

**Hearing on Legislative Proposals to Promote Job Creation, Capital Formation,
and Market Certainty before the Capital Markets Subcommittee of the House
Committee on Financial Services**

Statement of Luke Zubrod
Director, Chatham Financial

March 16, 2011

Good afternoon Chairman Garrett, Ranking Member Waters, and members of the subcommittee. I thank you for the opportunity to testify today regarding legislative proposals to promote job creation, capital formation and market certainty. My name is Luke Zubrod and I am a Director at Chatham Financial ("Chatham"). Today, Chatham speaks on behalf of the Coalition for Derivatives End-Users ("Coalition"). The Coalition represents thousands of companies across the U.S. that utilize over-the-counter ("OTC") derivatives to manage day-to-day business risks. The companies represented by the Coalition use derivatives to reduce risks in their businesses - not to take on risk through speculation.

Chatham is an independent advisor and service provider to hundreds of businesses that use derivatives to reduce their interest rate and foreign currency risk. A global firm based in Pennsylvania, Chatham serves as a trusted advisor to over 1,000 end-user clients ranging from Fortune 100 companies to small businesses, including clients in 46 states and every state represented by Members of this subcommittee.

The Coalition supports the efforts of this subcommittee to pass legislation aimed at reducing systemic risk and increasing transparency in the OTC derivatives market. The Coalition also appreciates the bipartisan nature of the present undertaking. The Coalition believes that a bipartisan, bicameral effort will be necessary to ensure that end users of derivatives are not unduly burdened by regulation intended to curb risks associated with firms whose derivatives use makes them systemically risky. The overwhelming, and bipartisan, support for end users was made clear in the amendments adopted to the financial reform legislation that passed the House in December of 2009. Several amendments, including the Murphy-McMahon amendment which passed with 304 votes, were intended to ensure that the salient economic requirements of the Act were appropriately focused on those entities whose use of derivatives could jeopardize financial stability. In essence, they were intended to protect end users from onerous bank-like regulation that would divert precious working capital from job-creating activities, including research & development and business expansion.

Let me turn to where things now stand in terms of implementing the derivatives title of the Dodd-Frank Act and point out where end users have the greatest concerns.

The Coalition appreciates recent comments by Federal Reserve Board Chairman Ben Bernanke, Commodity Futures Trading Commission ("CFTC") Chairman Gary Gensler, and Securities and Exchange Commission ("SEC") Chairman Mary Schapiro indicating that margin requirements should not be imposed retroactively. Appropriately, the chairmen recognize that the retroactive imposition of a margin requirement would upset the reasonable expectations of market participants when they entered into pre-existing contracts and could severely restrict economic growth.

The Coalition is concerned, however, by recent testimony provided by regulators concerning the imposition of margin requirements on end-user transactions used prudently for the purpose of risk management. Congress recognized that the imposition of margin on end user transactions would divert working capital from job-creating activities and hamper economic growth, while offering no appreciable mitigation of systemic risk. Indeed, following the conclusion of the conference committee, the chairmen of the four committees with primary jurisdiction over Title VII took steps to make clear that regulators did not have the authority to impose margin on end-user hedges; however, in spite of congressional intent and the clear language of the statute, some regulators appear to have interpreted Title VII as giving them authority to impose margin on end-user hedges and - even worse - *requiring* swap dealers to impose margin requirements on all end-user hedges. We never thought we would need to come back to Congress seeking legislation to prevent regulators from imposing margin on end-user companies, either directly or indirectly, but that is the position in which we now find ourselves.

We respectfully request that this committee provide end users with certainty by clarifying that their hedges will not be subject to margin requirements. In addition to providing important certainty for Main Street businesses, such a clarification would promote international harmonization and minimize regulatory arbitrage.

The Coalition appreciates the hard work of the CFTC, SEC and prudential regulators in proposing more than half of the 150 or more expected rules to meet the one-year rulemaking timeline mandated by Congress. The regulators have run an open and transparent process and have met with representatives of the Coalition approximately a dozen times. The Coalition has submitted numerous comment letters to assist the regulators in improving proposed rules and in identifying regulations that might unintentionally harm well-functioning segments of the market. However, we are concerned that the statutory deadline for rulemaking does not allow regulators sufficient time to incorporate recommendations, craft thoughtful rules, and conduct adequate cost-benefit analyses. Though regulators have sufficient authority to adopt a phased-in approach to the implementation of rules, we are eager to ensure the final rules strengthen the market and minimize unintended and unnecessary consequences. We therefore respectfully ask this committee to consider extending the date by which final derivatives regulations must be promulgated, which is now set at July 15, 2011.

Additionally, though we strongly support the legislation's transparency objective, we are concerned that proposed real-time reporting rules could inadvertently jeopardize end user's ability to secure efficient market pricing in certain situations. In particular, it is important that large or less liquid transactions be classified as block trades and that the public reporting of such transactions be adequately delayed. If reporting of these types of trades occurs instantaneously, it could provide a roadmap for other market participants to trade on that information and, through such "front-running," make the end-user trades more expensive. In this way, the real time reporting requirement could work at cross-purposes to the objective of increasing transparency, ultimately increasing the cost of managing risk for larger trades.

Finally, the Coalition is concerned that capital adequacy guidelines finalized by the Basel Committee on Banking Supervision late last year could unnecessarily and substantially increase end-user costs incurred as they use

derivatives to manage their business risks. Though we support appropriate risk-based increases to banks' capital, we believe proposed requirements fail to reflect this committee's consensus that end-user risk management activities do not contribute to systemic risk. If capital charges are disproportionately increased, end users may opt out of hedging, which in turn would translate to increased volatility in consumer prices for things like airline tickets, apartment rents, farm equipment, various types of financing, life insurance contracts, and even the price of cereal.


As regulators go about the important work of finalizing rules intended to address problems revealed by the financial crisis, it is critical that well-functioning aspects of these markets not be harmed. It is essential to preserve Main Street businesses' efficient access to these important risk management tools. We appreciate your attention to these concerns and look forward to continuing to support the subcommittee's efforts to ensure that derivatives regulations do not unnecessarily burden American businesses, jeopardize economic growth, or harm job creation.

Thank you for the opportunity to testify today and I am happy to address any questions you may have.

United States House of Representatives
Committee on Financial Services

“TRUTH IN TESTIMONY” DISCLOSURE FORM

Clause 2(g) of rule XI of the Rules of the House of Representatives and the Rules of the Committee on Financial Services require the disclosure of the following information. A copy of this form should be attached to your written testimony.

1. Name:	2. Organization or organizations you are representing:
Luke Zubrod	see attached
3. Business Address and telephone number:	
<div style="background-color: black; width: 100%; height: 40px;"></div>	
4. Have <u>you</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?	5. Have any of the <u>organizations you are representing</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?
<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets.	
See attached	
7. Signature:	
	

Please attach a copy of this form to your written testimony.

Supplement to "Truth in Testimony" Disclosure Form

Luke Zubrod

**March 16, 2011 Testimony before the Capital Markets Subcommittee of the
Financial Services Committee of the U.S. House of Representatives**

Question 2. Organizations you are representing: Coalition for Derivatives End-Users, Chatham Financial Corp.

Question 6. Grants or contracts awarded: Chatham Financial Corp. was awarded a service contract by the FDIC in June 2009, which is still in effect. To date, Chatham Financial Corp. has received payment in the total amount of \$495,500 in connection with that contract.