May 18, 2009

The Honorable Christopher J. Dodd
Chairman
Senate Committee on Banking,
Housing and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Richard Shelby
Ranking Member
Senate Committee on Banking,
Housing and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Barney Frank
Chairman
House Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

The Honorable Spencer Bachus
Ranking Member
House Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Dear Chairmen Dodd and Frank, and Ranking Members Shelby and Bachus:

The Conference of State Bank Supervisors (CSBS), the National Association of Insurance Commissioners (NAIC) and the North American Securities Administrators Association (NASAA) have each proposed principles for financial services regulatory reform that we believe will help guide the ongoing policy debate over the changes necessary to strengthen the nation's financial services regulatory structure. The unique experiences of state regulators on the front lines of consumer and investor protection provide the basis for our suggestions. Any regulatory reform measure must recognize the importance of ground level detection and policy sensitivity. These are critical characteristics of state regulation and necessary components of an effective financial regulatory structure.

At this time, we want to address one particular issue that has received considerable attention from your Committees in recent months – identifying and managing systemic risk in our financial markets. We encourage you to consider several basic recommendations from state banking, insurance and securities regulators as you reflect upon structural methodologies to address this challenge. After analyzing a number of strategies, we have concluded that the responsibility of identifying and managing systemic risk should not be assigned to a single agency but should be carried out by a council made up of state and federal regulators. We believe this approach holds the greatest promise of success in evaluating and controlling systemic risk in the marketplace because it will formalize regulatory cooperation and communication among state and federal regulators that oversee our financially intertwined markets.

Membership. The systemic risk council should include representatives from all federal and state banking, insurance and securities regulators. This holistic approach is effective and efficient. It creates a body with access to all relevant information regarding the accumulation of risk in our financial system, and it draws upon the existing expertise and proficiency of each functional regulator. It also minimizes the possibility of regulatory capture or philosophical bias that might arise if an existing federal agency were tasked with overseeing systemic risk. As a further measure against undue influence or capture, we believe the council should be headed by an independent chair. This would maintain balance and reduce the likelihood that any one member of the council or any one regulatory perspective exerts undue influence over the council's policies and operations.

Including state regulators on the council is necessary and appropriate. In all financial sectors, state regulators gather and act upon large amounts of information from industry participants and from investors. Consequently, they serve as an early warning system. As a general proposition, state regulators are usually the first to identify risks and related trends that are substantial contributing factors to systemic risk.

Function. The council should be tasked with collecting and evaluating data from all financial sectors to assess existing levels of systemic risk as well as the identification and analysis of new financial products or business practices that may be expected to increase levels of risk. In addition, when the council perceives the need for corrective measures, it should issue recommendations to the regulators with primary authority over the market sector in question. Those recommendations may range from the suggestion that various actions be taken, including emergency market intervention, the promulgation of new regulations, or even enforcement actions. In addition, the council would, where appropriate, recommend the passage of new legislation at the federal or state level.

Authority. The council should have the authority to require industry participants and other agencies to share information relevant to the mission of risk assessment. In other respects, however, its powers should be carefully circumscribed and its primary focus should remain the collection and analysis of data and issuing appropriate recommendations, leaving the authority of existing functional regulators intact.

In conclusion, as the state organizations representing the three major sectors of financial services regulation, we are committed to working with Congress to address the problem of systemic risk in our financial markets. We believe that the systemic risk council model described above is the optimal approach, as it recognizes and incorporates the states' vital role in financial services regulation and consumer protection.

Sincerely,

Timothy J. Karsky CSBS Chairman North Dakota Banking Commissioner	Roger Sevigny NAIC President New Hampshire Insurance Commissioner	Fred J. Joseph NASAA President Colorado Securities Commissioner

cc: Senate Banking, Housing, and Urban Affairs Committee members
House Financial Services Committee members