# Statement of the U.S. Chamber of Commerce

**ON:** Who's In Your Wallet? Dodd-Frank's Impact on Families, Communities and Small Businesses.

**TO:** U.S. House Subcommittee on Oversight and Investigations

**DATE:** July 19, 2012

The Chamber's mission is to advance human progress through an economic,
political and social system based on individual freedom,
incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations.

More than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, 70 percent of which have 10 or fewer employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross-section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business -- manufacturing, retailing, services, construction, wholesaling, and finance – is represented. Also, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the U.S. Chamber of Commerce's 115 American Chambers of Commerce abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross-section of Chamber members serving on committees, subcommittees, and task forces. More than 1,000 business people participate in this process.

Good Morning, Chairman Neugebauer, Ranking Member Capuano, Members of the Subcommittee, it is a pleasure to appear before you this morning. My name is Jess Sharp and I am Managing Director of the Center for Capital Markets Competitiveness at the U.S. Chamber of Commerce.

I am here today in my capacity with the Chamber; but, I am also here representing the Coalition for Derivatives End-Users, in which more than 300 end-user companies and dozens of trade associations have been active. We represent companies across the economy, both financial and non-financial, in the manufacturing, agricultural, energy, and other sectors, all united in one respect; they use derivatives to manage risk, not create it. Throughout the legislative and regulatory processes of the Dodd-Frank Act, the Coalition has advocated for strong regulation that brings transparency to the derivatives market and imposes thoughtful, new regulatory standards that enhance financial stability while avoiding needless costs on end users.

The diversity of the Coalition demonstrates the widespread use of derivatives by Main Street businesses, and helps drive home the real economic consequences of getting derivatives regulation wrong. Many U.S. companies maintain successful operations due in large part to a variety of risk management tools available through the use of derivatives. End-users currently use exchange trading, clearinghouses and over-the-counter (OTC) derivatives to help manage these risks.

For example, many auto manufacturers use derivatives to manage market risks such as foreign exchange, commodity, and interest rate risks resulting from the design, manufacture, sale and financing of vehicles. In manufacturing operations, derivatives are used to hedge currencies and commodities to lock in some near-term certainty for both revenues and costs from global vehicle production. For example, cars that are manufactured in Chicago, Illinois, are not only shipped to various states within the U.S., but are also exported to Canada, Mexico, and many other countries. Currency exposure that arises from production costs being in U.S. Dollars, and revenues in Canadian Dollars and Mexican Pesos, is hedged using foreign exchange swaps, forwards, and option contracts. OTC derivatives are also used to hedge commodities used in production such as aluminum and copper, while opting for long-term supply arrangements for some commodities that do not have a deep and liquid financial market. Many product and sourcing decisions are made years in advance of delivery.

Auto and other manufacturers also have large pension obligations to retired and deferred participants in the U.S. who depend on company pension funds for their retirement. These pension funds use derivatives to manage risk and mitigate funded status volatility that would be harmful to participants in the pension plans and to the

company. For example, one of the biggest risks faced by pension funds is interest rate risk. A one percentage point drop in interest rates can cause pension liabilities to increase by billions of dollars.

For other members of the Coalition, use of derivatives is driven by the desire to reduce commercial risk associated with their business. In the case of a bottle and can manufacturer, for example, the business involves buying billions of dollars of aluminum coils per year, converting those coils into cans and selling them to large beverage and food companies. As aluminum is an actively traded commodity, they are able to use OTC swaps to exactly match the prices and timing of when they buy coils of aluminum to when they sell the completed cans. This risk management technique allows companies to prudently manage their costs and reduce volatility of price changes during the manufacturing process as well as over the life of multi-year contracts.

For commercial businesses that rely on customer financing to sell their products, derivatives also play a large role in their day-to-day operations. Companies that sell large construction or agriculture equipment, for example, provide financing for their customers on a significant percentage of sales in both good and bad economic times that may involve both fixed and variable rate financing to meet the various long and short-term financing needs of customers. These companies issue debt in the commercial paper, medium term note, and asset-backed securitization markets to fund their loan and lease portfolios. Institutional debt investors purchase the majority of the debt securities, and the demand for these securities varies as economic conditions change. Derivatives enable these companies to match the interest rate characteristics of the funding available in the capital markets with the financing needs of their customers.

Energy company members of the Coalition also rely on derivatives because of the nature of the business of energy production and transmission. For example, in the case of electricity, it must be produced and consumed simultaneously, cannot be stored, and has exposure to volatile fuel markets in coal, natural gas, and uranium. Furthermore, electricity gets delivered to thousands of points along the grid at a moment's notice. Physical energy markets are volatile and unpredictable, but hedging with derivatives allows energy companies to manage these risks and provide thousands of customers with electricity and natural gas at a low fixed price.

These are just a few examples of how thousands of U.S. companies use derivatives in their businesses to provide products at low and fixed prices to millions of customers across the country. All Americans, including businesses as well as

consumers, benefit from the availability of derivatives as a way to manage commercial risk.

I'd like to take a moment to thank the Committee for its hard work in passing legislation in the House to address some of the unintended consequences of the Dodd-Frank Act and overreaching regulations put in place by regulators that threaten the ability of U.S. companies to use derivatives to manage their risk.

End-users are primarily concerned about proposed margin requirements, regulation of inter-affiliate trades, and the effectiveness of the clearing exception. In each of these three areas, we have seen strong bipartisan support for measures that would shield Main Street businesses from regulatory overreach.

H.R. 2682, which this committee approved unanimously, and the full House approved 370-24, creates a narrow, partial exemption from margin requirements for non-financial businesses that use derivatives in their commercial operations. Imposing unnecessary margin requirements on these end-users would divert working capital away from productive business use. Despite clear evidence that Congress did not intend for regulators to impose margin requirements on end-users, prudential banking regulators have proposed to do so, which would drain capital from the economy and eliminate jobs.

A survey by the Coalition found that imposing a 3% initial margin requirement on over-the-counter derivatives could cause the loss of 100,000 to 120,000 jobs and reduce capital spending by $5.1 to $6.7 billion within with the S&P 500 companies alone. The passage of H.R. 2682, in particular, helps protect Main Street from these huge cash calls that could become reality under proposed regulations.

H.R. 2779, which this committee also approved unanimously and the full House approved 357-36, prevents internal, inter-affiliate trades from being subject to regulatory burdens that were designed to be applied only to market-facing swaps and ensures that companies are not forced to abandon hedging through central risk-mitigation centers. These centers generate economic savings by allowing U.S. companies to manage commercial risk more effectively and secure better pricing for their derivatives trades—savings that companies can pass on to consumers or use to grow their business and create jobs. Without H.R. 2779, companies could be pushed towards using hedging methods that are riskier and less efficient

The overwhelmingly bi-partisan and collegial process that led to passage of H.R. 2682 and H.R. 2779 in the House demonstrates that the two bills provide noncontroversial approaches to helping grow business and improving the economy.

With regulatory compliance deadlines expected to begin in early fall for several CFTC regulations, the Coalition's concerns in these areas are more pressing than ever and have not been adequately addressed by regulation.

Ensuring that Congressional intent is followed by the CFTC and other regulators is critically important to the entire end-user community. We had hoped after passage of the Dodd-Frank Act that future legislation would not be required to address the concerns I have outlined here today. However, if legislation is not passed to clarify the statute's intent, end-users risk losing the ability to use derivatives to manage risk with the same cost-effective methods that they use today. It is important to remember that end-users rely on derivatives to reduce risk; bring certainty and stability to their businesses; and, ultimately to benefit their customers.

Thank you and I am happy to address any questions that you may have.