June 15, 2010

The Honorable Barney Frank, Chair
U.S. House-Senate Financial Reform Conference Committee
2129 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Frank and Members of the Committee:

As the Committee seeks to reconcile H.R. 4173, we write as leaders of the National Conference of Insurance Legislators (NCOIL) to caution you that the base bill neglects a major problem that state legislators have identified in the credit default swaps (CDS) market—the lack of any material interest in so-called “naked” CDS transactions.

We share your conviction that the CDS market, after operating with minimal oversight for nearly a decade after passage of the federal Commodity Futures Modernization Act, must be regulated. However, NCOIL continues to believe that CDS—which are most often defined as “insurance” against negative credit events—should be regulated as insurance.

Last year, NCOIL developed Credit Default Insurance Model Legislation to guide states in regulating CDS as insurance. Our model would, for the first time, outlaw naked swaps by requiring material interest as a prerequisite for buying protection. It also contains standard insurance requirements regarding company licensing, capital and surplus, and policy forms and rates, among other things.

Not only does H.R. 4173 ignore the need for material interest and allow naked swaps, it goes further to effectively prevent state efforts to require material interest. Pages 658 and 998 say that the states may not regulate swaps as insurance. The provisions were added to the House and Senate bills without much debate.

As NCOIL President and as the Chair of its Financial Services & Investment Products Committee, we strongly urge you to reconsider whether CDS are, and should be regulated, as insurance. At the very least, Congress should consider banning naked CDS—swaps that significantly exacerbated, if not caused, the nation’s financial crisis.

Sincerely,

Representative Robert Damron (KY)    Armyman Joseph Morelle (NY)
NCOIL President      NCOIL Financial Services & Investment Products Committee Chair

cc: NCOIL Legislators
U.S. House and Senate Leadership

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