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United States Senate

COMMITTEE ON COMMERCE, SCIENCE,
AND TRANSPORTATION

WASHINGTON, DC 20510-6125

WEBSITE: <https://commerce.senate.gov>

March 16, 2023

Ms. Mary Daly
President and Chief Executive Officer
Federal Reserve Bank of San Francisco
101 Market Street
San Francisco, CA 94105

Dear President Daly:

As the Ranking Member of the U.S. Senate Committee on Commerce, Science, and Transportation (“Committee”), which has broad jurisdiction over the technology companies that made up the majority of customers for Silicon Valley Bank (“SVB”), I write regarding the failure of the Federal Reserve Bank of San Francisco (“SF Fed”) to properly supervise SVB despite the obvious risks SVB faced as interest rates soared. The SF Fed’s failure to properly examine and supervise SVB, in turn, led to SVB’s quick collapse and the Biden administration’s decision to grant a taxpayer bailout to SVB’s tech firm clients and their wealthy founders. I seek to understand how the SF Fed missed so many obvious warning signs about SVB’s lax risk management practices.

The three primary reasons behind SVB’s collapse are well known. First, SVB purposefully concentrated its customer base with technology startups and the venture capital firms supporting them. SVB claims to be “the financial partner of the innovation economy” and its website touts that “nearly half” of “US venture-backed technology and life science companies bank with SVB.”¹ Technology startups are notorious for being unprofitable and quickly burning through cash.² While interest rates were kept artificially low over the past 15 years under the Federal Reserve’s exceptionally accommodative monetary policy, the tech industry boomed and SVB’s customers raked in cash.³ As a result, SVB received a deluge of deposits that “tripled in a two-year span to \$189 billion.”⁴ Second, according to SVB’s recent regulatory filings, more

¹ Global, SVB (accessed on Mar. 14, 2023), available at www.svb.com/global.

² Eric Rosenbaum, *What Comes After the Easy Money Era Ends for Cash-Burning Tech Companies in Silicon Valley*, CNBC (May 19, 2022), available at <https://www.cnbc.com/2022/05/18/what-comes-after-easy-money-era-ends-for-cash-burning-tech-companies.html>; Matt Phillips, *Behind Silicon Valley Bank’s Sudden Rush for Cash*, AXIOS (Mar. 10, 2023), available at <https://www.axios.com/2023/03/10/behind-silicon-valley-banks-sudden-rush-for-cash>.

³ Rosenbaum, *supra* note 2.

⁴ Ben Foldy et al., *How Silicon Valley Turned on Silicon Valley Bank*, THE WALL STREET JOURNAL (Mar. 12, 2023), available at <https://www.wsj.com/articles/how-silicon-valley-turned-on-silicon-valley-bank-ee293ac9>.

than 96% of its deposits were uninsured.⁵ That meant that the bank’s customers were prone to rapidly withdraw cash upon the first sign of trouble.⁶ Third, SVB purchased “huge amounts” of long-dated government securities immediately before the Federal Reserve began raising interest rates.⁷ The interest rate hikes led to “big losses” in SVB’s investments,⁸ earning SVB the unenviable title of the bank with the highest securities portfolio as a percentage of total assets.⁹ In sum, these risks made SVB ripe for a run.

Indeed, these risks were apparently “lurking in plain sight” long before SVB went under.¹⁰ SVB recorded its rapid rise and deposits on its balance sheets, and its increasing losses on bond holdings were “evident” in the notes to its financial statements.¹¹ Such “[r]apid growth,” according to Daniel Tarullo, a former Federal Reserve governor, “should always be at least a yellow flag for supervisors.”¹² Moreover, according to Timothy Coffey, associate director of depository research at Janney Montgomery Scott LLC, “regulators were aware that unrealized losses in banks’ securities portfolios could lead to trouble, but didn’t take specific steps to address the issue.” And apparently analysts “have been publicly screaming about these very issues for many, many months.”¹³ That is why one Brookings Institution scholar exclaimed that he was “at a loss for words to understand how [SVB’s] business model was deemed acceptable by their regulators”—that’s the SF Fed.¹⁴

The SF Fed’s failure to address SVB’s obviously risky structure is frankly shocking. As you know, one of the central purposes of the Federal Reserve system is to promote the safety and soundness of financial institutions. It employs a team of over 400 economists, including dozens in the supervision and regulation division.¹⁵ The SF Fed, in particular, has a dedicated fintech

⁵ As of December 31, 2022, SVB held \$173.1 billion in deposits. “[T]he amount of estimated uninsured deposits in U.S. offices that exceed the FDIC insurance limit were \$151.5 billion...[with]...foreign deposits of \$13.9 billion ... [that]...were not subject to any U.S. federal or state deposit.” SVB, Annual Report (Form 10-K) (Feb. 24, 2023), available at <https://www.sec.gov/Archives/edgar/data/719739/000071973923000021/sivb-20221231.htm>.

⁶ Ben Eisen & Andrew Ackerman, *Where Were the Regulators as SVB Crashed?*, THE WALL STREET JOURNAL (Mar. 11, 2023), available at <https://www.wsj.com/articles/where-were-the-regulators-as-svb-crashed-35827e1a>.

⁷ Emily Flitter & Rob Copeland, *Silicon Valley Bank Fails After Run on Deposits*, THE NEW YORK TIMES (Mar. 10, 2023), available at <https://www.nytimes.com/2023/03/10/business/silicon-valley-bank-stock.html>.

⁸ Andrew Barry, *How SVB Was Doomed By a Bad Bet on Mortgage Securities and the Fed’s Rate Hikes*, BARRON’S (Mar. 11, 2023), available at <https://www.barrons.com/articles/svb-silicon-valley-bank-rates-securities-693c931c>.

⁹ *Dissecting Recent Bank Failures*, LPL Research (accessed on Mar. 15, 2023), available at [https://lplresearch.com/2023/03/13/dissecting-recent-bank-failures/#:~:text=SVB%20Financial%20Group%20\(SIVB\)%20was,67.4%25%2C%20and%2060.4%25](https://lplresearch.com/2023/03/13/dissecting-recent-bank-failures/#:~:text=SVB%20Financial%20Group%20(SIVB)%20was,67.4%25%2C%20and%2060.4%25).

¹⁰ Eisen & Ackerman, *supra* note 6.

¹¹ *Id.*

¹² *Id.*

¹³ Christopher Rugaber & Fatima Hussein, *Fed Criticized for Missing Red Flags before Bank Collapse*, ASSOCIATED PRESS (Mar. 14, 2023), available at <https://apnews.com/article/federal-reserve-silicon-valley-bank-regulation-609bde9b9248fbc590ff98775e0c8d49>.

¹⁴ *Id.*

¹⁵ *Meet the Economists*, Federal Reserve (accessed on Mar. 15, 2023), available at <https://www.federalreserve.gov/econres/bsrstaff.htm>.

team.¹⁶ And until March 10, 2023 SVB’s CEO served on the board of the SF Fed.¹⁷ The SF Fed had all of the resources and information necessary to properly supervise SVB, yet it spectacularly failed to do so.

Instead of fulfilling its statutory mandate to supervise SVB, the SF Fed has been distracted with engaging in politically-charged research and advocacy on environmental, social, and governance (“ESG”) and diversity, equity, and inclusion (“DEI”) topics, like global warming and racial justice.¹⁸ Recent academic research has shown that Federal Reserve regional banks, including the SF Fed, have increasingly engaged in research on activist topics (i.e., climate, race, gender, and inequality).¹⁹ In fact, this research, which was conducted by academics at the University of Pennsylvania and Haverford College, found that the SF Fed was one of the regional banks publishing the most on activist topics, especially on global warming issues.²⁰ This woke mission creep was evident on the front page of the SF Fed’s website on March 13, 2023, the day after the Biden administration announced its bailout of SVB’s tech firm clients and their wealthy founders. The front page promoted an upcoming SF Fed sponsored seminar on “climate economics” and a statement from the SF Fed declaring its “commitment to equity.” The American people would be better off had the SF Fed focused its attention on bank supervision rather than pushing a liberal ESG and DEI agenda.

In order for the Committee to understand why this failure may have occurred, please provide written responses to the following questions no later than March 30, 2023. In your response, identify the specific question to which you are responding. In responding to these questions, please keep in mind that SVB is now owned by the American people and their government has a duty to be transparent with them. You owe them more than general objections that the requested information is purportedly confidential supervisory information.

1. As a bank holding \$100 billion or more in assets, SVB should have been subject to Regulation YY and internal liquidity stress test requirements.

¹⁶ *About Us*, Federal Reserve Bank of San Francisco (accessed on Mar. 15, 2023), available at <https://www.frbsf.org/our-district/about/>.

¹⁷ Saleha Mohsin & Kate Davidson, *Fed Opens Probe of SVB Oversight Amid Criticism After Collapse*, BLOOMBERG (Mar. 13, 2023), available at <https://www.bloomberg.com/news/articles/2023-03-13/fed-s-oversight-of-svb-questioned-after-bank-s-sudden-failure#xj4y7vzkg>.

¹⁸ Letter from U.S. Senator Pat Toomey to SF Fed President Mary Daly (Mar. 29, 2021), available at <https://www.banking.senate.gov/imo/media/doc/Toomey%20Letter%20to%20San%20Fed.pdf>; Minority Press Release, U.S. Senate Banking Committee, *Toomey Launches Review of Mission Creep by Regional Federal Reserve Banks* (Mar. 29, 2021), available at <https://www.banking.senate.gov/newsroom/minority/toomey-launches-review-of-mission-creep-by-regional-federal-reserve-banks>.

¹⁹ Carola Binder & Christina Parajon Skinner, *Mission Critical or Mission Creep? The Research Function of the Federal Reserve Banks*, Mercatus Center (Apr. 2022), available at <https://www.mercatus.org/research/policy-briefs/mission-critical-or-mission-creep-research-function-federal-reserve-banks>.

²⁰ *Id.*

- a) Did SVB perform internal liquidity stress tests required by Regulation YY over the past five years, and if so, were they conducted on a monthly or quarterly basis?
 - i. Provide the date of each monthly or quarterly liquidity stress test SVB performed over the past five years and identify what the stress test(s) showed.
 - ii. If there was no stress test performed in any given month or quarter, please note and explain why none was performed.
 - iii. Did monthly or quarterly stress tests consider rising interest rates commensurate with the Federal funds rate? Please indicate the yield of the 3-month Treasury and the 10-year Treasury in Q1 2023 in both the baseline and adverse scenario of each test.
 - b) Did SVB receive any exemption from its liquidity stress test obligations under Regulation YY at any period in the last five years? If SVB was subject to an exemption during any period(s), explain why SVB was exempt and identify the period(s) during which SVB was exempt.
 - c) While Greg Becker, SVB's former CEO, served on the board of the Federal Reserve Bank of San Francisco, did he discuss any possible exemptions from Regulation YY with any employee or board member of the Federal Reserve of San Francisco? If so, with whom did he have those discussions?
 - d) Did anyone at the SF Fed discuss any possible exemptions for SVB from Regulation YY with any depositor or non-managerial shareholder of SVB? If so, please identify who those individuals were and to whom they spoke to at the SF Fed.
2. Did any employee, contractor, or board member of SVB communicate with anyone affiliated with the SF Fed about any risks associated with SVB's unrealized losses? If so:
- a) Identify who was involved in those communications;
 - b) Identify when they took place;
 - c) Identify how they took place (in-person, email, etc.); and
 - d) Produce all documents containing and relating to those communications.

3. Did any employee, contractor, or board member of SVB communicate with anyone affiliated with the SF Fed regarding SVB's ESG or DEI efforts? If so:
 - a) Identify who was involved in those communications;
 - b) Identify when they took place;
 - c) Identify the topic or subject of those communications;
 - d) Identify how they took place (in-person, email, etc.); and
 - e) Produce all documents containing and relating to those communications.

Thank you for your attention to this matter.

Sincerely,



Ted Cruz
Ranking Member

cc:

Hon. Jerome Powell, Chairman, Board of Governors of the Federal Reserve System
Hon. Lael Brainard, Vice Chairman, Board of Governors of the Federal Reserve System
Hon. Michael S. Barr, Vice Chairman for Supervision, Board of Governors of the Federal Reserve System
Hon. Michelle W. Bowman, Governor, Board of Governors of the Federal Reserve System
Hon. Lisa D. Cook, Governor, Board of Governors of the Federal Reserve System
Hon. Philip N. Jefferson, Governor, Board of Governors of the Federal Reserve System
Hon. Christopher J. Waller, Governor, Board of Governors of the Federal Reserve System