

**From:** Dorothy Coleman <DColeman@nam.org>  
**Sent:** Thursday, August 19, 2010 11:43 AM  
**To:** dfadefinitions <dfadefinitions@CFTC.gov>  
**Subject:** NAM: Preliminary Comments on Derivatives Regulation  
**Attach:** DColeman Ltr to The Honorable David A. Stawick 8-19-10 \_2\_.pdf; Picture (Device Independent Bitmap) 1.jpg

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Mr. Stawick: attached please find NAM's preliminary comments on CFTC's proposed rule-making on title VI of the Dodd-Frank legislation. Please give me a call if you have any questions. Regards DC

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August 19, 2010

The Honorable David A. Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Center  
1155 21st Street, NW  
Washington, DC 20581

**VIA ELECTRONIC MAIL**

Initial Comments on OTC Derivatives Rulemaking

Dear Mr. Secretary:

The National Association of Manufacturers (NAM)—the nation's largest industrial trade association—is pleased to submit our initial comments to the Commission regarding implementation of the new rules on over-the counter (OTC) derivatives in the Dodd-Frank Act. As end-users of OTC derivatives to manage risk, American manufacturers have a strong interest in the implementation of these provisions.

**Overview**

With the U.S. economy still in recovery mode, it is critical that any new regulations on derivatives not inadvertently harm economic growth. For example, rules that impose margin requirements on manufacturers or that impose financial regulation (such as a Swap Dealer or Major Swap Participant) on non-financial businesses, could seriously harm the recovery by diverting companies' financial resources from much-needed business investment and job retention and creation.

Similarly, regulations that make hedging too expensive will place manufacturers in the uncomfortable position of either having to divert additional money away from production, or discontinue hedging business risk, which would require liabilities to reappear on corporate balance sheets, driving up the cost of capital.

Manufacturers encourage the Commission to act carefully to avoid these consequences. We look forward to commenting further when rules are proposed. In the meantime below we have identified some areas with the potential to most egregiously harm America's manufacturers if not implemented narrowly and with great care.

### **Definition of Major Swap Participant (MSP)**

It is crucial that new regulations on derivatives include a strong and workable exemption for end-users, like manufacturers, that use derivatives to hedge commercial risk. Failing to preserve this exemption could cost U.S. companies millions, and in some cases, cases, billions of dollars and limit their ability to drive job growth. The definition of MSPs is the lynch-pin of the end user exemption.

NAM members feel strongly that, in drafting rules on the MSP definition, the Commission should ensure that business end-users, like manufacturers, are not deemed to be major swap participants. Similarly, the rules should preserve the exemption from the MSP definition for captive finance affiliates that use derivatives to hedge underlying commercial risks related to interest rate and foreign currency exposures. In addition, regulations should support the provisions in the final legislation that positions held by pension plans to manage risk are not considered in determining whether an entity is an MSP.

**Substantial Position:** The term “substantial position” is an important feature of the definition of MSP. In order to clarify that the definition of MSP does not capture companies that are commercial end-users, we urge the Commission to interpret “substantial” on a net basis and with regard to whether the market participant’s positions create significant systemic risk. As the legislation states, “substantial position” is meant to ensure that the Commission can monitor entities whose outstanding, uncollateralized or poorly collateralized positions “are systemically important or can significantly affect the financial system of the United States.” It should be expected that the number of non-financial businesses that meet this test is extremely small.

### **Definition of Swap Dealer**

Manufacturers are concerned that a broad definition of “swap dealer” could make end-users ineligible for the exemption if they hedge business risks in the ordinary course of business. We urge the Commission to clarify, through the rule-making process, that the definition of “swap dealer” does not include companies whose primary business is that of a commercial end-user. In addition, the Commission should exclude from the definition of swap dealer any commercial end-user that enters into swaps with its customers for its own account, but not as its primary business, as long as those swaps, on a net basis, do not comprise a substantial portion of its business. It should be clarified that this de minimis exception applies broadly with respect to customer transactions related to a non-financial company’s ordinary business.

### **Capital and Margin Requirements for Non-Banks:**

Under the new legislation, margin and capital requirements are imposed on swap dealers but not their commercial end-user counterparties. Nonetheless, manufacturers are concerned that these additional costs imposed on end-user transactions will be passed on to commercial end-users. NAM members urge regulators to draft rules that base capital charges on swap dealers on actual risk of loss and promoting the safety and soundness of the financial system, rather than using capital charges as incentives to centrally clear transactions, or

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otherwise penalize OTC derivatives. If capital and margin requirements on swap dealers are too high, the clearing exemption for end-users will become uneconomic and meaningless.

**Grandfathering:** Manufacturers urge regulators to reaffirm that the law does not apply to existing contracts with respect to margin requirements.

### Clearing

**End-User Exception:** Manufacturers support provisions in the legislation that exempt commercial end-users from the clearing requirement if they are not major swap participants and they use swaps to hedge commercial risk or if they are captive financing affiliates that provide financing for customers of the parent company and use swaps to mitigate risk. In addition, to be eligible for the exception, end-users must demonstrate how they meet their financial obligations associated with entering non-cleared swaps, in a manner set forth by the Commission.

In drafting these rules, we urge the Commission to define "commercial risk" broadly to encompass the many ways derivatives are currently used by non-financial businesses. For instance, hedging in ways that are indirect or not perfect are nevertheless important means for corporate risk managers to manage balance sheets. The Commission should acknowledge that any hedge directly or indirectly related to the operations of a company is a legitimate end user activity.

### Conclusion

The issues identified above are some of many that will impact the way America's manufacturers hedge their commercial risk. In order to ensure minimal disruption of legitimate business activity, and to ensure that capital is directed towards hiring, research and economic expansion, we respectfully request the Commission to proceed cautiously and with an eye to the impact of its rulemaking on non-financial companies. Thank you once again for your leadership on this issue.

Sincerely,

A handwritten signature in black ink that reads "Dorothy Coleman". The signature is written in a cursive style with a large, looped initial "D".