AMERICANS for PROSPERITY

March 29, 2023

The Honorable Patrick McHenry Chairman House Financial Services Committee	The Honorable Maxine Waters Ranking Member House Financial Services Committee

Dear Chairman McHenry and Ranking Member Waters:

I write on behalf of millions of Americans for Prosperity (AFP) activists across the country concerning the recent collapse of Silicon Valley Bank (SVB) and Signature Bank. We applaud the committee's decision to bring Chairman Gruenberg, Vice Chair of Supervision Barr, and Under Secretary Liang before the committee to better understand the events that unfolded surrounding the failures of SVB and Signature Bank. While there are still many unknowns regarding the details around these failures, we believe it's important for policymakers to be aware of what factors we know contributed to these failures, and others we know were not a factor. Understanding these details is important to avoid any rash policy responses that could burden rather than benefit America's banks and customers.

Some have claimed that the Economic Growth, Regulatory Relief, and Consumer Protection Act (S. 2155) which passed during the 115th Congress, was responsible for the collapse of SVB. This legislation garnered strong bipartisan support with a focus on tailoring and right-sizing regulations for community and regional banks. Some have pointed to Title IV of S. 2155 as the culprit behind the recent failures, claiming it rolled back certain regulatory requirements for mid-sized banks, such as those related to liquidity requirements.[1] However, S. 2155 left in place supervisory stress testing of financial institutions with assets between $100 billion and $250 billion while simply allowing the Federal Reserve the discretion to apply individual enhanced prudential provisions. To that end, in 2019 the Federal Reserve exercised this discretion by putting in place enhanced internal liquidity stress testing of SVB, over and above the statutory requirement.

Recent evidence suggests the strict regulations critics claim would have prevented SVB's failure would not have been successful in doing so. For example, recent analysis shows that SVB would likely have been subject to a modified liquidity coverage ratio (LCR) and that it would have met the requirements for that test.[2] In fact, the very long-term Treasury securities that exposed SVB to interest-rate risk are precisely the type of asset typically considered safe. These enhanced regulations of the LCR would not have kept SVB from failure.

It also appears unlikely the Federal Reserve's "stress tests" would have set off any alarms. According to experts, the annual stress test scenarios did not account for dramatic increases in interest rates.[3] Because SVB's exposure to interest-rate risk was a main factor in its failure, this would make these stress test scenarios potentially moot.

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[1] https://www.warren.senate.gov/newsroom/press-releases/warren-porter-dozens-of-democratic-lawmakers-introduce-bill-to-repeal-2018-rollback-of-critical-dodd-frank-protections
[2] https://bpi.com/silicon-valley-bank-would-have-passed-the-liquidity-coverage-ratio-requirement/
[3] https://www.wsj.com/articles/stress-testing-wouldnt-have-saved-silicon-valley-bank-fomc-federal-reserve-treasury-bank-run-signature-bank-1573ab77

There is still much to be learned about the events and circumstances that led to SVB's collapse. However, it has become apparent there were serious failures from both bank management and federal and state regulators. The rapid growth SVB experienced over the past few years should have been a red flag for supervisors. In 2018, SVB had $49 billion in deposits which skyrocketed to $189 billion in 2021 largely stemming from start-ups and venture capitalists.[4] As deposits flowed in, SVB invested in long-term Treasury securities. Unfortunately, as the Fed began to raise the Fed Funds Rate to counter inflation in part fueled by the Administration's misguided fiscal policies, SVB became highly exposed to interest-rate risk because of the large amount of assets it had invested those long-term securities. These factors, coupled with the bank having 93 percent of its deposits uninsured by the Federal Deposit Insurance Corporation (FDIC), ultimately led to the first Twitter fueled bank run as it experienced $42 billion in withdrawals in a matter of hours.[5] Regardless of what regulations were in place, many of these points should have alarmed federal and state regulators.

SVB's precarious financial position was not unknown to regulators and even those in the private sector. In Vice Chair of Supervision Barr's testimony released prior to the March 28th Senate Banking hearing, he recalls "six supervisory findings related to the bank's liquidity stress testing, contingency funding, and liquidity risk management."[6] According to his testimony, this occurred near the end of 2021. Reports also indicate that last November, JPMorgan raised concerns about the risks associated with SVB's unrealized losses.[7] Yet, despite SVB's poor financial position being widely known months and even years in advance, it still failed.

For policymakers and the public to better understand how they should proceed, it is imperative that Congress conduct thorough oversight. Americans for Prosperity encourages Members of Congress to consider questions along these lines to better understand what went wrong and why: 1) Inquire what information regulators knew about SVB's financial position, a timeline of those events, and why that process ultimately failed 2) Explain why instead of finding private market solutions, regulators rushed to invoke the systemic risk exception and 3) Explain whether or not regulators considered the harm to small and mid-sized banks and their customers and the potential for additional future risk introduced into the banking system through the resolution actions taken by regulators.

We applaud the committee for organizing this important oversight hearing. Americans for Prosperity and its millions of activists stand ready to help strengthen America's banks to help better serve their customers.

Sincerely,

Brent Gardner
Chief Government Affairs Officer
Americans for Prosperity

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[4] https://www.nytimes.com/2023/03/10/business/silicon-valley-bank-stock.html
[5] https://www.washingtonpost.com/business/2023/03/15/svb-billions-uninsured-assets-companies/
[6] https://www.federalreserve.gov/newsevents/testimony/barr20230328a.htm
[7] https://nypost.com/2023/03/12/jpmorgan-analysts-warned-about-silicon-valley-banks-16b-in-unrealized-losses-in-november/