U.S. HOUSE COMMITTEE ON FINANCIAL SERVICES
– RANKING MEMBER MAXINE WATERS –
BACKGROUND ON RECENT BANK FAILURES

Following the failures of Silicon Valley Bank (SVB) on March 10th and Signature Bank on March 12th – the second and third largest bank failures in U.S. history, respectively – the U.S. Department of the Treasury (Treasury), Federal Deposit Insurance Corporation (FDIC), and the Board of Governors of the Federal Reserve System (Fed) announced a plan to fully protect depositors of those two banks, as well as to create a new liquidity facility to support solvent banks and credit unions.[1] Since then, while banks have accessed these and other sources of liquidity in record numbers, others have faced challenges. For example, large banks deposited $30 billion in First Republic Bank to shore up the bank, and the Swiss government helped arrange for UBS to buy Credit Suisse on March 19th after the bank nearly failed. Along with other investigations underway,[2] Chairman McHenry and Ranking Member Waters requested GAO conduct a review and announced that the House Financial Services Committee would hold a series of bipartisan hearings, beginning with a hearing on March 29th with officials from the Treasury Department, FDIC, and Federal Reserve testifying.[3] Below is a fact sheet describing these and related developments.

Silicon Valley Bank Failure

On Friday, March 10, 2023, Silicon Valley Bank was closed by the California Department of Financial Protection and Innovation (DFPI), and the FDIC was named as receiver. SVB was a state-chartered bank that was a member of the Federal Reserve System; therefore, its primary federal regulator was the Fed.[4] SVB was the 16th largest bank in the U.S. As of December 31, 2022, SVB had about $209 billion in total assets and about $175 billion in total deposits. Roughly $151 billion of those deposits were uninsured.[5]

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[1] See Treasury, *Joint Statement by the Department of the Treasury, Federal Reserve, and FDIC* (Mar. 12, 2023); and Fed, *Federal Reserve Board announces it will make available additional funding to eligible depository institutions to help assure banks have the ability to meet the needs of all their depositors* (Mar. 12, 2023). Also see FSC, *Waters, Brown Commend Federal Regulators for Protecting Banking System* (Mar. 12, 2023).

[2] For example, the Fed announced on that Vice Chair for Supervision Michael S. Barr is leading a review of the SVB's supervision and regulation, which will be publicly released by May 1. Additionally, the Inspectors General for the Fed and FDIC are examining these bank failures, and there are reports that DOJ and SEC are investigating as well.

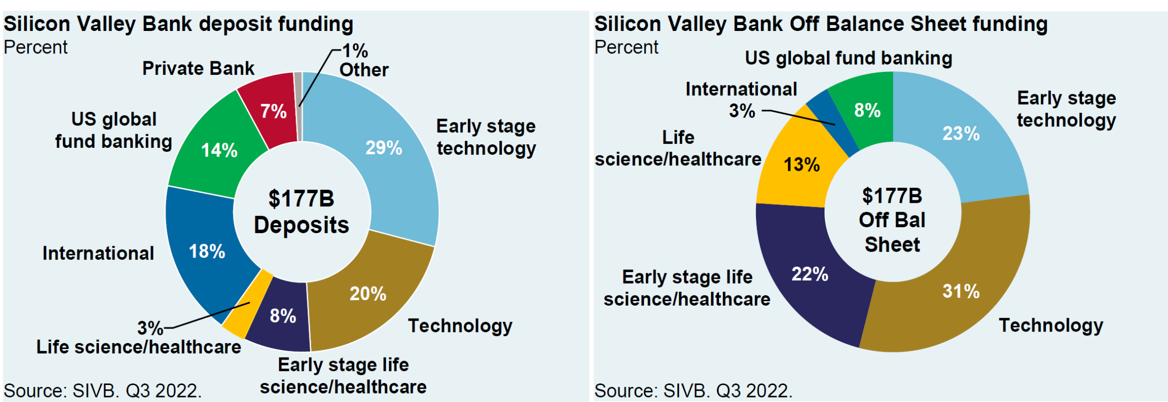
[3] FSC, *Waters, McHenry Announce First Hearing on Silicon Valley Bank and Signature Bank Failures* (Mar.17, 2023).

[4] For more on how banks are regulated, see CRS, *Who Regulates Whom? An Overview of the U.S. Financial Regulatory Framework* (Mar. 10, 2020).

[5] It has been reported that deposits dropped significantly since the end of last year, especially in recent days, as customers withdrew money before the bank closed. For example, see New York Times, *Silicon Valley Bank Fails After Run on Deposits*, (Mar. 10, 2023). The balance sheet of SVB at the time of FDIC's takeover is unclear.

While causes of the SVB failure will likely become clearer over time, there have been reports laying out several contributing factors to the bank's failure.[6] SVB predominantly served companies in the tech industry, along with venture capital investors. SVB's deposits rose quickly in recent years, from $57 billion in 2018 to at least $200 billion by 2022. During the pandemic, the bank experienced an average growth of 76% in interest-earning assets in the first quarter of 2021. According to FDIC data, the bank's assets rose from $70 billion in 2019 to $114 billon at the end of 2020, and again to about $209 billion at the end of 2021. During this period of rapid growth, the Fed allegedly raised concerns about SVB's risk management at least four years before its failure. Specifically, in January 2019, the Fed reportedly cited SVB for having deficient risk-management systems, and in 2020, warned that the bank's system to control risk did not meet expectations for a large financial institution.[7] The Fed reportedly later issued six more warnings in 2021 in the form of Matters Requiring Attention (MRAs) and Matters Requiring Immediate Attention (MRIAs) for weak risk controls, and in 2022, SVB was restricted by the Fed from acquiring any other bank.

As the Federal Reserve increased interest rates over the past year to address inflation, the market value of SVB's investments in Treasurys and government-sponsored debt securities, like mortgage-backed securities issued by Fannie Mae, which were purchased when rates were low, declined compared to similar securities issued today. When SVB had to sell $20 billion of these securities to meet the demand for deposit withdrawals, it did so at a $2 billion loss. SVB's parent company planned a $2.25 billion share sale to raise more funds, but it was unsuccessful, leading to broad concerns about the viability of the bank. SVB also appeared to rely on a high percentage (approximately 95%) of deposits that were uninsured (deposits over $250,000), which historically tend to be less stable and more flighty than insured deposits. Reportedly, customers withdrew about $42 billion of deposits on Thursday, March 9th, leaving the bank with a negative cash balance of nearly $1 billion by the end of the day Thursday. This is reported to be the largest run on a bank in history, and these dynamics likely contributed to the decision to close the insolvent bank in the middle, instead of the end, of the following day.



Source: JP Morgan Analysis (March 10, 2023)

After regulators authorized a systemic risk exception (SRE) to protect depositors as described below, FDIC transferred SVB's assets and liabilities to a bridge bank where SVB depositors have access to all of their funds. The FDIC is in the process of taking bids from private entities until March 24th that may want to buy parts

[6] This paragraph is drawn from various sources, including: Wall Street Journal, *Silicon Valley Bank Closed by Regulators, FDIC Takes Control* (Mar. 10, 2023); New York Times, *Silicon Valley Bank Fails After Run on Deposits* (Mar. 10, 2023); Financial Times, *Silicon Valley Bank shut down by US banking regulators* (Mar. 10, 2023); Washington Post, *Silicon Valley Bank failure raises fear of broader financial contagion* (Mar. 10, 2023); and USA Today, *What Silicon Valley Bank collapse means – and why it's not 2008 again* (Mar. 10, 2023).
[7] Wall Street Journal, *Fed Raised Concerns About SVB's Risk Management in 2019* (Mar. 19, 2023).

or all of the bank.[8] Ranking Member Waters recently urged the FDIC to ensure the continued implementation of SVB's $11 billion Community Benefits Plan (CBP), which is aimed at providing housing, small business, and other community development support to underserved communities, by both the bridge bank and any buyer of the bank.[9]

Signature Bank Failure

On Sunday, March 12th, Signature Bank was closed by the New York Department of Financial Services (NYDFS) and the FDIC was appointed as receiver of the bank. The FDIC transferred all the deposits and substantially all of the assets of Signature Bank to Signature Bridge Bank, N.A., a full-service bank that will be operated by the FDIC as it markets the institution to potential bidders. Signature Bank was a state-chartered bank that was not a member of the Federal Reserve System; therefore, its primary federal regulator was the FDIC. The bank was the 29th largest U.S. bank with total assets of approximately $110 billion and total deposits of approximately $89 billion as of December 31, 2022. Signature Bank is the second bank closely associated with the cryptocurrency and digital assets industry to fail in the past week,[10] the first being Silvergate Bank – a bank previously associated with Facebook's Libra – which announced that it would voluntarily wind down operations and liquidate the bank on Wednesday, March 8th.[11] On March 19th, the FDIC announced that most of Signature Bank's loans and deposits were purchased by Flagstar Bank (a wholly-owned subsidiary of New York Community Bancorp), with the exception of $60 billion in loans that will remain in receivership, and the former bank's $4 billion digital asset-related deposits.[12] In addition, the former bank's 40 branches began to operate under Flagstar Bank starting on March 20th. The FDIC estimates the cost of Signature Bank's failure to the Deposit Insurance Fund (DIF) would be approximately $2.5 billion.[13]

Systemic Risk Exception, Emergency Liquidity, and Private Sector Support

When managing the resolution of any failed bank, the FDIC is generally required to do so in a manner that is least costly to the Deposit Insurance Fund (DIF), referred to as the "least cost test." However, there is a systemic risk exception (SRE) to the least cost test that allows the FDIC to use the DIF to support uninsured depositors. On March 12th, the Treasury Department, with the support of at least two-thirds of the FDIC Board of Directors, and at least two-thirds of the Fed Board of Governors, authorized a SRE for both SVB and Signature Bank to protect all depositors, while deciding to not protect shareholders and certain unsecured debtholders, and removing senior bank management. If there are any losses to the DIF, the FDIC would charge a special assessment of banks to cover the losses, meaning there would be no cost to the taxpayer. The FDIC previously used the SRE to establish several widely available debt guarantee programs during the 2008 financial crisis, including the Transaction Account Guarantee Program (TAGP).[14]

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[8] FDIC, *FDIC Extends Bid Window For Silicon Valley Bridge Bank, N.A.* (Mar. 20, 2023).
[9] FSC, Ranking Member Waters Urges FDIC to Ensure California Communities Remain Supported Through Silicon Valley Bank's Housing, Community Reinvestment Plan | U.S. House Committee on Financial Services Democrats (Mar. 18, 2023).
[10] The Verge, *Signature Bank is closed by regulators, the third US bank failure in a week* (Mar. 12, 2023); Wall Street Journal, *SVB, Signature Bank Depositors to Get All Their Money as Fed Moves to Stem Crisis* (Mar. 12, 2023); and New York Times, *Regulators Close Another Bank and Move to Protect Deposits* (Mar. 12, 2023).
[11] Silvergate, *Silvergate Capital Corporation Announces Intent to Wind Down Operations and Voluntarily Liquidate Silvergate Bank* (Mar. 8, 2023). *Also see* Wall Street Journal, *Crypto Bank Silvergate to Shut Down, Repay Deposits* (Mar. 8, 2023); and Financial Times, *Facebook Libra: the inside story of how the company's cryptocurrency dream died* (Mar. 10, 2022).
[12] FDIC, Subsidiary of New York Community Bancorp, Inc., to Assume Deposits of Signature Bridge Bank, N.A., From the FDIC (Mar. 19, 2023).
[13] FDIC, Subsidiary of New York Community Bancorp, Inc., to Assume Deposits of Signature Bridge Bank, N.A., From the FDIC (Mar. 19, 2023).
[14] For more information, see FDIC, *Temporary Liquidity Guarantee Program* (Feb. 19, 2019); and FDIC, *The Temporary Liquidity Guarantee Program: A Systemwide Systemic Risk Exception* from *Crisis and Response: An FDIC History, 2008–2013*.

Additionally, on March 12th, the Fed utilized its authorities under Section 13(3) of the Federal Reserve Act to establish the Bank Term Funding Program (BTFP). This program is a new source of liquidity for banks and credit unions by offering loans of up to one year, so long as the financial institutions pledge U.S. Treasuries, agency-backed debt, and other qualifying assets as collateral. This program supplements liquidity available to depository institutions through the Fed's discount window, which has a 90-day limitation on its loans compared to a much longer one-year loan available through BTFP. Importantly, securities pledged to the BTFP will be valued at par value, rather than the market value that is used for discount window collateral, which will help avoid fire sales of otherwise safe assets held by banks during times of stress, at no cost to the taxpayer.

Recent data shows that banks took out nearly $12 billion in BTFP's first three days of operating, while also taking out a record-breaking $153 billion from the Fed's discount window last week. Banks also received liquidity from the Federal Home Loan Banks (FHLBs), which issued more than $300 billion in discount notes and bonds to meet member demand and to maintain liquidity for the 11 FHLBs themselves.[15] Furthermore, while market turmoil continued to affect a few other banks, 11 of the largest U.S. banks agreed to deposit a combined $30 billion in First Republic Bank on March 16th, a move that was welcomed by financial regulators.[16] However, the bank has continued to face pressure in the market.[17]

International Developments

Troubles in the banking sector have extended to jurisdictions beyond the U.S. Most notably, on March 15th, Credit Suisse announced that it would borrow up to 50 billion Swiss francs (USD $53.7 billion) from the Swiss National Bank, after its stock had crashed as much as 30% to a new record low.[18] On March 19th, Swiss regulators facilitated the merger of Credit Suisse and UBS, "to restore necessary confidence in the stability of the Swiss economy and banking system."[19] UBS Group will pay 3 billion Swiss francs (USD $3.2 billion) for the 167-year-old Credit Suisse Group, which was once worth more than $90 billion.[20]

Additionally, on March 19th, the Fed, along with central banks from Canada, United Kingdom, European Union, Switzerland, and Japan announced that they would coordinate to increase the frequency of their U.S. dollar liquidity swap arrangements from weekly to daily from March 20 through at least the end of April to increase the flow of U.S. dollars through the global financial system.[21] These swap arrangements were utilized in the 2008 financial crisis when markets seized up, and allow central banks to exchange their home currencies for dollars, helping to promote financial stability and ease strains in financial markets.[22]

Trump-Era Deregulation

After the 2008 global financial crisis, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) into law. One of the key reforms was a requirement that bank holding companies with more than $50 billion in total assets were subject to enhanced prudential standards.[23] This meant

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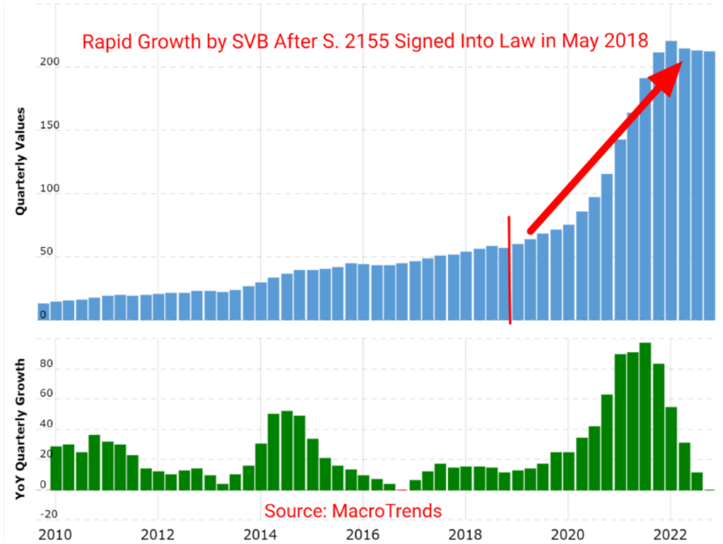
[15] See American Banker, *Federal Home Loan banks issued $304 billion to meet liquidity demands* (Mar. 20, 2023).
[16] Wall Street Journal, *Eleven Banks Deposit $30 Billion in First Republic Bank* (Mar. 16, 2023).
[17] Wall Street Journal, *JPMorgan CEO Jamie Dimon Leading Efforts to Craft New First Republic Bank Rescue Plan* (Mar. 20, 2023).
[18] CNN, *There's still a fight on Credit Suisse hands despite $54 billion lifeline* (Mar. 16, 2023).
[19] Credit Suisse, *Credit Suisse and UBS to Merge* (Mar. 19, 2023).
[20] Reuters, *Bank shares rise after Credit Suisse rescue eases crisis* (Mar. 19, 2023).
[21] Fed, *Coordinated central bank action to enhance the provision of U.S. dollar liquidity* (Mar. 19, 2023).
[22] *See* Mark Thompson, *Fed and other central banks try to head off crisis by keeping dollars flowing*, CNN (Mar. 19, 2023).
[23] *See* CRS, *Enhanced Prudential Regulation of Large Banks* (May 6, 2019).

they were subject to more stringent capital and other requirements to ensure they were safe and sound as a means of promoting financial stability. In 2015, Congress considered a measure to relax this requirement for banks with less than $250 billion in total assets. Greg Becker, CEO of SVB, submitted a statement for the record urging support for this effort, arguing that SVB had a "low risk profile" and a "traditional banking business model."[24] In 2018, Congress ultimately enacted these reforms into law,[25] when SVB had $53 billion in total assets before rapidly growing to have more than $200 billion in total assets. In 2019, Trump's regulators issued rules implementing the 2018 law and generally relaxed requirements for or otherwise exempted bank holding companies with less than $250 billion from enhanced prudential standards.[26] For example, instead of being subject to robust semiannual, company-run stress tests and annual supervisory stress tests, SVB was subject to a supervisory stress test every two years. But given the timing of its growth, the was not scheduled to receive its first supervisory stress test until 2024. Additionally, SVB was exempt from the liquidity coverage ratio (LCR) and only had to do quarterly internal liquidity stress tests. SVB was also exempt from Dodd-Frank's resolution planning requirements (also referred to as "living wills") while only having to do a more narrow resolution plan separately required by the FDIC for insured depository institutions.[27] Moreover, the bank was able to opt out of capital requirements relating to accumulated other comprehensive income (AOCI), which allowed the bank to seem better capitalized than it was with a large amount of unrealized losses in their securities portfolio.[28]



With respect to Signature Bank, they had $44 billion in total assets in 2018 before quickly growing to have more than $110 billion in total assets,[29] though they were one of the few large banks that did not have a bank holding company. While that meant that some of Dodd-Frank's original enhanced prudential standards would not have automatically applied,[30] certain stress testing requirements would have applied prior to the 2018 law,[31] and regulators used other authority to apply other enhanced measures, such as resolution planning.[32]

[24] *See* Senate Committee on Banking, Housing, and Urban Affairs hearings entitled, "Examining the Regulatory Regime for Regional Banks," held on March 19, 2015, and March 24, 2015.

[25] P.L. 115-174, S. 2155 (115th Congress), the Economic Growth, Regulatory Relief, and Consumer Protection Act (Crapo).

[26] See Fed, *Federal Reserve Board finalizes rules that tailor its regulations for domestic and foreign banks to more closely match their risk profiles* (Oct. 10, 2019). Also see Davis Polk, *The Final Tailoring Rules for U.S. Banking Organizations* (Nov. 21, 2019), and Todd Phillips, *How 2018 Regulatory Rollbacks Set the Stage for the Silicon Valley Bank Collapse, and How to Change Course, Roosevelt Institute* (Mar. 15, 2023).

[27] SVB submitted their first and only IDI resolution plan in December 2022. See SVB, *2022 Covered Insured Depository Institution Resolution Plan: Public Section* (Dec. 2022).

[28] *See* Seeking Alpha, *SVB Financial: Incompetence Allowed By Flawed Regulations* (Mar. 12, 2023). For more info on enhanced prudential standards that applied to SVB, see pp 11-12 from their Form 10-K for the fiscal year ending Dec. 31, 2022.

[29] See Fed, *Large Commercial Banks – Statistical Release* (Mar. 30, 2018).

[30] Given how nonbank financial company is defined in Dodd-Frank, the Financial Stability Oversight Council (FSOC) has authority to designate and subject any bank that does not have a bank holding company to enhanced prudential standards, though they have not done so to date.

[31] Under the original Dodd-Frank provisions, Signature Bank would have been required to conduct annual company-run stress tests, and the bank could have been subject to annual supervisory stress tests at the Fed's discretion.

[32] Signature Bank was required to submit a resolution plan for insured depository institutions (IDI) to the FDIC once every three years, though given the timing of when the crossed the $100 billion threshold, they had not done so before they failed. For more on IDI resolution plans, see FDIC, *FDIC and Financial Regulatory Reform - Title I and IDI Resolution Plans* (Jan. 3, 2023). For more info on enhanced prudential standards that applied to Signature Bank, see pp 22-37 from their Form 10-K for the fiscal year ending Dec. 31, 2022.

These developments raise serious questions about how Trump's regulators implemented the 2018 law may have contributed to the banks' failures. For example, regulators only required stress testing be done once every two years for most banks between $100 billion and $250 billion. Given the timing of SVB's rapid growth, they were not required to take their first stress test until 2024. Additionally, Dodd-Frank originally required there be at least 3 stress test scenarios (baseline, adverse, and severely adverse), however the 2018 law reduced that requirement to 2 stress test scenarios, eliminating the adverse scenario. While the Fed has not recently tested a scenario where interest rates rise rapidly (as they have over the past year), they previously did so in 2013 and 2015 using the adverse scenario that the 2018 law eliminated.[33] If the Fed was required to still test multiple scenarios, there may have been a greater likelihood the Fed may have tested a rising interest rate economic environment in recent years.

Short-Term Rates Spike Just Twice In Fed's Stress Tests

Tests typically model near-zero rates in shocks

Year	Adverse Scenario	Severely Adverse Scenario
2013	**Rise to 2.5% in one year**	**Remain near zero**
2014	Remain near zero	Remain near zero
2015	**Rise to 2.5% in one year, then 5.3% over next two years**	**Remain near zero**
2016	Remain near zero	Fall, remain at -0.5%
2017	Fall, remain near zero	Fall, remain near zero
2018	Fall, remain near zero	Fall, remain near zero
2019	Fall (scope unspecified)	Fall, remain near zero
2020	N/A	Fall, remain near zero
2021	N/A	Remain near zero
2022	N/A	Remain near zero
2023	N/A	Fall, remain near zero

Source: Bloomberg analysis of Federal Reserve documents
Note: The Federal Reserve eliminated the adverse scenario from stress tests in 2020. All years also include a baseline scenario that typically features gradual interest-rate increases associated with moderate economic expansion.
Bloomberg

Investigations and Next Steps

On March 17, following reports that SVB's and Signature Bank's executives had played a part in, and may have profited from the banks' failures, the Biden Administration called to Congress to strengthen penalties against banking executives if mismanagement contributed to their institutions' failures.[34] The same day, Ranking Member Waters announced she will be crafting legislation to enhance executive authority around bank failures to better protect depositors, and sent a letter to the Fed, FDIC and SEC urging them to finish bank compensation rules, and use their available enforcement tools to hold executives accountable for any unlawful activity.[35]

In addition, Chairman McHenry and Ranking Member Waters sent a joint letter to the Government Accountability Office (GAO) calling for a study and investigation into the recent collapse of SVB and Signature Bank, in particular, to examine the factors that led to the mismanagement of both banks, including any regulatory or examination failures.[36] Specifically, the letter asks GAO to examine stock sales and bonus payments made just before SVB's closures, as well as the role of investment bank underwriters, credit rating agencies, and the Federal Home Loan Bank system.

[33] Bloomberg, *Fed's Bank Tests Overlooked Risk of Rapid Rise in Interest Rates* (Mar. 15, 2023).
[34] Bloomberg, *Biden Seeks Tougher Penalties on Executives of Failed Banks* (Mar. 17, 2023).
[35] FSC, *Ranking Member Waters Announces Legislation in Progress to Strengthen Administration's Authorities on Clawbacks and Penalties, Urges Regulators to Finish Rules and Use Existing Authorities to Hold Executives Accountable Following Bank Failures* (Mar. 17, 2023).
[36] FSC, *Ranking Member Waters, Chair McHenry Send Letter to the Government Accountability Office Urging Immediate Study, Investigation into Recent Bank Failures* (Mar. 17, 2023).

Additional Information and Background

- FDIC: Subsidiary of New York Community Bancorp, Inc., to Assume Deposits of Signature Bridge Bank, N.A., From the FDIC
- Treasury, FDIC and Fed: Joint statement on the approval of actions to complete resolutions of Silicon Valley Bank and Signature Bank
- Fed: Federal Reserve Board announces it will make available additional funding to eligible depository institutions to help assure banks have the ability to meet the needs of all their depositors
- Fed: Coordinated central bank action to enhance the provision of U.S. dollar liquidity
- FDIC: Failed Bank Information for Silicon Valley Bank, Santa Clara, CA
- FDIC: FDIC Establishes Signature Bridge Bank, N.A., as Successor to Signature Bank, New York, NY
- FDIC: When a Bank Fails - Facts for Depositors, Creditors, and Borrowers
- Fed: Discount Window Lending
- CRS: Bank Failures and the FDIC
- CRS: Federal Deposit Insurance for Banks and Credit Unions
- CRS: Federal Reserve: Emergency Lending
- CRS: The Federal Home Loan Bank (FHLB) System and Selected Policy Issues
- CRS: Over the Line: Asset Thresholds in Bank Regulation
- CRS: Enhanced Prudential Regulation of Large Banks
- CRS: Economic Growth, Regulatory Relief, and Consumer Protection Act (P.L. 115-174) and Selected Policy Issues