August 1, 2023

The Honorable Jerome Powell
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Prohibition Against Conflicts of Interest in Certain Securitizations

Dear Chair Powell:

We are writing to ensure you are aware of the Securities and Exchange Commission's (SEC) Conflict of Interest proposal[1] and are working directly with the SEC to address concerns on how it might impact the ability of companies that fall under the agency's purview to adequately manage risk.

The SEC is in the process of implementing a provision of the Dodd-Frank Act that would significantly increase the difficulty, burden, and cost of basic risk mitigating activities, including interest rate hedging. Section 621 of Dodd-Frank mandates the SEC to "prohibit material conflicts of interest between those who package and sell asset-backed securities and those who invest in them."[2] However, the proposed rule is much broader than the law intends, and we are concerned that the re-purposed rule exceeds the original intent of Congress and fails to accomplish the goal of preventing conflicts of interest while ensuring the healthy functioning of Asset Backed Security (ABS) markets.

This re-proposal has several severe consequences – including potentially disallowing bona fide capital markets capital raising, risk management, hedging, and investment opportunities. The rule introduces broad prohibitions impacting the continuation of routine market activities and would encompass a wide range of market participants and institutions, many who may have limited or no connection to the relevant securitization. The recent failures of Silicon Valley Bank (SVB), First Republic, and Signature Bank can partly be attributed to a lack of adequate hedging strategies, strategies which are absolutely necessary for financial institutions to handle normal market risk.

On March 28, 2023, Federal Reserve Vice Chair for Supervision Michael Barr testified before the Senate Banking, Housing and Urban Affairs Committee that a contributing factor to SVB's failure was that "the bank did not effectively manage the interest rate risk of those securities or develop effective interest rate risk measurement tools, models, and metrics." It is not often that, as policymakers, we are given a glimpse into the future of the unintended consequences of our decisions. However, in this case, SVB failed partly because it did not appropriately hedge its

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[1] https://www.sec.gov/rules/proposed/2023/33-11151.pdf
[2] https://www.sec.gov/spotlight/dodd-frank-section.shtml#621

interest rate risk. We expect our regulators to help safeguard the stability of our financial institutions, and hope you are already working with the SEC to prevent a repeat of recent history.

We strongly urge you to work directly with SEC Chair Gary Gensler and his staff to address consequential market concerns on how the rule will impact the ability of companies you regulate to properly and effectively and manage risk. We respectfully request a written response by August 15, 2023 describing your agency's coordination with the SEC as it pertains to the Conflicts of Interest Rule. Thank you for your attention to this matter.

If you have any questions, please do not hesitate to reach out to Megan Guiltinan (Megan.Guiltinan@mail.house.gov) in Rep. Barr's office or Zach Gates (Zach.Gates@mail.house.gov) in Rep. Wagner's office.

Sincerely,

Andy Barr
Chairman
Subcommittee on Financial Institutions and Monetary Policy
House Financial Services Committee

Ann Wagner
Chairman
Subcommittee on Capital Markets
House Financial Services Committee

CC: Mr. Gary Gensler, Chair, U.S. Securities and Exchange Commission