FAIR PRESENTATION---AN ETHICAL PERSPECTIVE ON FAIR VALUE ACCOUNTING PURSUANT TO THE SEC STUDY ON MARK-TO-MARKET ACCOUNTING

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ABSTRACT

Fair value accounting has received a significant amount of blame as the cause of the current financial crisis. Fair value accounting does not cause illiquidity or volatility in financial markets. Banks, rather than accounting, caused the existing crisis, ultimately through bad lending decisions and inadequate risk management. Accounting rules are designed to reveal the full extent of losses and future risks. This transparency would enable banks, regulators, and government to identify specific sources of the crisis and take steps toward recovery and future prevention. Shooting the accounting messenger is not a solution to the problem. Perhaps confusion exists regarding the conflict between transparency and financial stability. Transparency is an objective of accounting standards. Long term stability is best achieved by restoring investor confidence in financial markets and assets. Transparent accounting standards and sound auditing provide support for that confidence. Evidence from the recently released SEC study on mark-to-market accounting supports fair value as the most relevant measurement attribute for financial instruments. Suspension of fair value in favor of alternative cost-based measures would mask losses in value, mislead investors, and diminish investor confidence. From an ethical perspective, accounting has a responsibility to see that financial statements are fairly presented---reflect economic reality. Accountants and auditors are ethical detectives holding businesses to ethical standards of honesty, completeness, neutrality, and representational faithfulness. Accountants and auditors are bound by their professional code of conduct to protect the public interest. So grounded, accounting is the provider of one of the essential checks and balances on commerce.

INTRODUCTION

Recently, there has been considerable media coverage on the subject of fair value accounting. While some commentators applaud the use of fair value accounting as a positive factor in promptly revealing the values of financial assets in today's troubled credit markets, others decry the use of fair value accounting as a negative factor exacerbating the problems in the credit markets.

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Over the past 18 months, what some viewed as a subprime mortgage crisis has spread to the global economy. The National Bureau of Economic Research announced that the United States has been in a recession since December 2007 and is expected to "likely be the longest, and possibly one of the deepest, since WWII."

Some posit that the fair value accounting standards have contributed to or exacerbated the crisis in this illiquid market by requiring asset write downs below their underlying or intrinsic economic values. Critics assert that these write downs have triggered a downward market spiral, causing diminished investor confidence, further losses in value, and lessened liquidity. Fair value supporters counter that fair value reporting enhances transparency and, therefore, investor confidence. They argue that suspension of fair value reporting would decrease transparency, thereby, leading to greater uncertainty and instability in the market.

Our paper examines the current economic tsunami as it relates to fair value reporting and explores the role of accounting and auditing from an ethical perspective. We believe that accounting is applied ethics, and accountants and auditors are the gatekeepers of business ethics. Contemporary ethical models are applied to the accounting profession. Results of the recently released SEC study on mark-to-market accounting are considered and fair value reporting rules are evaluated from an ethical perspective.

THE FINANCIAL REPORTING FRAMEWORK AND BACKGROUND INFORMATION ON FAIR VALUE ACCOUNTING

SFAC No. 1 states that the objective of financial reporting is to provide information to investors and creditors that are useful in decision-making. SFAC No. 2 states that the two primary qualitative characteristics that provide decision-utility are relevance and reliability, with secondary qualities of comparability and consistency. Financial information is also used in prudential oversight. According to the Basel Committee on Banking Supervision, prudential oversight is to foster safety, soundness, and financial stability.

Under current U.S. GAAP, items on the balance sheet are measured using a mixed-attribute model. This model calls for carrying some assets and liabilities at historical cost, some at fair value, and some at other bases, such as lower-of-cost-or-fair-value. GAAP rules governing appropriate measurement attributes for specific accounts hark back to conceptual framework theory relating choice of measurement attribute to promoting relevance, reliability, and comparability so as to maximize decision utility. SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands fair value measurement disclosures. One objective of SFAS No. 157 is to improve consistency and comparability of fair value measurements. Fair value is defined as the "price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date" [SFAS No. 157]. Thus, fair value is an exchange price, an exit price. FASB concluded that an exit price objective is appropriate since it embodies current expectations about future inflows associated with the asset and future outflows

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associated with the liability from the market participant perspective. Continued use of current (fair) values is consistent with FASB's and the IASB's conceptual preference for the primacy of the balance sheet over the income statement. Fair value represents measurements related to the present. Historical cost represents measurements relating to the past.

Current GAAP requirements for fair value measurement of select assets and liabilities hark back to the banking and Savings & Loan crisis of the 1980s. At that time, many financial institutions were paying higher interest on deposits than they were earning on long-term fixed-rate mortgage loans. The historical cost model, the prevailing measurement attribute under GAAP at that time, masked the problem by recognizing losses gradually through negative net interest income. The current value of the institutions' assets was less than the current value of the liabilities, effectively making the institutions insolvent. The historical cost model obscured the problem due to the requirement of carrying assets at inflated cost figures. Therefore, transparency was greatly diminished.

Existing fair value and mark-to-market requirements were developed over several decades to address specific market events or conditions as noted above. These standards were the result of an extensive due process, and their elimination could erode investor confidence in financial reporting, contributing to greater market instability. Mark-to-market accounting standards apply only for select financial instruments and derivatives held for grading purposes. Mark-to-market rules, therefore, apply to a minority of investments/assets. For the SEC study, 22% of bank, 3% of insurance company, and 1% of credit institution assets are marked-to-market. On 70% of the overall study sample, adoption of SFAS No. 157 fair value rules had no impact, and no issuers had an impact over 5% of equity.

SEC roundtable discussions of fair value accounting and auditing standards reflected that "investors indicated fair value is the most relevant attribute for financial instruments in the current market environment." Participants considered historical cost to be more reliable, but less relevant and less comparable. They argued that while fair value is not precise or as objective (not as reliable), it is the most relevant measurement attribute, increasing transparency and consistency in financial reporting. Many panelists stated that they did not believe that fair value accounting caused or contributed to the current global economic crisis. They asserted that accounting information reports economic activity; it does not cause it.

THE SEC STUDY ON MARK-TO-MARKET ACCOUNTING

The EESA (Emergency Economic Stabilization Act), passed into law on October 3, 2008, mandated a study on mark-to-market accounting to be conducted by the SEC in consultation with the Board of Governors of the Federal Reserve System and the Secretary of the Treasury. Events and causal factors leading up to the Congressional call for this study were assertions that fair value accounting, along with SFAS No. 157 guidance on measuring fair value, contributed to instability in our financial markets. Critics alleged that such instability resulted from inappropriate write-

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downs in the value of investments held by financial institutions---write-downs that did not reflect underlying, intrinsic economic values of the securities in an inactive, illiquid, or irrational market. Correlation between U.S. GAAP reporting and regulatory requirements of financial institutions could, in their view, lead to failure of financial institutions, broader negative impact on prices and markets, and further financial instability.

However, other market participants, notably investors, stated that fair value accounting enhances transparency of financial statement information to the public. Investors, therefore, called for adherence to fair value reporting as vital in times of financial stress in the marketplace. Suspension of fair value reporting would, in their view, weaken investor confidence due to lessened transparency and thus, result in even greater market instability. According to these participants, the current financial market instability is a result of poor lending decisions, inadequate risk management, and regulatory inadequacy---not accounting standards.

The SEC study considered all viewpoints concerning the effects of fair value accounting on financial markets. Roundtable discussions and extensive research provide the foundation for the SEC study conclusions. The study focused on the usefulness of fair value accounting to investors, the potential market behavior effects of fair value accounting, challenges in applying fair value measurements, potential improvements in current standards, and auditor assurance with regard to fair values. For many years, accounting standards have required measurement of financial instruments on a financial institution's balance sheet at fair value. Losses or gains on trading securities (carried on the balance sheet at fair value) are reflected in income and retained earnings in accordance with U.S. GAAP and generally recognized in regulatory capital. For available-for-sale securities (measured at fair value on the balance sheet), changes in fair value are generally reported in equity (accumulated other comprehensive income) and bypass the income statement, unless an impairment has occurred.

As noted in the study, most challenges to fair value accounting revolve around four main concerns, addressed below. First, that fair value accounting measurements are unreliable in the absence of quoted market prices, leading to lack of reliability and comparability of financial statements. The body of academic research supports survey results from the SEC study supporting the relevance of fair value information to investors. Most previous academic studies examine whether stock prices are associated with reported fair values and fair value disclosures. Results indicate a positive correlation between business entity's stock prices and reported fair values and disclosures for financial instruments. Song, ET. Al [2008] test the value relevance of SFAS No. 157's Fair Value Hierarchy and find that Level 1 and 2 fair value measurements are value relevant to investors, but Level 3 estimates are less value relevant. Ryan [2008] also found that investors view fair value measurements to be relevant. Though comparability concerns were also raised in the context of fair value accounting in the absence of quoted market prices, a similar case can be made for historical cost which results in identical assets measured at different values reflecting different purchase prices.

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A second concern is increased income statement volatility resulting from fair value write-up/write-downs. While prior research does indicate increased volatility in income and regulatory capital under fair value accounting, increased income volatility under fair value may be a proxy for market risk, reflecting underlying economic risks.

Third, concern exists about the inconsistency of valuing some assets and liabilities at a current exit price and assuming a going concern doctrine for measuring other assets and liabilities. FASB will address this and other issues in its measurement component of the Conceptual Framework project. Fourth, does fair value understate the underlying (intrinsic) economic value of financial instruments in depressed markets? Significant concerns have been raised concerning whether fair value accounting induced pro-cyclical downward pressure in asset prices, causing security prices and asset values to fall below true inherent values. Write-downs caused by fair value rules may compel some financial institutions to sell securities in illiquid markets in order to comply with regulatory capital requirements. To address this issue, one must separate the effects of regulatory capital standards from accounting standards. Many study participants expressed the view that pro-cyclicality concerns arise from the use of financial reporting results for regulatory capital purposes. Regulatory capital standards relate to capital adequacy for financial institutions. Accounting standards promote fair and accurate financial reporting for use by investors in the efficient allocation of scarce capital resources.

SFAS No. 157's objective is to provide transparent, unbiased information about value. GAAP is designed to primarily serve the information needs of external users who must rely on information provided by management. Regulatory capital requirements, which relate to oversight objectives of regulatory agencies, are outside the purposes and objectives of financial reporting and accounting standards. The SEC study results conclude that pro-cyclicality arises from deleveraging market effects, an economic decision.

Key findings from the SEC study note that investor generally believe fair value accounting increases financial reporting transparency and facilitates better investment decision-making. The report also observes that fair value accounting did not appear to play a meaningful role in bank failures in 2008. The report indicates that U.S. bank failures appeared to be the result of growing probable credit losses, concerns about asset quality, and in certain cases, eroding lender and investor confidence.

After considering the available evidence gained from roundtable discussions, surveys of market participants, and the body of academic research on the value relevance of fair value accounting, the SEC determined that the suspension of fair value, returning to historical cost measurements, would adversely impact debt and equity security valuation. Withholding current (fair) value information would introduce greater uncertainty, information asymmetry among market participants, and further lessen market liquidity. In our currently depressed markets, suspending fair value would result in removing useful information from investors at a time of great uncertainty and risk, when it is needed most. Also, suspending fair value rules would not relieve companies from recognizing impairment losses.

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The SEC study concluded that: (1) fair value measurements were used to measure a minority of financial institutions' assets and liabilities; (2) fair value accounting did not appear to play a significant role in 2008 bank failures; (3) investors support fair value measurement as providing the most transparent financial reporting of investments and, therefore, the greatest decision-making utility as well as the most efficient allocation of scarce capital resources; and (4) suspension of fair value accounting and a return to historical cost-based measurement would increase investor uncertainty---suspension of SFAS No. 157 would result in inconsistent and conflicting fair value measurements.

The study warned that suspension of fair value accounting "would be akin to shooting the messenger and hiding from capital providers the true economic condition of a financial institution." SEC recommendations deriving from the study included improvements to existing practice in accounting for impairments and the development of additional guidance for determining fair value of investments in inactive markets, including situations where market prices are not readily available.

CONTEMPORARY ETHICAL MODELS

Over the years, several theoretical models have emerged for explaining ethical behavior. A brief description follows.

Utilitarianism

Many ethicists hold that the fairness of an action can best be determined by its results or consequences. If the consequences are good, the action or decision is considered good. The Utilitarian principle is, therefore, a consequential principle or teleological principle. This approach asserts that we should "… strive to make decisions that optimize the greatest possible good… for the greatest number of people…" [Epstein and Spalding, 1993]. The attractiveness of utilitarianism is that it proposes a standard outside of self-interest by which to judge the value of a course of action and forces the decision-maker to consider the general welfare. A cost-benefit analysis is an example of utilitarian thinking. Utilitarianism forces us to consider an action in the context of its impact on stakeholders.

Using this reasoning may lead to the problematic argument that the end justifies the means. The sheer numbers of stakeholders affected by the decisions of a single accountant make prediction of the consequences for each one impossible. Ultimately, the individual is faced with the issue of determining what the greatest good for the greatest number is. Using this principle, it is very difficult to formulate rules to guide decision making.

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Pragmatism (Egoism)

In this model, only the good for the decision maker need be considered. However, this system has great potential for conflict and, therefore, is not a functional basis for developing ethical standards. As an example, businesses seek to maximize profit and minimize cost. The individual accountant, who prepares/audits the financial statements reflecting these accounts, has an individual goal of maximizing utility. Only by coincidence would the two goals result in the same desired action. Further, it is improbable that the good of the company or the accountant would always serve the needs of the larger community of stakeholders.

Egoism is the normative ethical position that moral agents should act in their own self-interest. Economic theory implies that when faced with a choice between ethics and self-interest, the latter will prevail. Both Adam Smith and John Bares Clark indicate that a strong sense of ethics is necessary for capitalism to overcome the inherent greed motivated by self-interest. Clark considers religion as the ethical base and prescribes the morally superior person as the solution [Everett, 1946].

Religion

The religious model relies on the guidance of a supreme being, God, who sets standards of right and wrong. The Judeo-Christian ethic provides moral imperatives such as: be honest, do good to others, respect human life, respect the property of others, and so forth. Although multi-national firms and a global marketplace may encompass operations in areas of the world not governed by Judeo-Christian principles, religion does provide the broadest basis that society has for an ethical framework as well as justification for ethical acts such as fair labor practices, environmental responsibility, and workplace safety.

Deontology

Deontological theories focus on duties. This ethical approach focuses on the action and ignores the consequences. An accountant has a moral duty to present fairly (honestly, completely, without bias) the financial statements of a company. The accountant is bound by his/her duty to adhere to the AICPA Professional Code of Conduct as well as personal ethical values. Stakeholders expect accountants and auditors to follow this ethical code and, therefore, assume a fair and representationally faithful set of books as a result.

One disadvantage of the deontological model is that it provides no framework for continuous evaluation of what is "best." There are still gray areas in accounting---topics for which no accounting principles have been promulgated or for which accounting standards may need to be revised. Fallible human beings promulgate fallible accounting standards. Accountants and auditors have a duty to the profession to follow GAAP and GAAS, even though existing GAAP in some

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cases may be inadequate. GAAP is procedural, and if less than fair, can be changed. However, input for or against changing existing accounting standards is most often self-serving (based on egoism). Suspension of fair value accounting, which masks the true value of financial assets/liabilities, has been called for heavily in the banking industry. Avoiding asset write-downs and losses in the short-term may allow banks to meet regulatory capital requirements and report higher earnings, but could lead to nasty surprises for investors in the future. Ethics should provide the ultimate guidance to accountants. The ethical standard is fairness (honesty, freedom from bias).

Hermeneutical Model

This ethical model portrays the accountant as an agent giving an account. Schweiker [1993] claims that "…a hermeneutical and ethical examination of the activity of giving an account as basic to understanding the moral dimension of accounting practice and research." In this ethical perspective, the relationship between the accountant and the accounting records/financial statements involves a higher ethical imperative than the economic imperative of profit maximization and self-interest. According to Schweiker, giving an account equates to giving the corporation a "moral identity." Thus, the accountant's act of giving an account exposes the amoral world to ethical accountability. Schweiker posits that accounting gives identity to the "we" in the Socratic ethical question, "how should we live?" when the *we* is the corporation. The accountant provides answers to questions regarding how the corporation "can and must live in relation to others and themselves" [Schweiker, 1993].

Giving an account provides identity. The corporation, known to others through the financial statements, is a member of a moral community similar to an individual. In giving an account, the corporation subjects itself to a universal means of discourse to examine itself, and to be examined, through the fiduciary agent, the accountant or auditor. Ergo, the accountant becomes the soul or moral conscience for the corporation. Giving an account provides a snapshot, a temporal identity, of the corporation's actions and makes them accountable for those actions to the larger community. The accountant is professionally and ethically bound to faithfully render the corporation's identity.

Communitarian Model

The communitarian perspective harks back to the early Greek philosopher, Aristotle [1980]. This approach argues that ethical considerations emerge from within a particular community and considers universal ethical imperatives suspicious. While the deontological aspects of accounting are clear, as explained above, strong communitarian influences can also be identified in the process by which GAAP in the U.S. has emerged. Prior to the stock market crash of 1929, accounting principles were not explicit, were internally inconsistent, and not universally enforced. The significance of this is that accounting principles for properly financial statement reporting emerged from within the community itself. Thus, GAAP emerged through a process of exchange between

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firms and government. GAAP was codified, became more internally consistent through this communitarian system of due process for standard setting, and financial statements became more comparable. Financial statement relevance and reliability were enhanced, making them more useful for decision making by external users. Communitarian principles can also be observed in regard to international accounting standard setting, which is also influenced by the community served.

The Investors Technical Advisory Committee (ITAC) has expressed concern regarding calls for suspension of fair value accounting by banking and insurance lobbyists, politicians, and others recently in the media. According to ITAC, the critical tenet of independent private sector accounting standard setting empowered by an extensive, public due process system prioritizing investor needs could be impaired, thereby, diminishing investor confidence in financial reporting. ITAC strongly supports fair value accounting and suggests that financial reporting would be significantly improved if fair value was the measurement attribute for all financial instruments.

ETHICS AND FAIR VALUE ACCOUNTING

Accounting plays a key role in the economic and social progress of a nation. Stakeholders, such as investors, creditors, and others, rely on the integrity of accounting information in corporate financial statements. Ethics is a critical element of the accounting profession, as evidenced by the profession's time-honored commitment to serve the public interest. Francis [1990] states that accounting is a discipline which is thoroughly ethical in nature. Dolfsma [2006] asserts that accounting is applied ethics.

In 1494, the Italian, Luca Pacioli, was the first to bring out a book where the principles of double-entry bookkeeping were explained. This double-entry bookkeeping system provided internal controls for consistency. One reason for starting to keep accounts was a moral one: to be able to know and keep track of which individuals and organizations were due how much [de Wal, 1927]. Accountants could be perceived as minding the rights that different parties have toward others, drawing on deontological ethical considerations. The Dutch East India Company [de Boer, 1957] was the first to regularly prepare public financial reports and also the first "firm where ownership and management were separated," leading to a control struggle wherein moral arguments played a significant role. Accountants' fiduciary responsibilities involve not only tracking rights and obligations to various stakeholders, but also extend to maintaining accountability for integrity of funds---insuring that money is spent for its intended purpose. Again, this suggests the moral overtones of accounting.

The responsibility of the auditor is to recognize the ethical dilemmas their clients may face and detect whether the client has behaved unethically. The auditor must serve as an ethical detective. Post-Enron reforms have gone a long way toward restoring investor confidence in auditors and the audit profession's alignment with investors. Capital markets thrive when investors have confidence in them. Like law, auditing is a gatekeeper profession in our corporate governance system. Accounting and auditing as a profession are not only repositories of financial expertise, but

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also cultures of ethical responsibility. At the heart of the major professions---medicine, law, and accounting---is a dedication to serving their clients and upholding high standards of technical competency and moral integrity. The ultimate objective is to serve the public interest/good.

A significant trend toward ethics improvements is the impetus for enhanced transparency. Corporate transparency refers to a quality or state in which activities, practices, processes, decisions, and financial reporting become open and visible to public scrutiny. Opacity, the opposite of transparency, describes a condition where activities, decisions, and financial reporting remain obscure (hidden) from public stakeholder review. Stakeholders want to know the reality of what is occurring within business organizations. Recent scandals such as WorldCom and Enron have exerted greater public pressure for transparency in financial reporting and greater independence in auditing. The Sarbanes-Oxley Act of 2002 mandates greater transparency and independence. Transparency leads to accountability. Increasingly, companies are realizing the internal benefits of transparency as an ethical practice. Pagano and Pagano in their book *The Transparency Edge: How Credibility Can Make or Break You in Business*, promote a transparent management approach. In their view, a "what you see is what you get" code of conduct will enhance a company's credibility in the marketplace, build loyalty, and enable the company to gain the trust and confidence of stakeholders. Tapscott and Ticoll in their book, *The Naked Corporation: How the Age of Transparency Will Revolutionize Business*, direct companies to "undress for success." They argue that corporate transparency is inevitable, not optional. As companies become more open in their reporting practices, the public and other stakeholders will come to have greater confidence in them because of the greater disclosure (more will be exposed to view).

Transparency implies openness, communication, and accountability. It is the construct of removing all barriers to, facilitating free and easy public access. Relevant meanings include: very clear, easily understood, candid, and frank. The best definition of transparency in business is financial statements of high quality. A complex, opaque financial report gives no idea about the true risks and real fundamentals of the company. High-profile cases involving financial opacity, such as Enron and Tyco, demonstrate how managers employ fuzzy financials and complex business structures to hide unpleasant news. Lack of transparency often means nasty surprises ahead.

Transparency pays according to Robert Eccles, author of "Building Public Trust---The Value Reporting Revolution." Eccles shows that companies with fuller disclosure gain more investor trust. Relevant, reliable information equates to less risk to investors and a lower cost of capital, translating into higher valuations. Key findings indicate that companies who share key metrics and performance indicators with investors are more valuable than companies who keep information to themselves. Transparency makes analysis easier and, therefore, lowers investor risk. Transparency is assurance.

Fair value accounting, according to the SEC study, provides greater transparency to investors and therefore, greater value relevance. Fair value accounting requirements have existed for a number of years. Only recently, when market values necessitate write-downs have preparers questioned the relevance of these measurements. When bull markets existed, no one objected to

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fair value rules. As suggested by the SEC study findings, fair value accounting has increased the quality and relevance of financial reporting for investors. Investors have indicated that fair value provides more relevant information, reflecting current economic reality that should not be replaced by other alternative accounting measures, such as historical cost. Investor confidence is reinforced by providing transparency relating to the underlying asset value of their investments; removing that information would lead to greater uncertainty and greater instability in the financial markets.

"Suspending mark-to-market accounting, in essence, suspends reality," asserts Beth Brooke, global vice chair at Ernst & Young LLP. Accounting firms argue that such a change would deceive investors about troubled loan values and the value of mortgage-backed assets. Ultimately, the point of fair value accounting is to provide accurate information to investors---companies should account for their assets at their real values. Goldman Sachs Group Inc. CEO, Lloyd Blankfein, upheld mark-to-market accounting and argued that it should be even more rigorous. Goldman, which has largely avoided the current financial crisis, cites adherence to fair value accounting rules as "a key contributor to our decision to reduce risk relatively early." He states that if financial institutions had properly valued their positions/commitments at the outset, they could have substantially reduced their risk exposure.

Fair value accounting has received a significant amount of blame as the cause of the current financial crisis, not least by politicians. Fair value accounting does not cause illiquidity or volatility in financial markets, but makes it more transparent to market participants. Banks, rather than accounting, caused the existing crisis, ultimately through bad lending decisions. Politicians, lobbyists, and media representatives may not understand the operation of the capital markets and accounting's key role in resource allocation decisions within those markets. The danger is in their power to interfere in accounting rules, which should be free from outside pressure. Politicians and other naysayers misunderstanding may be deliberate, since changing the rules may serve to cover up the extent of the problem, without solving it. Accounting rules are designed to reveal the full extent of losses and future risks. This transparency would allow banks, regulators, and governments to identify specific causes of the crisis and take steps toward recovery and future prevention. Bad loans, inadequate risk management, and overreliance on rating agencies were cited in the SEC study as causes of the crisis. Shooting the accounting messenger is not a solution to these problems. Perhaps there is confusion related to a conflict between transparency and financial instability. Transparency is an objective of accounting standards. Long term financial stability is best achieved by restoring investor confidence in financial markets and assets. Transparent accounting standards and sound auditing provide support for that confidence.

While fair value measures the effects of a transaction on an entity's financial statements, it does not drive underlying economic activity. Credit Suisse Group asserted, "In our view, mark-to-market accounting is not the problem; it is reflecting an economic reality--asset values are falling. The sooner accounting reflects those losses, the better. The real problem was overexposure to certain assets, poor risk management, misunderstood and mispriced risks and lots of leverage. We would prefer to see the financial statements reflect real economic volatility rather than a false sense

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of stability." Fair value accounting has been in application for 15 years. Despite upward/downward trends in the market, investors need the financial statements to reflect value relevant information. R.J. Chambers [1991] says, "We should speak…of the immorality of accounting; for it has been the quirks of accounting that have provided many of the opportunities for misdemeanors on the part of corporate officers; and corporate accounting does not do violence to the truth occasionally and trivially, but comprehensively, systematically and universally, annually and perennially." Chambers and other observers lament that business demands on accounting to 'bend the rules' have become extreme, and some have questioned the resolve of the accounting profession to respond effectively to the critical challenge such pressures induce. Chambers [1991] aligned ethics with commercial, legal, economic, financial, and social foundations. The ideas of equity and fair dealing are ethical or moral norms. They permeate almost everything that is done in communities that have outlawed willful appropriation, by some, of the properties, persons and rights of others. Equity, trustworthiness, and fair dealing do not relate to some morality higher than and beyond the bounds of commercial affairs. They are necessary conditions of continued, more or less harmonious collaboration between parties having diverse and in some respects opposing interests in property and power. They are implicit in all contracting, all legislative and judicial processes, all arbitration, and all collaboration [Dean, 2003]. Ethics relate to the prevalent tone of the accounting profession. So grounded, accounting is the provider of one of the essential checks and balances on commerce.

SUMMARY AND CONCLUSIONS

Fair value accounting transparently reflects, under current economic conditions, the value of a firm's assets and liabilities. Suspension of fair value accounting would result in a loss of information and investor confidence. Returning to alternative cost-based measures would mask losses in value and risks and mislead investors. Evidence from the SEC study on mark-to-market accounting supports fair value as the most relevant measurement attribute for financial instruments in the current market environment. Study findings expressed strong support for independent accounting standard setting, free from political or regulatory intervention. From an ethical perspective, accounting has a responsibility to require that financial statements 'present fairly' the financial condition and operating results of an entity. In other words, the financial statements should reflect reality. They should be clear and understandable (transparent), honest, unbiased, complete, and representationally faithful (reflect economic reality). Accountants and auditors are bound by their professional code of conduct to, first and foremost, protect the public interest. They serve as the moral conscience of their clients.

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