



FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, DC 20543

OFFICE OF THE CHAIRMAN

March 2, 1992

Mr. Dennis Beresford
Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856

Dear Mr. Beresford:

As you know, both your organization and the American Institute of Certified Public Accountants have been considering a requirement that financial institutions phase-in market value accounting, beginning with investment securities. Because of heightened attention being directed to this issue, we think it is important to reiterate our concerns.

The FDIC has several concerns regarding market value accounting. First, many assets and liabilities of depository institutions simply cannot readily be marked to market. The function of depository institutions in the intermediation process is, in great part, to develop lending and deposit relationships that organized markets cannot support. Thus, the act of ascribing a "market value" to these relationships and related financial instruments would require making a "guess" as to how a market, if it existed, would determine value.

Further, to adopt market value accounting for only a portion of the balance sheet would distort depository institutions' true financial condition. At a minimum, if certain assets are to be marked to market, a corresponding amount of liabilities also should be subject to the same treatment.

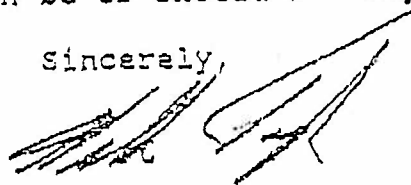
As you know, prior to 1938, banking organizations were required to use market value accounting for their investment securities portfolios. In 1938, the Secretary of the Treasury, at the urging of the President, initiated a series of conferences with representatives of the bank regulatory agencies to review then-existing supervisory policies. One of the concerns that led to these conferences and the subsequent change in the accounting treatment of the investment securities held by banks was that the continued use of market value accounting was thought to be affecting adversely the capacity of banks to carry out the credit intermediation process. Instead of focusing on the ability of

the obligor to repay, banks were forced to concentrate on short-term interest-rate fluctuations, the effect of which normally could be absorbed by banks with few safety and soundness concerns.

Although this letter has reiterated some of our concerns, we would underscore the serious need to enforce existing accounting standards and supervisory policies governing the use of market value accounting by banks. Current policies stipulate that banks carry high-quality securities held for investment at amortized cost. If securities are held in banks' trading accounts, they must be marked to market. If securities are held for sale, they must be carried at the lower of cost or market. Banks that seek to evade these requirements by engaging in excessive trading or sales of investment account securities, should be disciplined accordingly.

In closing, we would stress that many issues need to be examined and debated before market value accounting as it relates to financial institutions can be or should be adopted.

Sincerely,

A handwritten signature in dark ink, appearing to read 'William Taylor', with a large, sweeping flourish extending to the right.

William Taylor