NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.

NASAA

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The Honorable Richard Shelby Chairman Senate Banking, Housing, and Urban Affairs Committee	The Honorable Paul Sarbanes Ranking Member Senate Banking, Housing, and Urban Affairs Committee
The Honorable Michael Oxley Chairman House Financial Services Committee	The Honorable Barney Frank Ranking Member House Financial Services Committee

RE: Financial Services Regulatory Relief Act

Dear Senators and Congressmen:

As you work to resolve differences between the Senate and House versions of the Financial Services Regulatory Relief Act, members of the North American Securities Administrators Association (NASAA)[1] respectfully request that you keep in mind our concerns over Section 209 in the House passed version of H.R. 3505.

Section 209, "Selling and Offering of Deposit Products" alters current law by preempting states from licensing independent contractors — not employees — of federal savings associations selling products that include not only traditional FDIC insured certificates of deposit, but other products that may be complex and risky, such as market-indexed certificates of deposit (see attached article). Another problem is that the jumbo deposit products being sold can exceed the limits of FDIC insurance.

These independent contractors are individuals who do not have the employee affiliation with the thrift, do not necessarily have adequate training, and do not fall under the supervision of the thrift. The problem is exacerbated because many investors assume that a salesperson representing a financial institution is an employee, fully backed by the institution. Yet this is not the case, and these independent agents need oversight if they are going to offer the more complex and riskier deposit products.

NASAA is supportive of regulatory relief that is the appropriate balance between

[1] The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc., was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, the U.S. Virgin Islands, Canada, Mexico and Puerto Rico. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

regulatory efficiency and protections for all investors. We are pleased that this language is not contained in S. 2856 and we recommend the language not be included in the Financial Services Regulatory Relief Act of 2006 when it is signed into law.

Sincerely,

Patricia D. Struck
NASAA President
Wisconsin Securities Administrator

Joseph P. Borg
NASAA President-elect
Director, Alabama Securities Commission

cc: The Honorable Mike Crapo
The Honorable Christopher J. Dodd
The Honorable Chuck Hagel
The Honorable Spencer Bachus
The Honorable Richard Baker
The Honorable Paul E. Kanjorski
The Honorable Bernard Sanders

May 17, 2006

Linking stock index returns to CDs may be a risky move

By Sandra Block
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The March issue of Popular Science highlights cool stuff we thought someone would have invented by now - a flying car, a cure for baldness, a robot maid.

Another item to add to the wish list is an investment that delivers great returns with no risk. Unfortunately, such an investment doesn't exist. But that hasn't stopped some financial advisers from claiming that they've found a way to defy the laws of economics.

The latest example: market-indexed certificates of deposit. These products, also known as market-linked CDs, seem to offer the best of both worlds. Your principal is guaranteed by the Federal Deposit Insurance Corp. And you can earn returns based on a stock market index.

That sounds like a great way to strap a jetpack to what has historically been a humdrum investment. But a market-indexed CD "has more risk than a typical bank CD," says Grace Vogel, executive vice president for the New York Stock Exchange. You could lose money or earn less than you expected.

The New York Stock Exchange has seen an increase in the sale of market-indexed CDs and is concerned that some customers don't understand the difference between these hybrid products and traditional CDs.

THE FINE PRINT

In a recent memo, the NYSE said brokerage firms should disclose in clear language the risks of these products, which include:

Market risk. If you redeem a conventional CD before it matures, you'll forfeit some of your interest earnings but you'll still recoup your initial investment. That's not always true with market-indexed CDs. If you sell before it matures, you could lose some of your principal, says Robert Mooney, acting deputy director for the Federal Deposit Insurance Corp.'s division of supervision and consumer protection.

Liquidity risk. If you have to redeem your market-indexed CD before maturity, your bank may allow you to get your money only on specific "liquidation dates," which are disclosed ahead of time.

Limits on returns. Some market-indexed CDs impose a cap on the amount you can earn. For example, if the underlying index rises 15 percent, the cap may limit your CD's earnings to just 6 percent, the NYSE says. Make sure you understand before you invest.

Taxes. Even though some of your returns are linked to the stock market, all the earnings on a market-indexed CD are considered interest for tax purposes. That means they'll be taxed at your ordinary income tax rate, not the lower capital-gains rate for long-term investments in stocks and mutual funds.

Call provisions. Some market-indexed CDs allow the financial institution to redeem the CDs before maturity, as long as the investor is notified in advance.

STAYING SAFE

If you understand these risks and still want a CD with some potential for above-average returns, then a market-indexed product might have a place in your portfolio.

But most people who invest in CDs buy them because they're very safe and deliver a guaranteed interest rate as long as they're held until maturity, says Patricia Struck, president of the North American Securities Administrators Association. When you buy a market-indexed CD, she says, "That's not what you're getting."

If you want the security of a traditional CD but would like to earn above-average returns, shop around.

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