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July 21, 2023

Via U.S. Mail and electronic submission

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

James P. Sheesley, Assistant Executive Secretary,
Federal Deposit Insurance Corporation,
Attention: Comments-RIN 3064-AF93,
550 17th Street NW,
Washington, DC 20429

RE: RIN 3064-AF93: Proposed Rule Imposing Special Assessment Pursuant to Systemic Risk Determination - Comment from Oklahoma, Idaho, Louisiana, Mississippi, South Carolina, South Dakota, Tennessee, Texas, and Utah

Dear Mr. Gruenberg and Mr. Sheesley,

The Federal Deposit Insurance Corporation's ("FDIC") handling of the failures of Silicon Valley Bank ("SVB") and Signature Bank ("Signature") has been nothing short of disastrous. Misplaced priorities, neglect in oversight duties, trigger-happy response, and bad decision making have culminated in this equally disastrous Notice of Proposed Rulemaking. Rather than take responsibility for its failure to provide adequate oversight, the FDIC, together with the Federal Reserve ("Fed"), the Treasury Secretary, and the President of the United States (collectively the "Federal Government"), made the arbitrary and reckless decision to invoke the systemic risk exception ("SRE") of the Federal Deposit Insurance Act ("Act") to bail out uninsured depositors of SVB and Signature. This decision has had resounding ramifications.

The unprecedented decision to invoke the SRE to protect the uninsured, elite customers of SVB and Signature culminated in this Notice of Proposed Rulemaking. The FDIC now proposes a special assessment to recoup the losses it forced upon the Deposit Insurance Fund ("DIF") from the bailout. The Attorney General for the State of Oklahoma, along with the Attorneys General for Idaho, Louisiana, Mississippi, South Carolina, South Dakota, Tennessee, Texas, and Utah (collectively "States"), write to express our disagreement with the Federal Government's decision to invoke the systemic risk exception and disappointment with the actions taken by the FDIC. The States hope this comment letter will motivate the Federal Government to re-evaluate its actions and correct its course for the betterment of the banking industry moving forward.



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I. The Federal Government’s reckless decision to invoke a systemic risk exception to bail out the elite clientele of SVB and Signature will have far-reaching and disastrous consequences.

First and foremost, the States applaud and agree with the FDIC’s decision to exclude community banks from the proposed special assessment. Small, community banks were not responsible for the actions of SVB and Signature that led to their collapse. Moreover, on every conceivable metric—total assets, depositor characteristics, business models, risk seeking behavior, growth rate, etc.—community banks are dissimilar to institutions like SVB or Signature. Importantly, community banks do not hold high ratios of uninsured deposits like SVB, Signature, and other larger institutions.¹ What’s more, community banks provide essential relationship-focused services to our communities and are not similarly situated to large, super-regional or international banking institutions who may be better positioned to absorb the shock of special assessment fees. For these reasons and more, community banks should not bear the burden of any special assessment resulting from the SVB and Signature bailouts.

But make no mistake, community banks and taxpayers will ultimately bear the brunt of the FDIC’s reckless use of the systemic risk exception to bail out SVB’s and Signature’s uninsured deposits. Perhaps most obviously, that decision creates a moral hazard.² Eliminating the insurance cap for depositors weakens “market participants’ incentives to properly manage risk if they come to expect similar emergency actions in the future.”³ This moral hazard extends not only to depositors, but to banking institutions themselves. When the Federal Government demonstrates it will bail out depositors not otherwise protected under the Act, or banks engaging in risky lending practices, it reduces their incentive to guard against financial risk themselves. “Put simply, if large depositors know that they will be bailed out in the event of bankruptcy, they will have less incentive to exercise prudence in placing deposits in well-managed banks.”⁴

The response from certain government officials only worsened this moral hazard. At the time of the bailout, President Biden assured the American people that they “can have confidence that their bank deposits will be there when they need them.”⁵ When announcing the bailout of SVB

¹ See David Hayes, *SVB, Signature racked up some high rates of uninsured deposits*, S&P GLOBAL (Mar. 14, 2023), <https://tinyurl.com/bdd243nx>.

² See Elizabeth Nolan Brown, *Everyone Is Learning the Wrong Lessons From the Silicon Valley Bank Collapse*, REASON (Mar. 13, 2023), <https://tinyurl.com/yc2s4vft>.

³ GOV’T ACCOUNTABILITY OFFICE, *Report to the Committee on Financial Services, House of Representatives: Preliminary Review of Agency Actions Related to March 2023 Bank Failures*, GAO-23-106736 at 31 (Apr. 2023), <https://www.gao.gov/assets/gao-23-106736.pdf> [hereinafter “GAO Report”].

⁴ James A. Haley, *SVB Failure Underscores the Need to Regulate Financial Intermediaries*, CENTRE FOR INT’L GOVERNANCE INNOVATION (May 24, 2023), <https://tinyurl.com/2s44v9hy>.

⁵ Statement from President Joe Biden on Actions to Strengthen Confidence in the Banking System (Mar. 12, 2023), <https://tinyurl.com/5n6rvm7v>.



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and Signature, the FDIC highlighted “our commitment to take the necessary steps to ensure that depositors’ savings remain safe.”⁶ And Treasury Secretary Yellen assured the public that “similar actions could be warranted if smaller institutions suffer deposit runs that pose the risk of contagion.”⁷ The role of market discipline will now lessen, as participants believe—rightly or wrongly—that the government will bail them out like it did SVB and Signature.

The moral hazard created by the Federal Government’s bailout will be a long-term challenge facing the banking industry and was a foreseeable consequence of invoking the SRE.⁸ Those costs will continue to hit smaller community banks hardest, whose customers and uninsured depositors will now believe that their deposits would be safer at a larger bank with a higher ratio of uninsured deposits that would be more likely to be bailed out. The Federal Government has now set a new standard for using systemic risk exceptions that puts smaller, community banks at a competitive disadvantage.

The Proposed Rule will also burden the entire banking industry, as well as American taxpayers who will ultimately bear the brunt of the special assessment fees. No matter how well-intentioned the Federal Government’s actions may be, it cannot guarantee that “[n]o losses will be borne by the taxpayer.”⁹ The special assessment may not be directly levied against them, but those costs will ultimately be passed on to taxpayers. What’s more, any needless loss to the DIF will ultimately be a loss borne by taxpayers, and the Federal Government has now signaled that future bailouts and special assessment may be on the horizon.

It has also recently come to light that the FDIC’s decision to invoke the systemic risk exception resulted in bailouts for large, wealthy tech companies and foreign firms.¹⁰ Despite the Federal Government’s characterization of the bailout as protecting “small businesses across the

⁶ Joint Statement by the Department of the Treasury, Federal Reserve, and FDIC (Mar. 12, 2023), <https://www.fdic.gov/news/press-releases/2023/pr23017.html>.

⁷ Remarks by Secretary of the Treasury Janet L. Yellen at the American Bankers Association’s Washington DC Summit (Mar. 21, 2023), <https://home.treasury.gov/news/press-releases/jy1354>.

⁸ Scott Murdoch & Marolina Mandl, *Experts flag moral hazard risk as U.S. intervenes in SVB crisis*, REUTERS (Mar. 13, 2023), <https://tinyurl.com/yuv6pzbu>.

⁹ Joint Statement, *supra* note 6; *see also* Remarks by President Biden on Maintaining a Resilient Banking System and Protecting our Historic Economic Recovery (Mar. 13, 2023), <https://tinyurl.com/3c8wf6aj>.

¹⁰ Those companies include SVB Financial Group, the holding company of SVB (\$3 billion), Sequoia, a wealthy venture capital firm backing companies including Apple, Google, and WhatsApp (\$1 billion), Kanzhun, a company backed by Chinese giant Tencent (\$902.9 million), and Altos Labs Inc., a life sciences startup backed by billionaires including Jeff Bezos and Yuri Milner (\$680.3 million). Lizette Chapman & Jason Leopold, *The Big Names That Got Backstop for Billions in Uninsured SVB Deposits*, BLOOMBERG (June 23, 2023), <https://tinyurl.com/bdzhf488>.



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country[.]”¹¹ it appears that wealthy venture capitalists and foreign interests were the main beneficiaries. Americans living in rural Oklahoma, Idaho, Louisiana, Mississippi, South Carolina, South Dakota, Tennessee, Texas, and Utah should not be forced to pay the bill for wealthy national and foreign elites and tech investors, who are savvy enough to assume their own risks. Just as Main Street should not bail out Wall Street, Red River Valley should not bail out Silicon Valley.

Instead, the wealthy investors and uninsured depositors of SVB and Signature, as well as those institutions and their parent companies, should bear responsibility for the consequences of their risk-prone decision making. President Biden recognized that when it comes to investors of the bank, “[t]hey knowingly took a risk and when the risk didn’t pay off, investors lose their money. That’s how capitalism works.”¹² Ironically, however, the Federal Government fails to acknowledge this same principle when it comes to wealthy venture capitalists with uninsured deposits at SVB and Signature. Middle America, community banks, and even larger banks who rightly decided not take on the same unnecessary and significant risks as SVB and Signature, should not bear that burden.

II. The FDIC’s misguided priorities and neglect in oversight caused the crisis that predicated the invocation of a SRE to bail out SVB and Signature.

A. Misguided priorities.

The FDIC’s misguided priorities clearly contributed to, if not caused, the neglect leading to this self-induced crisis. The FDIC describes its core mission as providing regulatory oversight that “maintain[s] stability and public confidence in the nation’s financial system.”¹³ The FDIC’s statutory mandate is to “insure . . . the deposits of all banks and savings associations which are entitled to the benefits of insurance[.]” 12 U.S.C. § 1811(a), and to protect the Deposit Insurance Fund (“DIF”) from increasing losses. 12 U.S.C. § 1823(c)(4)(E)(i).

As the Attorneys General for Utah, Oklahoma, and fourteen other states wrote back on March 21, 2023, “your authority is limited solely to ensuring the safety and soundness of financial institutions” and “rather than decreasing risk to the financial system, the administration’s continued focus on combatting climate change actually increased that risk.”¹⁴ As the Attorneys General highlighted, “your focus on ‘climate risk’ incentivizes risk managers and bank examiners to focus on items other than those that truly present existential risk to institutions and systemic risk

¹¹ Remarks by President Biden, *supra* note 9.

¹² *Id.*

¹³ FDIC, *About FDIC*, <https://www.fdic.gov/about/what-we-do/> (May 15, 2020); *see also* FDIC, *The First Fifty Years* at 3 (1984), <https://www.fdic.gov/bank/historical/firstfifty/chapter1.pdf> (1984).

¹⁴ *See generally* Letter from Sean D. Reyes et al. to Janet L. Yellen et al. at 3-4 (Mar. 21, 2023), <https://tinyurl.com/5djchfvz> [hereinafter “AG Letter”].



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to the financial system.”¹⁵ In addition, the FDIC has recently emphasized its ongoing commitment to diversity, equity, and inclusion (“DEI”), claiming these principles “are fundamental aspects of the FDIC’s work”¹⁶ The FDIC’s Director of the Office of Minority and Women Inclusion promised this commitment to DEI would “impact not only our workforce, but the banking system and—even more broadly—our communities and our country.”¹⁷ She further confirmed back in 2020 that the FDIC was “work[ing] to create a more inclusive banking and financial system,” including by “exploring additional ways to increase outreach efforts to further encourage and guide regulated institutions to implement diversity policies and best practices”¹⁸

The FDIC’s misguided decision to prioritize left-wing political goals distracted it from its statutory mandate and core mission: providing regulatory oversight and protecting both insured deposits and the DIF. This, in turn, contributed to the failures of SVB and Signature, which led to the extraordinary invocation of a systemic risk exception and the Notice of Proposed Rulemaking. The decision to protect uninsured depositors of SVB and Signature directly undermined the FDIC’s obligation to protect *insured depositors* and the DIF, and likely would not have occurred had the FDIC provided appropriate regulatory oversight. The FDIC’s decision reflects a failure to adhere to its core mission.

B. Neglect in oversight.

Although the FDIC’s general neglect in regulatory oversight was apparent at the time of the bank failures in early March,¹⁹ the U.S. Government Accountability Office (“GAO”) recently confirmed those errors in an April 2023 report.²⁰ In the report, the GAO found regulators identified numerous concerns with SVB and Signature in the five years prior to the banks’ failures, “but both banks were slow to mitigate the problems the regulators identified and regulators did not escalate supervisory actions in time to prevent the failures.”²¹ Specific to the FDIC, the GAO concluded that despite taking some “actions to address supervisory concerns related to Signature Bank’s liquidity and management,” the FDIC “did not substantially downgrade the bank until the day before it failed.”²² In sum, the FDIC and the Fed missed warning signs of SVB and Signature’s impending collapse.

¹⁵ *Id.* at 5.

¹⁶ Message from Acting Chairman Gruenberg – Equal Employment Opportunity Policy Statement (June 2, 2023), <https://www.fdic.gov/about/diversity/eeostatement.html>; *see also* FDIC, *Diversity Equity and Inclusion: 2021-23 Strategic Plan*, <https://tinyurl.com/328fy39s>.

¹⁷ DIVERSITY PROFESSIONAL, *A conversation with Nikita Pearson* (Fall 2021), <https://tinyurl.com/h6ccvrvm>.

¹⁸ Statement of Nikita Pearson (Sept. 8, 2020), <https://tinyurl.com/5f2epd2j>.

¹⁹ *See* AG Letter *supra* note 14 at 3-4.

²⁰ *See* GAO Report, *supra* note 3.

²¹ *Id.* at PDF p. 2.

²² *Id.*



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As the GAO report confirmed: “[i]n the years prior to 2023, [the Fed] and FDIC identified liquidity and management risks at SVB and Signature Bank—key drivers of the banks’ failures. However, neither regulator’s actions resulted in management sufficiently mitigating the risks that contributed to the banks’ failures.”²³ By May of 2022—over ten months prior to the bank failures—the Federal Reserve’s Large and Foreign Banking Organization Program conducted a targeted review of SVB and “found that the bank’s governance and risk management practices were below supervisory expectations.”²⁴ The GAO report concluded that “[t]aking more decisive actions in the years prior to Signature Bank’s failure could have helped compel bank management to mitigate the liquidity and management weaknesses that contributed to the bank’s failure.”²⁵ A similar review of the SVB failure by the Fed concluded that SVB “failed because of a textbook case of mismanagement by the bank” and because “Federal Reserve supervisors failed to take forceful enough action”²⁶ Even the FDIC itself recognized that it “could have been more forward-looking and forceful in its supervision[.]” although it fell far short of accepting full responsibility for its role in the collapse of SVB and Signature.²⁷

The fall of SVB and Signature was also predictable based on key signals of risk such as the institutions’ rapid growth and disproportionately high ratio of uninsured deposits. As the GAO report highlighted, between 2019-2021, the total assets of both banks grew by 198% and 134% respectively—approximately four to six times the median growth rate of peer banks.²⁸ At the end of 2021 both SVB and Signature reported uninsured deposits totaling 80% and 82% of their assets, respectively—approximately double the ratios of their peers who reported median uninsured deposits ranging from 31%-41%.²⁹ The disproportionate reliance on uninsured deposits indicated “a long-standing concentration of risk.”³⁰ Despite all these risk signals, neither SVB nor Signature made the FDIC’s Problem Bank List at the end of 2022, reflecting how deep the neglect in oversight ran.³¹ And the FDIC cannot lay blame at the feet of existing laws and regulations, which were more than adequate to allow the FDIC to fully and forcefully address the problems. Had the FDIC adhered to its core function of providing adequate oversight, it may have been able to prevent

²³ *Id.* at 17.

²⁴ *Id.* at 20.

²⁵ *Id.* at 26.

²⁶ Michael S. Barr, *Re: Review of the Federal Reserve’s Supervision and Regulation of Silicon Valley Bank*, BD. OF GOVERNORS OF THE FED. RESERVE SYSTEM at 1 (Apr. 28, 2023), <https://tinyurl.com/2p96hmkz>; *see also id.* at 75 (“Stronger or more specific supervisory guidance or rules on incentive compensation for firms of SVBFG’s size, complexity, and risk profile—or more rigorous enforcement of existing guidance and rules—may have mitigated these risks.”)

²⁷ FDIC, *FDIC’S Supervision of Signature Bank* at 5 (Apr. 28, 2023), <https://tinyurl.com/5ut6s7ef>.

²⁸ GAO Report, *supra* note 3 at 11.

²⁹ *Id.* at 13-14.

³⁰ *Id.* at 13.

³¹ FDIC, *FDIC Quarterly 2023 Vol. 17, 1, Insured Institution Performance*, <https://www.fdic.gov/analysis/quarterly-banking-profile/qbp/2022dec/qbp.pdf>.



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the collapse of SVB and Signature in the first place, or at least adequately mitigate adverse effects without invoking the systemic risk exception.

III. The Federal Government’s decision to invoke a systemic risk exception to bail out uninsured depositors of SVB and Signature was improper, arbitrary, and capricious.

The systemic risk exception can only be invoked after a determination that compliance with the least-cost resolution framework “would have serious adverse effects on economic conditions or financial stability; and . . . any action or assistance under this subparagraph would avoid or mitigate such adverse effects” 12 U.S.C. § 1823(c)(4)(G)(i). Neither mandatory prerequisite was satisfied in the use of the SRE to bail out of SVB and Signature.

A. The FDIC’s decision to bail out uninsured depositors of SVB and Signature was highly unusual and unsupported by historical precedent.

Before invoking the systemic risk exception to bail out uninsured depositors of SVB and Signature, the SRE had only been invoked five times—all occurring during the 2008 financial crisis.³² The unprecedented nature of the 2008 financial crisis hardly needs further explanation. But as one point of comparison, in November of 2008 the Chicago Board Options Exchange’s (“CBOE”) Volatility Index, “a key measure of market expectations of near-term volatility[,]” reached an all-time high of 80.86.³³ In contrast, the CBOE Volatility Index was down to 26.52 on March 13, 2023 when the SRE was invoked for SVB and Signature—also down from a historic high of 82.69 in March of 2020.³⁴ Similarly, the unofficial FDIC “Problem List” included 117 banks in the third quarter of 2008, versus only 39 in the fourth quarter of 2022.³⁵

Prior uses of the systemic risk exception all had a common thread absent here—they involved very large failing institutions that were deeply interconnected to other financial institutions. For example, when the SRE was proposed for Wachovia in 2008, the banking organization was the fourth (4th) largest in the U.S., with over \$800 billion in assets and \$780 billion in deposits.³⁶ Wachovia was deeply connected to other financial institutions, meaning losses to shareholders would lead to direct and significant losses at other financial institutions.³⁷

³² Marc Labonte, CONG. RSCH. SERV., *Bank Failures: The FDIC’s Systemic Risk Exception*, IF12378 at 1-2 (Apr. 11, 2023), <https://crsreports.congress.gov/product/pdf/IF/IF12378>.

³³ FDIC, *Crisis and Response: an FDIC History, 2008-2013* at 79 n.36 (2018), <https://tinyurl.com/nrzp9ejk> [hereinafter “FDIC History”].

³⁴ CBOE, *Historical Data for CBOE VIX Index*, <https://tinyurl.com/yxu4bc8m>.

³⁵ FDIC, *Crisis and Response: An FDIC History, 2008-2013: Figure 4.7 Status of Institutions on Problem Bank List, 2008 – Q1 2017*, <https://tinyurl.com/274pfcpy> (last updated Dec. 18, 2017); FDIC, *Number of FDIC-Insured Institutions on the “Problem Bank” List*, <https://tinyurl.com/2vtxnwr5>.

³⁶ FDIC History *supra* note 33 at 69-70.

³⁷ *Id.* at 71-73.



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When the SRE was proposed for Citigroup, Inc. in 2008, it was one of the largest financial institutions in the world—boasting assets of over \$2 trillion and deposits around \$1.2 trillion.³⁸ Citigroup owned numerous banking and nonbanking entities or subsidiaries, “had an extensive international presence[,]” and “was a major participant in numerous domestic and international payment, clearing, and central counterparty arrangements”³⁹ In the wake of other major bank failures and the difficulty in finding potential acquirers with the size, complexity, and breadth of Citigroup’s operations, the potential failure plainly presented a serious systemic risk to the banking industry.

These facts stand in stark contrast to the circumstances surrounding the failure of SVB and Signature—institutions that were not particularly large, complex, or interconnected to other financial institutions. Around the time of their collapse, SVB was the sixteenth (16th) largest bank in the U.S. and Signature was the twenty-ninth (29th) largest bank in the U.S.⁴⁰ SVB had assets of approximately \$209 billion and deposits of approximately \$175 billion, while Signature had assets of approximately \$110 billion and deposits of approximately \$89 billion.⁴¹ The depositors of SVB and Signature were mostly linked to businesses financed through venture capital, not financial institutions.⁴² The FDIC barely attempted to explain the supposed systemic risk presented by the SVB and Signature failures, summarily declaring that invoking an SRE was necessary “to protect the U.S. economy by strengthening public confidence in our banking system.”⁴³

The invocation of the systemic risk exception here was unique for other reasons as well. Only one of the five planned prior uses of SRE⁴⁴ resulted in a net cost to the Deposit Insurance Fund, and because the cost of the program was offset—indeed exceeded—by another program enacted at the same time, the FDIC did not need to levy a special assessment.⁴⁵ This bailout of SVB and Signature was the first time the SRE has been invoked and implemented with a net cost to the DIF requiring a special assessment. The fact that the FDIC protected the DIF in one of the

³⁸ *Id.* at 78.

³⁹ *Id.*

⁴⁰ GAO Report, *supra* note 3 at 1.

⁴¹ *Id.* at 9-10.

⁴² Statement of Martin J. Gruenberg, Chairman FDIC, on the Federal Regulators’ Response to Recent Bank Failures before the Comm. on Fin. Servs. U.S. H. of Reps. at 5-6, 8 (Mar. 29, 2023), <https://tinyurl.com/3pmwpxhd> (describing that SVB’s deposits “were associated with its commercial and private banking clients, mostly linked to businesses financed through venture capital” and “Signature Bank was a commercial bank with several business lines.”).

⁴³ Joint Statement, *supra* note 6; *see also* Minutes of the Financial Stability Oversight Council at 3 (Mar. 12, 2023), <https://tinyurl.com/bdz75346> (citing a conclusory fear of “a meaningful contagion effect that had the potential to impact additional institutions and warranted extraordinary intervention”).

⁴⁴ Of the five prior SRE recommendations, only two were actually implemented.

⁴⁵ *See* Labonte, *supra* note 32 at 2.



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worst financial crises the country has ever faced yet incurred \$22 billion in losses to bail out two inconsequential banks here, speaks volumes.

Bank failures and losses to uninsured depositors were also not a unique occurrence before SVB and Signature. Before March of 2023, the FDIC allowed over 500 banks to fail, with collective assets totaling \$721 billion and deposits totaling \$522 billion.⁴⁶ Seven of those banks were located in Oklahoma, and the last bank to collapse before the 2023 SVB and Signature bailout was a Kansas Almena State Bank in the fall of 2020.⁴⁷ The bank at issue in one of those failures held \$307 billion in assets and \$188 billion in deposits—more than SVB and Signature at the time of their respective collapses.⁴⁸ When banks fail, uninsured depositors historically lose money.⁴⁹ Yet, none of these failed banks or their uninsured depositors received the same type of preferential treatment given to SVB and Signature this year, reinforcing the evident moral hazard resulting from the Federal Government’s reckless decision.

The unprecedented decision to invoke the systemic risk exception here suggests that the FDIC was acting out its dream of eliminating the statutory deposit insurance cap rather than acting in the best interests of the public and banking industry. The FDIC wasted no time using the failures of SVB and Signature as an opportunity to advocate for reform, writing that “[d]eposit insurance reform merits consideration in the wake of bank runs in March 2023 and trends that may have increased the susceptibility of the system more broadly.”⁵⁰ The FDIC engaged in similar advocacy before,⁵¹ except this time it acted unilaterally through the SRE instead of petitioning Congress. The FDIC’s work-around conflicts with directives of Congress, who selected the deposit insurance limit “because there is an expectation that depositors above the limit should be financially sophisticated enough to monitor their banks’ riskiness (i.e., impose market discipline).”⁵² The arbitrary and capricious decision to invoke the SRE to remove that limit for all depositors of SVB and Signature illustrates a contempt for congressional directives, as well as the limits of the FDIC’s

⁴⁶ FDIC, *Failed Bank List*, <https://www.fdic.gov/resources/resolutions/bank-failures/failed-bank-list/> (last updated May 1, 2023) (showing 566 entries).

⁴⁷ *Id.*

⁴⁸ FDIC History, *supra* note 33 at 28.

⁴⁹ Norbert Michel, *McKernan Underscores Problems with FDIC’s Systemic Risk Exception*, CATO INST. (May 16, 2023), <https://tinyurl.com/2jyxbau2> (“[A]s the FDIC’s own report explains, uninsured depositors historically lose money when banks fail – almost a 25 percent haircut prior to the 2008 financial crisis”).

⁵⁰ FDIC, *Options for Deposit Insurance Reform* at 55 (May 1, 2023), <https://tinyurl.com/4sutvuz4>; see also *id.* at 44-46 (exploring removing the insurance cap altogether)

⁵¹ Yuki Noguchi, *FDIC Wants To Raise Deposit Insurance Limit*, NPR (Oct. 1, 2008) <https://www.npr.org/2008/10/01/95236442/fdic-wants-to-raise-deposit-insurance-limit>.

⁵² See Labonte, *supra* n.32 at 2; see also 12 U.S.C. § 1821(a)(1)(E) (setting the standard maximum deposit insurance cap at \$250,000).



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role. It also raises serious questions about whether the Federal Government will improperly invoke the SRE for other purposes going forward.

B. The Federal Government never treated SVB and Signature as systemically important before their collapse.

Before the collapse of SVB and Signature, the Federal Government did not treat either bank as systemically important. Again, SVB and Signature were only the 16th and 29th largest banks in the U.S. Although the institutions may have been large in an ordinary sense,⁵³ the Federal Reserve did not consider either “large financial institutions” or “[f]irms identified as posing elevated risk to U.S. financial stability”⁵⁴ Neither SVB nor Signature was systemically important enough to undergo the 2022 Federal Reserve Stress Test, a test designed to “assess[] how large banks are likely to perform under a hypothetical recession”⁵⁵ Nor was either institution large enough to submit a Living Will (or Resolution Plan).⁵⁶ Finally, neither SVB nor Signature appeared on the 2022 List of Global Systemically Important Banks (G-SIBs) maintained by the international Financial Stability Board.⁵⁷

Others agree that neither SVB and Signature were systemically important, and that the failure of these “two mid-sized banks, in isolation, posed little risk to the economy or financial system.”⁵⁸ Moreover, the Fed’s 2022 Financial Stability Report failed to forecast any of the issues preceding the failures of SVB and Signature, instead “assur[ing] the American public that the banking system was financially sound, liquid and well-capitalized.”⁵⁹ Because the Federal Government failed to consider either SVB or Signature systemically important, and indeed SVB and Signature were not systemically important, compliance with the normal least-cost resolution framework in the winding down of SVB and Signature would not have had “serious adverse effects on economic conditions or financial stability” 18 U.S.C. § 1823(c)(4)(G)(i)(I).

⁵³ FED. RESERVE, *Insured U.S.-Chartered Commercial Banks That Have Consolidated Assets of \$300 Million or More*, <https://tinyurl.com/5y34pwz6> (Dec. 31, 2022).

⁵⁴ BD. OF GOVERNORS OF THE FED. RESERVE SYS., *Large Financial Institutions*, <https://tinyurl.com/yck76yvc> (last updated Dec. 18, 2020).

⁵⁵ BD. OF GOVERNORS OF THE FED. RESERVE SYS., *2022 Fed. Reserve Stress Test Results* at v (June 2022), <https://tinyurl.com/kfsy3hrz>.

⁵⁶ BD. OF GOVERNORS OF THE FED. RESERVE SYSTEM, *2022 Resolution Plans*, <https://tinyurl.com/387t8v4v> (last updated June 23, 2023).

⁵⁷ FIN. STABILITY BD., *2022 List of Global Systemically Important Banks (G-SIBs)* (Nov. 21, 2022), <https://www.fsb.org/wp-content/uploads/P211122.pdf>.

⁵⁸ Labonte, *supra* note 32 at 2.

⁵⁹ Paul H Kupiec, *Supervisory lessons from the SVB Failure*, AM. ENTER. INST. at 14 (May 17, 2023), <https://tinyurl.com/w3c9725u>.



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While the bailouts of the 2008 financial crisis begged the question are some banks “too big to fail[?]” the use of the SRE to bail out two isolated and inconsequential institutions now begs the question: are all banks “too big to fail[?]”

On the one hand, if SVB and Signature were systemically important (despite the Federal Government’s treatment to the contrary), it only raises more questions about how deeply rooted the FDIC and other federal agencies’ lack of oversight ran, and whether the FDIC should have invoked procedures under the Dodd-Frank Act instead of declaring a SRE. If these institutions were part of the “too big to fail” group, why wouldn’t their collapse trigger the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”)? The Dodd-Frank Act was designed to reduce the likelihood of systemic risk after the banking collapse of 2008 and “to end ‘too big to fail . . .’.”⁶⁰ SVB’s parent company, SVB Financial Group (“SVB Holding”), was a bank holding company (BHC) subject to enhanced prudential regulatory requirements under the Dodd-Frank Act.⁶¹ The Dodd-Frank Act has its own back-up resolution mechanism, the Orderly Liquidation Authority (OLA), which should have been used for SVB in lieu of declaring an SRE—that is if SVB’s closure were truly a systemic risk. Indeed, SVB Holding likely had sufficient assets to support the depositors from the failing SVB bank,⁶² calling into question whether the FDIC’s SRE declaration violated the Dodd-Frank Act’s promises.⁶³

On the other hand, if SVB and Signature were not systemically important (consistent with the Federal Government’s treatment), it only undermines the decision to invoke the systemic risk exception. SVB and Signature weren’t Citigroup, Bank of America, or JPMorgan—so how could the Federal Government so easily conclude the banking system couldn’t afford an ordinary wind-up process under the least-cost resolution framework? In either scenario, declaring a SRE to bail out the uninsured depositors of SVB and Signature was arbitrary and capricious, and in conflict with the text of the Act.

C. *Bailing out uninsured depositors would not avoid or mitigate adverse economic effects.*

To the extent the FDIC could claim the least-cost resolution framework for SVB and Signature would have serious adverse effects on economic conditions or financial stability, the specific action taken under the systemic risk exception—bailing out uninsured depositors—would

⁶⁰ H.R. 4173, Pub. L. 111-203, 124 Stat. 1376 (Jul. 21, 2010), <https://tinyurl.com/muaad6te>.

⁶¹ SVB Holding was a Category IV bank, making it subject to the Dodd-Frank Act, but not subject to the more stringent requirements of large financial institutions. GAO Report, *supra* note 3 at 19.

⁶² Michel, *supra* note 49 (“Selling the \$100 billion (plus) portfolio, even with the losses from recent interest rate increases, would have covered the \$18 billion insured deposits nearly five times over.”).

⁶³ See Arthur E. Wilmarth Jr., *The SVB and Signature bailouts broke Dodd-Frank's promises*, AM. BANKER (Apr. 25, 2023), <https://tinyurl.com/2s4jwawu>; Paul Kupiec, *Why did regulators ignore Dodd-Frank and orderly liquidation for failed banks?* THE HILL (Mar. 16, 2023), <https://tinyurl.com/5drky5cp>.



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not “avoid or mitigate” them. 12 U.S.C. § 1823(c)(4)(G)(i)(II). Again, any fear of adverse economic effects is patently unreasonable in light of the FDIC’s prior failure to treat either institution as systemically important. Thus, invoking the SRE could not avoid or mitigate effects that are non-existent or grossly exaggerated. In addition, by law, the SRE was unable to be used until after the collapse of SVB and Signature.⁶⁴ Consequently, by the time SRE was invoked, any predominant adverse effects should have already materialized.

To the extent the FDIC considered a generic fear of bank runs as the “serious adverse effect[]”, that fear would have only extended to *uninsured* depositors. Because the FDIC’s directive is to protect *insured depositors* and the balance of the DIF, that fear exceeded the FDIC’s statutory mandate.⁶⁵ Even under a broader interpretation of the FDIC’s purpose, however, “[t]he threat of bank runs may also deter bank risk-taking if bank management perceives that the risk of a run threatens bank franchise value.”⁶⁶ In other words, such a threat in general can promote financial stability and reduce broader market disruptions, as well as moral hazard that can result from extending deposit insurance.⁶⁷ Here, setting aside the statutory insurance cap would not have mitigated any adverse effects on economic conditions or financial stability.

In sum, because the use of a systemic risk exception to bail out elite customers of SVB and Signature was improper in the first place, the Notice and Proposed Rulemaking requiring a special assessment is fundamentally flawed. The FDIC cannot now hide behind the mandatory language of the law requiring a special assessment.⁶⁸ That mandate is based on the premise that the SRE was properly invoked in the first place. The States posit it was not, and that the FDIC’s actions invoking the SRE were reckless, arbitrary, and capricious.

IV. Conclusion and Recommendations.

In conclusion, the banking industry and public at-large should not be forced to subsidize the Federal Government’s mishandling of a crisis of its own creation. The States denounce the irresponsible decision-making that led to the use of the systemic risk exception to bail out SVB and Signature, and respectfully implore the FDIC to reverse course on its proposed special assessment.

⁶⁴ See, e.g., Statement of Martin J. Gruenberg, *supra* note 42 at 1 (noting “that these two institutions were allowed to fail.”); 12 U.S.C. § 1823(c)(4)(G)(i)(I).

⁶⁵ See, e.g., Kupiec, *supra* note 60 at 16 (“Under normal FDIC rules, because of the magnitude of their uninsured deposit balances, SVB and Signature Bank could have been resolved without any losses to the FDIC deposit insurance fund. Zero losses.”).

⁶⁶ *Options for Deposit Insurance Reform*, *supra* note 50 at 2.

⁶⁷ *Id.* at 2, 30.

⁶⁸ See Statement of Martin J. Gruenberg, *supra* note 42 at 2, 18 (suggesting a special assessment was “required by law” and that “the loss to the DIF arising from the use of a systemic risk exception must be recovered from one or more special assessments”).



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If the FDIC is not willing to reverse course, at a minimum, the special assessment should be borne only by those firms and entities directly responsible for or benefitting from the bailout. The Federal Government has promised that “those responsible” will be held accountable and that “no one is above the law.”⁶⁹ Yet, the Notice of Proposed Rulemaking does the opposite. Even banks with large uninsured deposits presumably have vastly different portfolios and management and oversight practices to the failed SVB and Signature. The same cannot be said for the parent holding company of SVB, SVB Financial Group, Inc., who had almost \$2 billion in deposits at SVB and yet somehow escaped any Dodd-Frank implications. It also cannot be said for venture capitalists who made the conscious decision to risk their money at poorly managed institutions like SVB or Signature. If the uninsured depositors were conducting their business in a responsible manner, however, the bailout also should have been unnecessary. Those entities should have been able to meet financial obligations under the ordinary winding up process. At least one major depositor at SVB has expressed that view.⁷⁰

Again, it is fundamentally unfair to pass on special assessment costs to other banking institutions who engaged in responsible business practices, unlike SVB and Signature. The States reiterate that it would be even more fundamentally unfair to pass on special assessment costs to community banks.

Although it is difficult to admit error, the States hope that the FDIC will do that here and reverse course on its Proposed Rule. The States also expect the FDIC to take responsibility for its part in the collapse of SVB and Signature, and the erroneous invocation of the systemic risk exception. If the FDIC can take away the correct lessons from these unfortunate circumstances, the banking industry will be better off for it.

Respectfully,



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⁶⁹ Remarks by President Biden, *supra* note 9.

⁷⁰ Chapman & Leopold, *supra* note 10 (describing that Marqueta Inc., with \$634.5 million deposited at SVB, acknowledged that “our ability to execute as a business and meet our financial obligations would not have been impacted, even if it was a longer resolution process”).



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