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Did FASB 157 Cause the Financial Crisis?

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Abstract

In light of the financial meltdown that followed the bankruptcy of Lehman Brothers in the fall of 2008, there is considerable debate in the financial community on the appropriate accounting methodology used to value financial assets. In fact, many analysts on Wall Street argue that much of the blame for the current financial and economic crisis is due to fair value accounting and the implementation of FASB 157, which regulators put into effect for financial statements released after November 15, 2007. The argument is that with assets trading in illiquid markets, financial institutions reported outsized losses by writing down the value of their security and loan holdings even if they had the intent and ability to hold the assets to maturity. The critics of FASB 157 charge that these sharp write-downs contributed to the failure of banks and forced others firms into a difficult financial situation. This study examines the issues surrounding fair value accounting and looks at the role accounting played in the financial crisis. We conclude that fair value accounting played no significant role and is the preferred accounting framework for financial institutions.

Keywords: Fair-value accounting, FASB 157, mark to-market, level 1, 2 and 3 assets**JEL Classification:** G01, G10, G21, M41[Suggested Citation](#) >[Show Contact Information](#) >

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