Mark-to-Market Regulatory Accounting

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Mark-to-market regulatory accounting (M-to-M) is demonstrated to be an inappropriate asset valuation-standard for use by the Federal Reserve in its regulation of financial-services firms. The paper argues that the Fed must reject the M-to-M method in favor of an accounting system that is coherent with its pursuit of legally mandated macroeconomic objectives. Especially in periods of severe disturbances as exemplified by the 2008-09 financial crisis, M-to-M valuation standards work at cross-purposes with well-designed central-bank stabilization policies. The inconsistency not only exists, it is also shown to be important. The use of M-to-M regulatory capital valuation standards can greatly damage the effectiveness of Federal Reserve monetary interventions.

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