

United States Senate

WASHINGTON, DC 20510

June 10, 2024

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

Dear Chair Powell:

We are writing regarding the Federal Reserve Board's ("the Board," or "the Fed") new *Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules*.¹ You committed to adopting such a policy after the Federal Reserve Inspector General (IG) Mark Bialek released an investigation of the Board's trading scandal involving trades made by and on behalf of senior Fed officials – including you – during blackout periods or while they were in possession of non-public knowledge about Fed actions.² These trades appeared to violate Fed rules, and were clear abuses of the public trust, and they underscored the culture of corruption that has taken root at the Fed under your watch.

The new policy was approved by the Board on March 25, 2024, but the document was only made public after staff inquired on May 6, 2024, and has yet to be otherwise publicized on the Board's website.³ The Board's new policy is a dismal failure: it appears to lack the safeguards needed to prevent another trading scandal, or provide accountability to the public for Fed officials that engage in prohibited trading activity. The policy fails to establish – or even recommend – any specific penalties for ethics violations.⁴ It leaves the decision of whether to punish a violator up to the Chair and the Board itself — a self-policing approach that makes a mockery of independent review.⁵

¹ Federal Reserve, "Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules," <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

² Office of Inspector General, "The Board Can Further Enhance the Design and Effectiveness of the FOMC's Investment and Trading Rules, April 26, 2023, pp. 28-30, <https://oig.federalreserve.gov/reports/board-FOMC-investment-trading-rules-apr2023.pdf>; Memorandum from Inspector General Mark Bialek to The Honorable Jerome Powell, July 11, 2022, <https://oig.federalreserve.gov/releases/board-closing-trading-activity-jul2022.pdf>; Letter from Senator Warren to Chair Powell, August 11, 2022, <https://www.warren.senate.gov/imo/media/doc/2022.08.10%20Letter%20to%20Chair%20Powell%20re%20Fed%20trading%20scandal%20and%20OIG%20report%20-%20new.pdf>.

³ Electronic mail from the Office of the Federal Reserve Inspector General to the Office of Senator Elizabeth Warren, May 7, 2024, [Document is on file with the Office of Senator Elizabeth Warren].

⁴ Federal Reserve, "Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules," <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

⁵ *Id.*, p. 3.

The policy gives the Board’s Designated Agency Ethics Officer (DAEO) “sole discretion” to decide whether or not a violation was material—and therefore, whether or not it will undergo further scrutiny and face consequences.⁶ The policy is ridden with conflicts of interests from the start—the DAEO is appointed by the Chair, and can be removed at the Chair’s discretion.⁷ The Chair, alone, decides whether to take a material violation up with the Board, which puts you in the position of being able to protect yourself and your fellow Board members from any accountability—as has occurred in the past when trades that appeared to violate the Fed ethics policy were made from your accounts.⁸

Finally, the policy contains no transparency whatsoever when it comes to violations of ethics policy, requiring no disclosure regarding investigations, outcomes, or penalties imposed on Reserve Bank employees that engage in illicit trades.⁹ This new policy is a farce: it will do more to aid and abet the coverups of Fed trading scandals than it will do to reveal and eliminate them. It is extraordinarily disappointing that you and other Board members are still not taking your ethics responsibilities seriously. You should withdraw this policy, and replace it with an effective, enforceable approach to preventing illicit trading by Fed officials.

The Fed’s 2020 Trading Scandal and the IG’s Review and Recommendations

In March 2020, while millions of Americans grappled with the COVID-19 pandemic and the economy teetered on collapse, leaders of the Federal Reserve System actively traded individual stocks and investments while helping set key policies in response to the crisis.¹⁰ During this time, Fed officials made multiple large trades that appeared to clearly violate the Fed’s ethics policies.¹¹ You were personally involved in this scandal: a series of trades were made involving your accounts during the Fed’s “blackout period,” when officials should have been banned from these activities.¹² This trading scandal – the most severe ethics failure in the Fed’s history – eroded the public’s trust and raised legitimate questions about the integrity of Fed officials and the Fed’s policy making process.¹³

In response, the Fed IG opened an investigation into the scandal, finding that senior Fed officials had made trades that were in violation of Fed policy or did not meet Fed disclosure requirements (although

⁶ *Id.*, p. 2.

⁷ Congressional Research Service, “Executive Branch Ethics and Financial Disclosure Administration: The Role of Designated Agency Ethics Officials (DAEOs),” Updated May 30, 2023, <https://crsreports.congress.gov/product/pdf/IF/IF12019>.

⁸ Letter from Senator Warren to Chair Powell, August 11, 2022, <https://www.warren.senate.gov/imo/media/doc/2022.08.10%20Letter%20to%20Chair%20Powell%20re%20Fed%20trading%20scandal%20and%20OIG%20report%20-%20new.pdf>.

⁹ Federal Reserve, “Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules,” <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>; New York Times, “Fresh Fed financial disclosures omit the officials who ignited ethics scandal,” Jenna Smialek, June 24, 2022, <https://www.nytimes.com/2022/06/24/business/fed-financial-disclosures-ethics.html>.

¹⁰ New York Times, “A Fed Official’s 2020 Trade Drew Outcry. It Went Further Than First Disclosed,” Jenna Smialek, January 6, 2022, <https://www.nytimes.com/2022/01/06/business/economy/richard-clarida-fed-stock-fund.html>.

¹¹ *Id.*

¹² Letter from Senator Warren to Chair Powell, August 11, 2022, <https://www.warren.senate.gov/imo/media/doc/2022.08.10%20Letter%20to%20Chair%20Powell%20re%20Fed%20trading%20scandal%20and%20OIG%20report%20-%20new.pdf>; Memorandum from Inspector General Mark Bialek to The Honorable Jerome Powell, July 11, 2022, <https://oig.federalreserve.gov/releases/board-closing-trading-activity-jul2022.pdf>.

¹³ *Id.*

the IG held none of them accountable)¹⁴ and in April 2023 – more than three years after the violations took place – released a report identifying six recommendations for the Board to enhance Federal Open Market Committee (FOMC) investment and trading rules and internal Board disclosure review processes to better determine and enforce consequences for ethics violations for Reserve Bank covered individuals.¹⁵

In a letter to Mr. Bialek on April 19, 2023, you agreed to implement all six of the IG’s April 2023 recommendations.¹⁶ Although you appear to have acted on all six recommendations, the IG still lists three of them as “open” – meaning they have not been fully reviewed or implemented.¹⁷ And several of those you have addressed appear to be insufficient. For example, in response to the IG’s recommendation that the Board “should develop a plan to enhance the System’s financial disclosure report review process, including considering additional controls and guidance,” (recommendation #3) the Board merely “hosted a training on how to properly review financial disclosure reports.”¹⁸ This does not fulfill the IG’s broader recommendation, which is that the Board create a new financial disclosure report review process with guidance and enforcement mechanisms.

The biggest gap in your response to the IG report appears to be the new enforcement policy.

The Fed’s New Enforcement Policy for Officials that Violate Investment, Trading and Disclosure Rules is Woefully Inadequate

On March 25, 2024—four years after the first set of trades in the biggest ethics scandal in Fed history—the Board of Governors approved the *Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules*,¹⁹ describing how it would take action when Fed officials violated the new trading rules. This enforcement policy is the linchpin of the new rules:²⁰ absent effective enforcement, the rules themselves are meaningless. And, whether by design or by mistake, that appears to be the outcome here: the new enforcement policy is so weak and so opaque that it effectively renders the new Fed trading rules null and void.

¹⁴ Letter from Senators Elizabeth Warren and Rick Scott to Federal Reserve Inspector General, March 6, 2024, pp. 5-6, <https://www.warren.senate.gov/imo/media/doc/2024.03.05%20Letter%20to%20Fed%20IG%20Mark%20Bialek%20re.%202024%20report.pdf>; Wall Street Journal, “Fed Leaders Eric Rosengren, Robert Kaplan to Resign Following Trading Controversy,” Michael S. Derby, September 27, 2021, <https://www.wsj.com/articles/boston-fed-leader-rosengren-to-retire-early-from-bank11632747033>.

¹⁵ Office of Inspector General, “The Board Can Further Enhance the Design and Effectiveness of the FOMC’s Investment and Trading Rules, April 26, 2023, <https://oig.federalreserve.gov/reports/board-FOMC-investment-trading-rules-apr2023.pdf>.

¹⁶ Office of Inspector General, “The Board Can Further Enhance the Design and Effectiveness of the FOMC’s Investment and Trading Rules, OIG Report 2023-SR-B-006, April 26, 2023, pp. 28-30, <https://oig.federalreserve.gov/reports/board-FOMC-investment-trading-rules-apr2023.pdf>.

¹⁷ Electronic mail from the Office of the Federal Reserve Inspector General to the Office of Senator Elizabeth Warren, May 7, 2024, [Document is on file with the Office of Senator Elizabeth Warren].

¹⁸ *Id.*

¹⁹ *Id.*; Federal Reserve, “Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules,” <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

²⁰ Federal Reserve, “FOMC Policy on Investment and Trading for Committee Participants and Federal Reserve System Staff,” amended effective January 30, 2024, https://www.federalreserve.gov/monetarypolicy/files/FOMC_InvestmentPolicy.pdf.

The IG recommended that the Board “[f]ormalize a process for determining and enforcing consequences” for violations of the trading policy.²¹ But the policy is woefully inadequate: it does not establish or even recommend concrete penalties for disclosure violations and violations of the *Investment and Trading Policy* by covered Reserve Bank individuals, it is too vague and has multiple loopholes, it is ridden with internal conflicts of interest affecting key decisionmakers, and it does not require any public disclosure of ethics violations or adjudication related to potential violations.²²

First, and most importantly, the policy does not establish or recommend any concrete penalties for violations, and no assurance that penalties will be enforced. While the policy acknowledges that the Board technically has the power to “approve the pay of Reserve Bank employees,”²³ “suspend or remove any officer of a Reserve Bank,”²⁴ and “exercise general supervision over Reserve Banks,”²⁵ the policy does not codify penalties in any way—it fails to establish any clear consequences for violations of ethics rules, and does not provide any guidance on how a penalty will or should correspond to violations. The sole guidance on penalties for violations of the policy is that “If the [Board’s Designated Agency Ethics Officer (DAEO)] determines a violation has occurred, the DAEO shall recommend a penalty ... making sure that any recommended penalty is proportionate to the violation.”²⁶ This new policy gives no guidance on when officials who violate the policy should be subject to fines, suspension, termination, or referral to law enforcement authorities – a yawning gap.

But if the DAEO overcomes this gap, identifies a violation, and recommends a penalty, even that will not necessarily result in the imposition of any penalty. According to the policy, the ultimate decision of how to punish the covered employee, if at all, is left up to you (the Chair) and a Board vote.²⁷ This approach amounts to self-policing: neither you nor Board members (particularly given your sorry record in adhering to trading rules)²⁸ can be considered impartial in adjudicating violations by covered officials.

²¹ Office of Inspector General, “The Board Can Further Enhance the Design and Effectiveness of the FOMC’s Investment and Trading Rules,” April 26, 2023, p.3, <https://oig.federalreserve.gov/reports/board-FOMC-investment-trading-rules-apr2023.pdf>.

²² Federal Reserve, “Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules,” p. 1, <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

²³ *Id.*, p. 1.

²⁴ *Id.*

²⁵ *Id.*

²⁶ *Id.*, p. 3.

²⁷ *Id.*, at p. 3. “If the DAEO determines a violation has occurred, the DAEO shall recommend a penalty to the Director of RBOPS,” who then will make a recommendation to the Chair, who may bring it to a Board vote: “The Chair will recommend to the Board the appropriate action to take. The Board shall decide whether to adopt the Chair’s recommendation.”

²⁸ Better Markets, “STATEMENT ON REVELATIONS THAT FEDERAL RESERVE CHAIR JAY POWELL ENGAGED IN PERSONAL TRADING DURING THE PANDEMIC IN 2020,” press release, October 19, 2021, <https://bettermarkets.org/newsroom/statement-on-revelations-that-federal-reserve-chair-jay-powell-engaged-in-personal-trading-during-the-pandemic-in-2020/>; New York Times, “A Fed Official’s 2020 Trade Drew Outcry. It Went Further Than First Disclosed,” Jeanna Smialek, January 6, 2022, <https://www.nytimes.com/2022/01/06/business/economy/richard-clarida-fed-stock-fund.html>.

Additionally, the policy only applies to “material” violations, creating a series of loopholes by which a violation may be misconstrued as an immaterial, rather than material violation.²⁹ The DAEO “has the sole discretion to determine whether a violation is material.”³⁰ The policy outlines no concrete definition of a “material violation,” but does create loopholes that allow the DAEO to write off a violation of trading rules based on “whether the potential violation was knowingly committed in disregard of the policy;” “the probability of serious reputational impact to the System;” “whether a pattern of violations exist;” and “whether the violation was as a result of the actions of a third party, the employee’s minor child or spouse.”³¹ Each of these loopholes create a potential “get out of jail free” card for covered employees that violate the trading rules.³² Indeed, this list of loopholes appears to be taken almost directly from the list of excuses used by you and other Board members to evade responsibility for your previous violations of Fed trading and disclosure rules.³³

The list of problems with this policy goes on. It is rife with personnel conflicts of interest—the DAEO is appointed by the Chair (you), and serves at the discretion of the Board.³⁴ It does not require recusal from votes for Board members with potential conflicts of interest. While it outlines scenarios to modify the process if violations involve a Fed President, First Vice President, or General Counsel, it outlines no process by which, if the Chair violates Fed policy, their case would be adjudicated and penalized.³⁵ This is a serious problem, since the Chair is the only Board official with the authority to bring a penalty to the Board for a vote.³⁶ And finally, the policy requires no public disclosure at all, eliminating the only process by which Reserve Bank officials and the Board and its members can be held fully accountable for violations of the trading policy.

²⁹ Federal Reserve, “Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules,” p. 2, <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

³⁰ *Id.*

³¹ *Id.*

³² Letter from Senators Elizabeth Warren and Rick Scott to Fed IG Mark Bialek, March 6, 2024, p. 3, <https://www.warren.senate.gov/imo/media/doc/2024.03.05%20Letter%20to%20Fed%20IG%20Mark%20Bialek%20re.%202024%20report.pdf>.

³³ Letter from Senator Warren to Chair Powell, August 11, 2022, <https://www.warren.senate.gov/imo/media/doc/2022.08.10%20Letter%20to%20Chair%20Powell%20re%20Fed%20trading%20scandal%20and%20OIG%20report%20-%20new.pdf>.

³⁴ Congressional Research Service, “Executive Branch Ethics and Financial Disclosure Administration: The Role of Designated Agency Ethics Officials (DAEOs),” Updated May 30, 2023, <https://crsreports.congress.gov/product/pdf/IF/IF12019>.

³⁵ Federal Reserve, “Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules,” pp. 2-3, <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>. Step #2 states that “the DAEO shall notify the General Counsel of the relevant Reserve Bank of the potential violation, unless the potential violation involves such General Counsel, in which case the DAEO shall notify the President of the relevant Reserve Bank,” and step #7 outlines an alternative process the Chair will follow for “violations involving a President or First Vice President.”

³⁶ Federal Reserve, “Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules,” <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

Conclusion

On multiple occasions, we have raised concerns about the culture of corruption that has arisen under your watch at the Federal Reserve,³⁷ and we remain concerned that the Board has not put sufficient barriers in place to prevent future scandals and restore the public's trust. This new enforcement policy, which comes nearly four years after the Fed trading scandal, is a massive failure.³⁸ The gaps in this policy render effective enforcement of Fed trading rules impossible, and indicate that, once again you do not appear to be willing to act in order to prevent further scandals. You should withdraw this policy, and replace it with an effective, enforceable approach to preventing illicit trading by Fed officials.

The public has waited too long for transparency and corrective action from the Board. The public deserves more from America's central bank than this weak and ineffective policy. With this in mind, we ask that you answer the following questions by June 24, 2024:

1. Besides Fed officials, what ethics experts did you consult with during the preparation of the new policy?
 - a. What recommendations did they provide?
 - b. Were all of these recommendations formalized in the new rules?
2. What is the range of penalties available for individuals who violate the Fed's trading policy?
 - a. Does the policy contain any required minimum penalties, even for individuals who knowingly and willfully violate the trading policy?
 - b. If so, where in the policy are those specifically denoted?
 - c. If not, why not?
3. Does the policy contain any requirement that adjudicated violations of the policy – and the names of the individuals that committed the violations – be made public?
 - a. If so, where is this transparency requirement listed in the policy?
 - b. If not, why not?
4. What policies are in place if you or any future Federal Reserve Board Chairs are accused of violating the trading policy? In this scenario, which Federal Reserve officials will adjudicate the case and which individuals will be responsible for determining penalties if a violation is identified?
5. In determining conflicts of interest, federal ethics rules impute the interests of a covered employee's "spouse, minor child, [or] general partner" to the employee.³⁹ But the new Fed

³⁷ Letter from Senator Elizabeth Warren to Federal Reserve Chair Jerome Powell, November 7, 2020, <https://www.warren.senate.gov/download/20221104-letter-to-chair-powell-re-fed-trading-scandal-and-fomc>; <https://www.warren.senate.gov/imo/media/doc/2024.03.05%20Letter%20to%20Fed%20IG%20Mark%20Bialek%20re.%202024%20report.pdf>.

³⁸ Federal Reserve, "Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules," <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

³⁹ U.S. Office of Government Ethics, "Analyzing Potential Conflicts of Interest," <https://www.oge.gov/web/OGE.nsf/Resources/Analyzing+Potential+Conflicts+of+Interest>.


ethics rules do not, specifically indicating that actions taken by a covered employee's spouse might not be subject to Fed enforcement process. Why did the Fed make this decision?

6. One criterion for determining if a violation of the policy is "material" is "the probability of serious reputational impact to the System."⁴⁰ This appears to indicate that a lack of transparency can prevent any type of violation from being "material." How will the DAEO assess the "probability of serious reputational impact to the System" for any given violation of the policy?
7. Another criterion for determining if a violation of the policy is "material" is "whether the potential violation was knowingly committed in disregard of the policy." Is this standard consistent with other ethics policies governing other federal employees? How will the Board be able to prove that any trade was knowingly made in disregard of the policy?
 - a. What is the process for selecting the Federal Reserve Board's Designated Agency Ethics Official (DAEO)? Likewise, what is the process for selecting the Reserve Bank ethics officers?
8. How will the DAEO determine whether a recommended penalty is "proportionate"⁴¹ to a violation?
9. The policy appears to be silent on potential violations of the Board's trading disclosure requirements. What enforcement policy is in place for these disclosure requirements?
10. How will all individuals involved in the process of determining violations of the *Investment and Trading Policy* and financial disclosure rules by covered Reserve Bank individuals, including the DAEO, General Counsel, and Chair be trained to see through and enforce the new *Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules*?

Sincerely,



Elizabeth Warren
United States Senator



Rick Scott
United States Senator

⁴⁰ Federal Reserve, "Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules," p. 2, <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.

⁴¹ Federal Reserve, "Policy for Addressing Covered Reserve Bank Employee Material Violations of the Investment & Trading Policy and Financial Disclosure Rules," p. 3, <https://www.federalreserve.gov/aboutthefed/files/ethics-enforcement-policy-for-board.pdf>.