January 16, 2024

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

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

The Honorable Michael J. Hsu
Acting Comptroller of the Currency
Office of the Comptroller of the Currency
400 7th Street SW
Washington, DC 20219

Dear Chair Powell, Chairman Gruenberg, and Acting Comptroller Hsu:

We write in regard to the proposed rules issued jointly on July 27, 2023 by the Board of Governors of the Federal Reserve System, Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively, "the Agencies") to implement the final components of the Basel III agreement.[1] While we strongly support the Agencies' objective to safeguard the safety and soundness of our banking system, we are concerned about the potential unintended impacts the proposed changes could have on the cost of banking services for American households and businesses, particularly for underserved and minority communities.

Given the current macro-economic environment, access to affordable credit is an urgent priority. Businesses and consumers, including first-time homebuyers, are experiencing continued cost pressures and barriers to financing options.[2] We have specific reservations about the proposal's potential impact on mortgage affordability that could exacerbate the racial homeownership gap and business credit availability, which is a vital pathway to wealth creation for minority communities. As you carry out your vital work on behalf of the American people, it is critical that you continue to prioritize economic mobility, access to capital for underserved communities and small businesses, and equity at the center of any regulatory changes.

It is with that backdrop that we would like to draw attention to key areas of concern with the Agencies' Basel III Endgame proposal and its impact on the affordability of banking services.

Mortgage Affordability

We appreciate your recognition and request for comment on how the proposed treatment of regulatory residential real estate exposures could impact home affordability and home ownership opportunities,

[1] Fed, *Agencies request comment on proposed rules to strengthen capital requirements for large banks* (Jul. 27, 2023)
[2] Taylor, F. (2023, November 1). Mortgage Applications Decrease in Latest MBA Weekly Survey. *Mba.Org*. Retrieved from https://www.mba.org/news-and-research/newsroom/news/2023/11/01/mortgage-applications-decrease-in-latest-mba-weekly-survey..

particularly for LMI borrowers or other historically underserved markets.[3] We are concerned that the proposal may increase costs for mortgage lending and undermine efforts to support homeownership in underserved communities. As currently written, the proposal increases the risk weight for mortgages to 20% higher than the international Basel agreement.[4] The proposal is particularly punitive to high loan-to-value (LTV) mortgages, which is especially problematic for Low-to-Moderate Income (LMI) and minority borrowers who disproportionately rely on high-LTV mortgages due to the generational racial wealth gap.[5] More than half of loans to Black borrowers would receive a risk weight of 70% or more, according to industry reports, compared with just 22% of white borrowers.[6] Moreover, the proposal could have a significant impact on the commercial real estate industry's ability to access financing for buildings used for affordable housing.

One significant factor in the treatment of high-LTV mortgages is that the proposal significantly limits the consideration of Private Mortgage Insurance (PMI). PMI protects the lender and government against potential losses and can enable a borrower to qualify for mortgage financing with a down payment as low as 3%.[7] By removing PMI from the equation, the proposal could create fewer options for low down payment borrowers, disincentivizing lenders to provide high-LTV mortgages or buy the loans at a later date.

We are encouraged that you acknowledge an alternative in the proposal to incorporate the same treatment for residential mortgage exposures as found in the current U.S. standardized risk-based capital framework. As you state, "such an approach would allow banking organizations to continue to offer prudently underwritten products through lending programs with the flexibility to meet the needs of their communities without additional regulatory capital implications."[8] While we are extremely supportive of Special Purpose Credit Programs and their intent, we are concerned that requiring loans to be offered through special programs could prove limiting and could discourage banks from making loans outside of those designated programs.

Business Credit Affordability

The Basel III proposal as currently drafted has the potential to raise the cost of small business credit. For capital purposes, the Agencies propose that banks treat businesses that are not listed on a national exchange, but might otherwise be deemed investment-grade, as less creditworthy than publicly traded companies. With 99% of U.S. businesses privately held,[9] this provision could make it harder for private firms – including mom-and-pop businesses – to access financing compared to public companies.

We acknowledge that the proposal offers risk weight reductions that can be applied to non-publicly traded companies. For example, loans to a small or medium-sized entity (SME) under $1 million are the starting

[3] Office of the Comptroller of the Currency. (2023, September 18). *Federal Register / Vol. 88, No. 179 / Monday, September 18, 2023 / Proposed Rules 64049.* Retrieved from https://www.occ.gov/news-issuances/federal-register/2023/88fr64028.pdf

[4] Deloitte. Center for Regulatory Strategy US. (2023, August). *US Basel III Endgame: Key changes, impacts and where to begin.* Retrieved from https://www2.deloitte.com/content/dam/Deloitte/us/Documents/Advisory/us-advisory-deloitte-basel-iii-endgame-august-2023.pdf?nc=42

[5] Goodman, L., & Zhu, J. (2023, September). *Bank Capital Notice of Proposed Rulemaking - Urban.Org.* Urban.Org. Urban Institute. Retrieved from https://www.urban.org/sites/default/files/2023-09/Bank%20Capital%20Notice%20of%20Proposed%20Rulemaking.pdf

[6] *Id.*

[7] U.S. Mortgage Insurers. (n.d.). What is MI? Retrieved from https://www.usmi.org/private-mi/what-is-mi/

[8] Office of the Comptroller of the Currency. (2023, September 18). *Federal Register / Vol. 88, No. 179 / Monday, September 18, 2023 / Proposed Rules 64049.* Retrieved from https://www.occ.gov/news-issuances/federal-register/2023/88fr64028.pdf

[9] Biery, M. E. (2013, June 7). *4 Things You Don't Know about Private Companies.* Forbes. Retrieved from https://www.forbes.com/sites/sageworks/2013/05/26/4-things-you-dont-know-about-private-companies/?sh=1a866723291a

point for a calculation that could lead to a risk weight of 55% or 85%.[10] However, the proposal offers greater advantages to publicly traded firms on the basis that public firms are subject to enhanced transparency and market discipline. Given this rationale, we encourage the Agencies to further explore an option to apply a lower risk weight to non-publicly traded companies that are also "highly regulated."

Further, we are concerned that banks may react to higher capital requirements not necessarily by increasing their lending rates, but rather by reducing the amount of credit available to certain businesses. Small businesses and start-ups, which often have insufficient collateral to pledge against their borrowing, will attract higher risk weighted capital requirements and thus have less access to credit. The Biden Administration has taken significant steps to support small businesses, particularly underserved and minority-owned small businesses.[11] Given this progress, we would encourage sensitivity towards the potential negative impact of the Basel proposal on small business credit.

Operational Risk

A substantial portion of the increase in capital is targeted at "operational risk," or the risk of losses associated with lawsuits, fines, cyber-attacks, etc. The analysis provided in the proposal overstates the actual risk, as demonstrated by historical loss data; banks' operational risk losses rarely exceed even 30% of the proposed increase, according to industry reports.[12] Given the significant capital increases for this risk category, we recommend a recalibration of the operational risk charge.

Conclusion

As our first line of defense against bank failures and financial instability, robust capital is essential to a strong, resilient economy. We support the Agencies' commitment to fortifying our financial institutions, thereby ensuring safety and soundness in the financial system. As you prepare to finalize the proposal, we urge you to strike the appropriate balance between safety and soundness on the one hand, and consumer access and affordability, with particular sensitivity to the impact on marginalized communities, on the other. A proposal as broad as Basel III could have a myriad of sweeping, unintended consequences, potentially discouraging large banks' investments in minority depository institutions (MDIs) and community development financial institutions (CDFIs). Further, the proposal may adversely impact U.S. capital markets, raising costs for retirement and college savers, towns issuing securities to fund local infrastructure projects, and businesses hedging risks. Undercutting U.S. capital markets could hamper the ability for U.S. businesses to compete internationally.

Given the vast effects of the proposal, we believe it is important that prudential regulations remain consistent with our policy goals, including closing the homeownership gap and supporting small businesses as the backbone of our economy. Otherwise, continued pressure may further push financial services and risk outside the banking system where there is less regulation, supervision, and oversight, making the financial system less able to address these challenges, and ultimately less safe.

We appreciate your extension of the comment period and the data collection currently underway as an indication that you are willing to hear from all impacted stakeholders. On behalf of the consumers and

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[10] Office of the Comptroller of the Currency. (2023, September 18). *Federal Register / Vol. 88, No. 179 / Monday, September 18, 2023 / Proposed Rules 64049.* Retrieved from https://www.occ.gov/news-issuances/federal-register/2023/88fr64028.pdf

[11] O'Donnell, K., & Guida, V. (2023, August 31). How Biden's goal to boost Black homeownership could be undone by a new mortgage rule. *Politico.* Retrieved from https://www.politico.com/news/2023/08/31/mortgage-housing-bank-cops-00112290

[12] Carrivick, L., et al. (2023). *Basel III and Standardized Approaches to Capital.* ORX. Retrieved November 20, 2023, from https://orx.org/resource/basel-iii-and-standardised-approaches-to-capital-2023

businesses we represent, we respectfully ask the Agencies to take these concerns into consideration when crafting the final Basel III rule. We look forward to our continued work together to ensure the banking system is robust, safe, and sound, and serves Americans in all communities.

Sincerely,

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Juan Vargas Member of Congress	Steven Horsford Member of Congress
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