Financial Reform Bill Blocked, But Derivative Bill Proceeds

By Editor Test *Tue, Apr 27, 2010*

Under an Agriculture Committee-backed bill, insurers who use derivatives to hedge against interest rate risk would have to use standardized derivatives contracts listed on exchanges.

Senate Republicans voted on Monday to block debate the Democrats' legislation to tighten regulation of the financial system, most recently known as the Wall Street Reform Act.

Sen. Christopher Dodd, D-Conn., chairman of the Senate Banking, Housing and Urban Affairs Committee, filed a 1,408-page version of the bill April 15. A compromise version of that bill was to be debated on Monday.

Meanwhile, members of the Senate Agriculture Committee have approved the Wall Street Transparency and Accountability Act, a bill that would regulate the use of derivatives by insurers.

The committee passed the bill, which does not yet have a bill number, by a 13-8 vote. Sen. Charles Grassley, R-Iowa, joined 12 Democrats in supporting the measure, which was sponsored by Sen. Blanche Lincoln, D-Ark., chairman of the Agriculture Committee.

The proposed bill would not regulate the use of custom derivatives by commercial users such as airlines, farmers, and others who use derivatives to lock in the cost of the fuel or other raw materials used in the products or services they make or sell.

But life insurance companies would face new constraints. Insurers who use derivatives to hedge life insurance policies or other policies against interest rate risk would have to use standardized derivatives contracts listed on exchanges, an insurance industry lobbyist says.

The House financial services reform bill provides an exemption for insurers that use custom derivatives, however.

The April 15 version of Senate Bill 3217-the Dodd bill-included sections that would:

- Create a Financial Stability Oversight Council with some ability to oversee non-bank financial companies.
- Create an "orderly liquidation authority" for large, troubled financial companies.
- Form an Office of National Insurance.
- Promote uniformity in regulation of reinsurance and surplus lines coverage.
- Create new derivatives markets regulations that might affect how insurers hedge credit and default risk.
- Change the rules governing asset-backed securitization.
- Overhaul rating agency rules.
- Impose new executive compensation system rules.

- Create “senior investor protection” rules, including annuity marketing standards developed by the National Association of Insurance Commissioners.
- Reorganize and consolidate the federal bank and thrift regulatory agencies.
- Impose a federal regulatory system on hedge fund advisors.
- Put new restrictions on banks’ capital markets activities.
- Revamp securities arbitration system rules.
- Increase the borrowing limit on Treasury loans.
- Establish a Bureau of Consumer Financial Protection that would not oversee insurance products.

The April 15 version of the bill would also call for studies on mutual fund advertising, conflicts of interest, the use of financial designations; municipal bond disclosure rules, and “harmonization” of the customer relationship standards that apply to brokers, dealers and investment advisors.

Democrats need support from at least 60 senators to have S. 3217 come up for a vote. Observers are speculating that at least one Republican, such as Sen. Scott Brown, R-Mass., might agree to vote for the bill, and then might have some ability to fine-tune the bill.