

Congress of the United States
Washington, DC 20515

December 19, 2023

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

Hon. Janet Yellen
Secretary
Department of the Treasury
1500 Pennsylvania Avenue N.W.
Washington, D.C. 20220

Dear Chairman Powell and Secretary Yellen,

We write today to urge the Federal Reserve Board (“Fed”) and the Department of the Treasury (“Treasury”) to conduct a detailed analysis regarding the impact of the Securities and Exchange Commission’s (“SEC” or “Commission”) proposed rulemaking titled “Further Definition of ‘As a Part of a Regular Business’ in the Definition of Dealer”¹ (the “Proposal”) on the costs of funding U.S. government debt, and, more broadly, on the resilience and liquidity of the U.S. Treasury market.

We wrote to SEC Chair Gensler to express our concerns with this Proposal in February 2023, but have not received a satisfactory response to date. As described below, we are concerned that the SEC has not assessed the most significant cost of the Proposal – the reduction of liquidity in the market resulting from private fund advisers modifying their investment strategies because registering as a securities dealer is untenable for their business model.

The Proposal would require non-dealers to register as dealers if one of three ambiguous qualitative standards or the Proposal’s quantitative standard is met.² As the Commission notes, registration and regulation as a dealer results in significant costs to the individual firms affected by the Proposal, but it will also result in foreseeable and to-date unassessed costs for the U.S. government and taxpayers. The costs to the U.S. government and resultant harmful effects to the overall economy of forcing non-dealers to either become dealers or change their investment behavior are likely to be significant and exceed any possible benefits.³

It is telling that the Commission has proposed a definition of “dealer” that is so broad that the Commission needed to exempt investment companies registered under the Investment Company

¹ *Further Definition of “As a Part of a Regular Business” in the Definition of Dealer and Government Securities Dealer*, 87 Fed. Reg. 23054 (Apr. 18, 2022) (the “Proposal”).

² Buying and selling more than \$25 billion in government securities in each of four out of the last six calendar months. *Id.* at 23071.

³ *Id.* at 23089-90.

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Act of 1940 (*e.g.*, mutual funds and ETFs) from its new definition. The Commission, however, did not propose a similar exemption for private fund advisers, despite the Commission's acknowledgement that registered private fund advisers are subject to comprehensive requirements under the Investment Advisers Act of 1940.

If faced with dealer registration, private fund advisers assert that they will change or abandon certain investment and hedging strategies. This would not be due to the monetary costs of the dealer registration process, which the Commission did consider, but instead will be driven by the incompatibility of ongoing regulation as a dealer for vehicles that pool investor capital (*i.e.*, private funds that are not established or intended to be operating companies). The SEC did not contemplate this in the Proposal and has sidestepped our questions on the issue. Instead, the SEC merely notes in the Proposal that “[t]he Proposed Rules would have uncertain impacts on efficiency, competition, and capital formation” and that “[t]he extent to which hedge funds may satisfy these standards is uncertain.”⁴ Looking at the total number of firms that may be required to become dealers, the SEC states that “[t]he precise number of affected parties is uncertain.”⁵ Not only does the Proposal repeat throughout its economic analysis that its impact on market participants is “uncertain,” the SEC states the Proposal's impacts on market efficiency, capital formation, and competition are also “uncertain.”⁶ The SEC's uncertainty is unsettling because the Proposal represents a seismic shift in broker-dealer regulation, which requires a careful and thorough cost-benefit analysis under relevant statutes. The SEC's uncertainty is also unacceptable, considering comment letters from market participants warning of the negative consequences for the U.S. government and Treasury market if the Proposal is adopted.

Given this uncertainty and the important role that private funds play (which is not equivalent to dealing activity) in the U.S. Treasury market, which the Commission acknowledges, we are concerned that a simple application of the dealer regime to these entities that are not structurally capable of functioning as dealers will prove counterproductive. The dealer regime will likely result in reduced liquidity and competition, which would harm markets that can ill-afford a further decline in liquidity, consolidation of market participants, or impaired efficiency.

We are concerned that the Proposal could significantly harm the market and the ability of the U.S. government to fund itself. As you consider this Proposal, we ask the Fed and Treasury to conduct a detailed analysis of the potential impact the Proposal would have on U.S. government funding and the U.S. Treasury market liquidity and efficiency.

⁴ *Id.* at 23078-82.

⁵ *Id.* at 23083.

⁶ *Id.* at 23091-92.

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We ask that this analysis be shared with us and the respective committees of jurisdiction in the Senate and House of Representatives by January 5, 2024.

We appreciate your prompt attention to our concerns.

Sincerely,



Bill Hagerty
United States Senator



French Hill
Member of Congress

cc: The Honorable Gary Gensler, Chairman, Securities and Exchange Commission