FMC Corporation

FMC Corporation
1735 Market Street
Philadelphia, PA 19103

215.299.6000 phone
215.299.5998 fax

www.fmc.com

Hearing before the Subcommittee on Capital Markets and Government Sponsored Enterprises – Committee on Financial Services

U.S. House of Representatives

Capitol Visitor Center - Room HVD-210
Washington, DC 20515

"Legislative Proposals to Enhance Capital Formation and Reduce Regulatory Burdens"

Testimony of Thomas C. Deas, Jr. – Vice President & Treasurer, FMC Corporation

April 29, 2015

Good afternoon Chairman Garrett, Ranking Member Maloney, and members of the Subcommittee. I am Thomas C. Deas, Jr., Vice President and Treasurer of FMC Corporation and Immediate Past-Chairman of the National Association of Corporate Treasurers, an organization of treasury professionals from several hundred of the largest public and private companies in the country. FMC and NACT are part of the Coalition for Derivatives End-Users (the "Coalition"). Our Coalition represents companies across the United States that employ derivatives to manage business risks they face every day. Hundreds of companies have been active in the Coalition, which has sought financial regulation that promotes economic stability and transparency without imposing undue burdens on derivatives end-users. I am also privileged to serve as the Immediate Past-Chairman of the International Group of Treasury Associations of which NACT along with the national treasury organizations of approximately 30 other countries are a part. Our message is straightforward: financial regulatory reform measures should promote economic stability and transparency without imposing undue burdens on derivatives end-users. For U.S.-based multinational companies, the need for international harmonization of derivatives rules is especially important. Thank you very much for giving me the opportunity to speak with you today about the impact of derivatives regulation on end-user companies.

End-Users' Concerns with Derivatives Regulation

The Coalition supports your efforts to oversee the implementation of the Dodd-Frank Act. We very much appreciate the strong bipartisan efforts by the Members of the Committee on Financial Services and this Subcommittee on behalf of American companies who use derivatives to manage many of the risks they face in running their businesses every day. The Coalition's several hundred members remain very appreciative of the bipartisan effort many of you led that resulted in January of this year in legislative relief for end-users from mandatory posting of initial and variation margin requirements for the derivatives positions of eligible end-users.

We support your efforts to redress problems with derivatives experienced during the financial crisis in 2008. End-users like FMC use derivatives to reduce risks arising from operating our businesses and do not engage the kind of risky speculative derivatives transactions that roiled the markets during the financial crisis. End-users comprise less than 10 percent of the total over-the-counter ("OTC") derivatives market and do not meaningfully contribute to systemic risk. The Coalition is gratified by the broad consensus that end-users should not be subject to regulations designed to reduce the risk of those who maintain derivatives positions that could pose risk to the financial system.

However, at this point over four-and-a-half years after passage of the Dodd-Frank Act, there are several areas where continuing regulatory uncertainty compels end-users to appeal for legislative relief from actions we believe will raise costs unnecessarily and hamper our ability to manage business risks with properly structured OTC derivatives. Among several areas of concern, I would like to invite your attention to three areas relating to cross-border transactions and international competiveness, particularly for U.S.-based multinational companies.

- Centralized Treasury Units engaging in inter-affiliate and external-facing derivatives transactions;
- Capital requirements for derivatives transactions; and
- Cross-border concerns.

<u>Centralized Treasury Units Engaging in Inter-affiliate Derivatives Transactions</u>

Throughout the legislative and rulemaking processes surrounding the Dodd-Frank Act, the Coalition has advocated for strong regulatory standards that enhance financial stability while avoiding needless costs. Many non-financial end-users utilize centralized treasury units ("CTUs") as a risk-reducing, best practice to centralize and net the hedging needs of affiliates. In fact, nearly half of the respondents to a survey of end-users by the Coalition use CTUs to execute OTC derivatives.

While the CFTC has recognized the undue burdens clearing requirements would place on corporate end-users that utilize this best practice and has attempted to ease these burdens through no-action relief, this well-intended relief is inadequate. In particular, many corporations are uncomfortable relying on no-action relief, because that relief only stipulates that agency staff will not undertake enforcement action for violations of the law; it does not change the law. In Europe, CTUs are not treated as financial entities. Consequently, European law does not apply clearing and other such requirements to CTUs of non-financial end-users.

Treasurers of non-financial end-users who operate CTUs that serve the risk-mitigating function of aggregating exposures on the books of a special-purpose subsidiary within their corporate group, netting the inter-affiliate exposures, and then entering into smaller derivatives with a bank or other swap dealer for the net amounts, could have to wind down those efficient units or meet burdensome new regulatory requirements that will be hard to justify. The alternative would be to retain more risk. This is because, as financial entities, these CTUs could be denied the end-user clearing exception despite the fact that they are only executing trades for non-financial end-user affiliates, which themselves, would otherwise be able to elect the end-user clearing exception.

The Coalition strongly supports H.R. 1317, which would clarify that certain swaps entered into with a CTU hedging the commercial risk of a non-financial affiliate are eligible for the end-user exemption from mandatory clearing and the requirement to post margin for their derivatives positions. This would also free CFTC staff from having to monitor end-users' compliance with the no-action guidance they had to update most recently on November 26, 2014.

Capital Requirements for Derivatives Transactions

With your help, end-users could successfully navigate the many regulatory issues we still face, only to find that the uncleared OTC derivatives we seek to continue using have become too costly because of much higher capital requirements. The Prudential Banking Regulators have now finalized rules implementing Basel III capital requirements which increase the capital bank counterparties would have to hold against derivatives in anticipation of a possible future deterioration in the financial markets such as that experienced in 2008. Additionally, anticipated bank capital measures, including the liquidity coverage ratio and net stable funding ratio, will further increase derivatives transaction pricing for end-users.

European policy makers have implemented capital charges on derivatives positions significantly more favorable to end-users than the U.S. Prudential Banking Regulators. Their approach is to recognize that end-users' hedging activities are in fact reducing risks; and so, should require less capital than activities of financial entities keeping open positions or making markets in derivatives. They intend to exempt non-financial end-users from certain of the additional capital requirements. The absence of a U.S. exemption could put American companies at a meaningful competitive disadvantage compared to our European competitors.

In summary, we believe the legislative intent of the Dodd-Frank Act was to exempt end-users from having to use their own capital for mandatory margining of derivatives transactions, diverting these funds from investment in business expansion and ultimately costing jobs. The imposition of additional capital requirements by U.S. Prudential Banking Regulators would undermine this intent by forcing our bank counterparties to hold much more of their own capital in reserve against end-users' derivatives positions, passing on the increased costs to these end-users.

Cross-Border Concerns

The Coalition appreciates the important efforts being undertaken by U.S. and foreign regulators to resolve differences in how their regulations apply to cross-border transactions. Applying derivatives reform rules in a global marketplace is an inherently complex undertaking. Unlike most stock market transactions, derivatives create an ongoing relationship between parties that is not severed once the transaction has been consummated. Thus, many transactions exist between parties in different jurisdictions for many years. While the United States has completed many of its derivatives rules first, other regulators around the world – particularly those in Europe – are just now finalizing and implementing many of their rules. Consequently, derivatives end-users now find themselves simultaneously subject to multiple regulatory regimes. Understanding and implementing compliance structures for derivatives rules across multiple jurisdictions is a significant and costly undertaking. Accordingly, end-users are subject to incentives to avoid complication by limiting their transactions to counterparties located in their same jurisdiction. The lack of regulatory harmonization can cause fragmented and less efficient markets for end-users, and can raise the cost of delivering stable prices to consumers. It is critical that U.S. regulators continue to work closely with their foreign counterparts and move quickly to recognize equivalency and substituted compliance with foreign regulatory regimes when the objectives of foreign regulations are comparable to those under the Dodd-Frank Act and where foreign regulations do not unduly burden end-users.

Summary

Let me take a moment to summarize our principal concerns with the application of derivatives regulation to end-users:

- First, the imposition of clearing and margining requirements on CTUs that execute swaps on behalf of non-financial affiliates threatens to deny those companies the benefits of risk-reduction by netting out opposite-way trades and entering into smaller derivatives with their bank counterparties. This practice is considered overwhelmingly by treasurers of U.S.-based multinational companies to be the best and most efficient practice.
- Second, despite the legislative fix that now clearly exempts end-users from margining requirements, we still have the risk that the banking regulators will require excessive capital be held in reserve against uncleared over-the-counter derivatives – with the cost passed on to end-users as they attempt to manage their business risks. The unintended consequence of punitive capital requirements could be for some end-users to cease hedging risks or to pay hedging costs that put them

at a disadvantage against foreign competition operating where end-user exemptions have been made more effective.

- Finally, international harmonization is of great importance and is particularly relevant for derivatives end-users, as many have affiliates located across the globe in several different jurisdictions. Inconsistencies lead to increased costs, confusion and duplication that could lead end-users to abandon efficient hedging practices or cause them not hedge at all. In your oversight of the implementation of the Dodd-Frank Act, we urge you to encourage U.S. regulators to continue to work with foreign regulatory regimes to recognize equivalence between jurisdictions using an outcomes-based analysis.

Conclusion

Thank you again for the opportunity to testify today on these important issues.

We are very concerned that the regulatory burden on end-users of derivatives will result in higher costs to Main Street companies that will limit their growth, harm their international competitiveness, and ultimately hamper their ability to sustain and, we hope, grow jobs.

The consequences of getting derivatives regulation wrong will be borne by American business and ultimately our customers.

I will do my best to respond to any questions you may have.