investment
 - Largest bank asset
 - Not marked to market
- Available-for-sale and held-to-maturity securities
 - Second largest bank asset
 - Marking debt securities to market has no effect on regulatory capital unless decline is deemed **“other than temporary”**
- Trading securities
 - Marking to market affects regulatory capital
 - Not controversial because intent is to sell in near term, meaning that current market prices are highly relevant

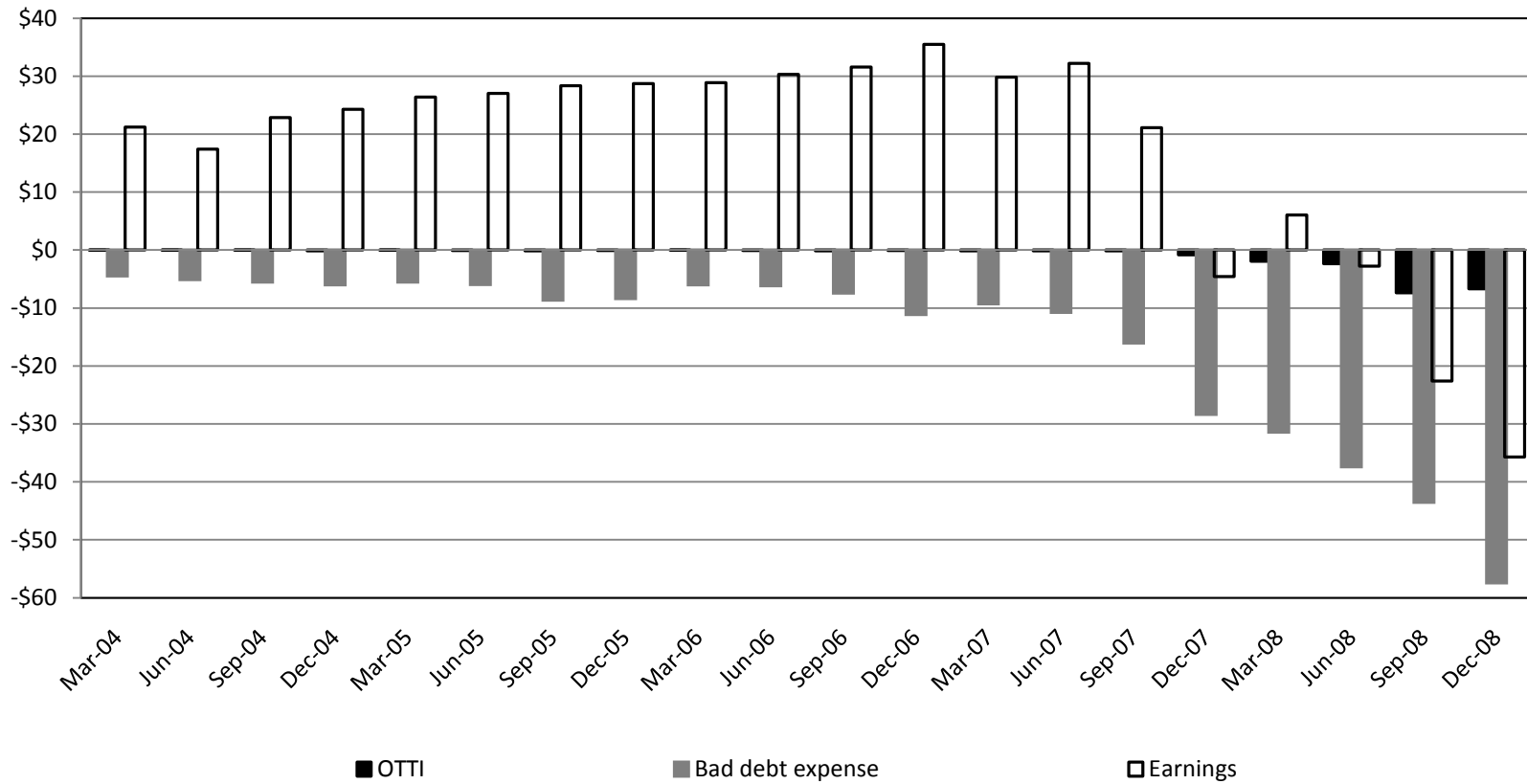
OTTI by Quarter (\$ billions)

Top 100 Banks Ranked by Non-Treasury AFS and HTM Holdings

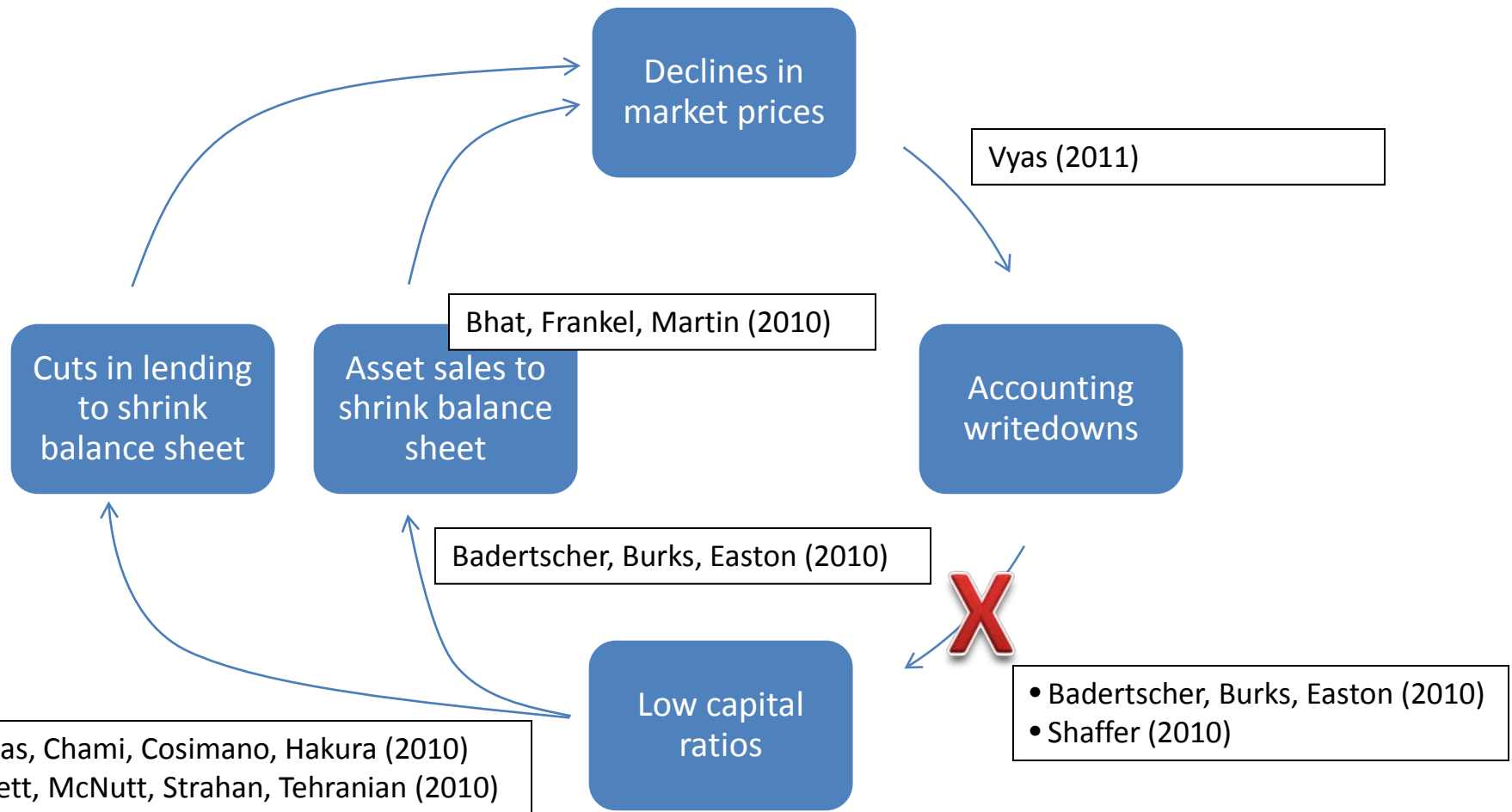


OTTI, BDE, and Earnings by Quarter (\$ billions)

Top 100 Banks Ranked by Non-Treasury AFS and HTM Holdings



Fair Value Accounting and Cyclicity



Conclusions

- Fair value accounting did not cause downward spirals in the commercial banking industry
- Mainly because not much fair value accounting was taking place
 - The crisis was not a lab test of pure-form fair value accounting
 - Thus, these studies don't necessarily support an expansion of fair value accounting
 - But the studies do show that the crisis is not a valid reason to curb fair value accounting