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COMMITTEE ON CORPORATE TREASURY

February 14, 2012

The Honorable Ben Bernanke
Chairman
Board of Governors of the Federal Reserve
20th Street and Constitution Avenue
Washington, DC 20551

The Honorable Martin Gruenberg
Acting Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

The Honorable Mary Schapiro
Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

The Honorable John Walsh
Acting Comptroller of the Currency
250 E Street, SW
Washington, DC 20219

The Honorable Gary Gensler
Chairman
Commodities and Futures Trading Commission
1155 21st Street, NW
Washington, DC 20581

Re: Prohibitions and Restrictions on Proprietary Trading and Certain Interests in and Relationships With, Hedge Funds and Private Equity Funds

Dear Chairman Bernanke, Acting Chairman Gruenberg, Chairman Schapiro, Acting Comptroller Walsh, and Chairman Gensler:

I am writing on behalf of Financial Executives International's Committee on Corporate Treasury (CCT) to express concern that the Volcker rule, as proposed, could have a negative impact on the markets that corporate treasurers from non-financial companies rely on for financing, raising capital, and hedging risk. The result of the proposed rule could adversely affect the ability of American businesses to grow, create jobs, and contribute to a healthy economic recovery.

Financial Executives International (FEI) is a professional association representing the interests of more than 15,000 chief financial officers, treasurers, controllers, tax directors, and other senior-level financial executives from over 8,000 major companies throughout the United States and

Canada. FEI's CCT formulates policy positions regarding treasury matters for FEI in line with the views of the membership and when appropriate, works to educate relevant policymakers and regulators on issues impacting corporate treasurers.

There is no question that the financial crisis and credit freeze was a massive problem for all market participants, and that systemic risk needed to be addressed to prevent the significant ripple effects seen in 2008 from occurring again. However, we are concerned that the rule, as proposed, has some unintended and undesirable consequences for non-financial companies. Our concerns center around the following three areas:

- Overall market impact and cumulative regulatory effects;
- Reduced liquidity and increased costs in the corporate bond market; and
- Availability to hedge risk in derivatives market.

<u>Overall Market Impacts and Cumulative Regulatory Effects</u>

The Volcker rule will directly impact banks and financial dealers that play an important role in providing liquidity for businesses accessing commodities, securities, and derivatives markets. As a result of the added cost and complexity of the proposed rule, financial entities may reduce their activity in, or pull out of, the markets businesses access to raise capital, creating fewer choices and driving up costs for non-financial companies. Less liquidity in the marketplace could mean that corporate treasurers would have to maintain greater excess cash instead of investing in business expansion and job creation, limiting overall economic growth.

In the wake of the financial crisis, financial institutions are not the only entities that must comply with a new regulatory regime, as corporate treasurers from non-financial companies will also have to adjust to a new regulatory landscape which comes with significant direct and indirect costs. Corporate treasurers face the potential liquidity impact of the proposed Volcker rule, and they will also feel the increased cost that will likely be passed on as a result of this proposed rule. Moreover, this impact comes over and above the increased costs resulting from new Basel III bank capital requirements.

Corporate treasurers are also faced with an additional direct impact on liquidity management as regulators consider further reforms to money market funds, which will affect how companies manage short term financing and investment. Some of the proposed money market reforms are likely to have a significant impact on demand for commercial paper, which will adversely impact another important borrowing source. As capital markets funding becomes more difficult and more expensive, this may lead to lower diversification among corporate borrowing sources. This will leave corporate borrowers more dependent on key banks thereby magnifying large banks' impact on the overall economy. As concerns have been expressed with the "too big to fail" status of some lending institutions, it seems counter-productive to increase regulations that will lead to disintermediation between corporate borrowers and the broader capital markets.

Furthermore, as the rules surrounding the regulation of the over-the-counter derivatives market have been proposed by the prudential regulators, corporate treasurers that use swaps to hedge business risk may also find themselves faced with margin requirements that could divert funds away from business investment. As the margin rules are finalized, there should be coordination in the final rulemaking process whereby end-users hedging legitimate business risk would not be subject to regulatory imposed margin requirements that would add further burden for corporate treasurers.

Aside from the overall reduction in liquidity and compliance costs that will affect non-financial companies, we are concerned with targeted impacts to the corporate bond and derivatives markets.

Reduced Liquidity and Increased Costs to Corporate Bond Market

Corporate bonds are debt securities issued by companies that allow them to finance investments in the business such as expanding into new plants, purchasing equipment, and developing new products, all of which are activities that contribute to strong economic growth. Reducing liquidity and access to this market could increase the costs of borrowing and would have a disproportionate impact on lower-rated bonds, often issued by smaller companies.

Banking entities play an important role in the corporate bond market, essentially serving as the supporter and facilitator, stepping in to take on risk when necessary. The corporate bond market will be affected by the proposed Volcker rule as financial dealers may be prohibited or deterred from taking on the inventory and risk associated with supporting and facilitating the market, creating new costs for investors and issuers alike. According to a recent study by Oliver Wyman, reducing liquidity in the market as a result of the proposed rule could cost investors up to $315 billion in mark-to-market loss of value on their existing holdings, and up to an additional $4 billion in annual transaction costs, while corporate issuers could be facing "$12 to 43 BN per annum in borrowing costs over time, as investors demand higher interest payments on the less liquid securities they hold[1]". Corporate issuers could be faced with higher yields on new debt if banking entities are restricted from serving as the market-makers for these debt securities.

Not all issuers are created equal, and as such, reduced liquidity will have a disproportionate impact on lower-rated bonds, usually raised by smaller corporations with higher debt burdens.

[1] OLIVER WYMAN, "The Volcker Rule Restrictions on Proprietary Trading Implications for the U.S. Corporate Bond Market," SIFMA. December 2011.

Banking entities supporting the corporate bond market may not be able to play a significant role in the market except for supporting the highest quality investment grade bonds that will likely have the most investor demand. The lower rated bonds belonging to smaller corporations may find themselves shut out of the market, or if able to participate, at the peril of substantially higher costs.

With increased costs, the number of active market participants is likely to decline, reducing pension funds and other investors' access to corporate debt securities.

Availability to Hedge Risk in Derivatives Market

We believe an overly restrictive final Volcker rule may also have unintended consequences for companies who utilize derivatives to hedge business risk. As proposed, the Volcker Rule may restrict the ability of financial entities to take on the various transactions that non-financial companies seek to hedge their business risk. Risk mitigation is an important component to the corporate treasury function, but without a willing banking entity or counterparty to take on the transaction, the risk is left on the company's balance sheet.

Some derivatives transactions can remain in place for a long period of time, and in some cases there may not be an exact offsetting transaction for the dealer to make if an end-user comes to them with a custom hedge. The final Volcker rule must allow for these instances to ensure companies can continue to legitimately hedge risk through derivatives.

Conclusion

When crafting the final Volcker rule, regulators should take sufficient time to thoroughly consider the impacts non-financial companies may bear. While the Volcker rule does not have direct impact, reduced liquidity affects all market participants, including corporate treasurers utilizing these markets for financing, liquidity management, capital formation, and risk management activities.

Sincerely,

Teri L. List-Stoll

Teri L. List-Stoll
Chair, Committee on Corporate Treasury
Financial Executives International