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Financial Institutions

Industry Update: What the FDIC's SVB Lawsuit Means for Financial Institutions and How to Stay Protected

The FDIC's recent legal action against former SVB Financial directors underscores the importance of sound governance and risk management for all financial institutions.

Note from CAC Group
As an experienced advisor in risk management and insurance for financial institutions, CAC Group is committed to keeping our clients informed about developments that could impact governance, liability, and regulatory oversight. While CAC Group is not affiliated or a party with the entities involved in this case, we believe the lawsuit presents valuable lessons and reminders about the importance of strategic risk planning and robust insurance programs.

Summary of FDIC Lawsuit against Silicon Valley Bank:

The Federal Deposit Insurance Corporation (FDIC) filed a negligence and breach of fiduciary lawsuit against former directors and officers of Silicon Valley Bank (SVB) on January 16, 2025. The lawsuit is a good example of the significant exposure executives and directors of banks face when they are taken over by the FDIC. The personal risk is even greater when you consider that their Directors & Officers (D&O) insurance might already be eroded through other shareholder actions brought against both executives and the entity previously.

Background:

SVB failed in March of 2023, which was the second largest bank failure in the history of the US. The bank grew from $70 billion in assets in 2019 to $209 billion by the end of 2021. There are various factors which lead to the bank's failure, some of which are directly alleged in the complaint as described below:

- SVB had a highly concentrated deposit base focused on technology and life-sciences sectors. By the end of 2022, more than half of total deposits were comprised of venture capital backed companies. Approximately 94% of SVB's deposit base was uninsured which made them a significant flight risk as well.

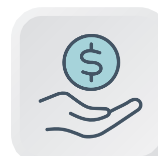
- During the low interest-rate environment, SVB purchased billions of dollars' worth of long-term securities at low and fixed interest rates.
- SVB's closure was effectively driven by a run on the bank. As interest rates began rising in March of 2022, the value of SVB's long-term fixed loan portfolio declined. This would have been fine if they could hold loans through maturity, but unfortunately a series of deposit withdrawals meant they needed to sell the securities at a loss.
- When the news circulated that the bank was raising capital, their share price declined—which led to further deposit withdrawals. Finally, on March 10 of 2023 regulators stepped in and assumed control of the bank.

Summary of the Complaint:

- The lawsuit names 17 individual defendants. 6 of the defendants were former officers, including the former CEO and CFO (along with various other officers). The other 11 defendants were all directors of SVB. Some of the officers also served as directors.
- The lawsuit alleges negligence, gross negligence, and breaches of fiduciary duties. Specifically, the complaint alleges that interest-rate and liquidity risks were mismanaged and that the directors and officers prioritized short-term profits while assuming unreasonable risks.
- There were 3 ways in which the defendants allegedly breached their fiduciary duties:

1. Defendants overexposed the bank to investments in long-term securities— held primarily in their unhedged securities portfolio to try and increase yield.

2. Defendants decided to terminate interest-rate hedges on its available-for-sale (AFS) securities portfolio. These hedges were designed to protect SVB's portfolio from losses if interest rates rise.



3. Finally, some of the defendants agreed to pay a $294 million bank-to-parent dividend less than 3 months before SVB's failure.

- As a result of the above actions, the FDIC seeks to recover billions of dollars in damages.

D&O Insurance Considerations:

- D&O insurance is limited. SVB's D&O insurance tower may already be substantially eroded by other claims brought against the entity and D&O's.
- It's important to carry sufficient dedicated Side A excess liability insurance. The traditional public company D&O insurance policy includes entity coverage for securities claims (SVB had securities class action lawsuits filed against them as well), which means that the limit can be eroded quickly defending the entity. Individual directors and officers need their own dedicated personal protection, which shouldn't be eroded by claims brought against the entity.
- Finally, directors should consider purchasing independent director liability (IDL) coverage as well. This is dedicated coverage for independent directors (not including officers) to ensure that they are appropriately protected in their roles.

Ask Your Broker

In light of this industry development, CAC Group recommends that clients proactively assess their Directors and Officers (D&O) liability coverage to ensure adequate protection.

01 How much D&O, side A, independent director liability (IDL), and outside director liability (ODL) insurance coverage should I purchase? Do I purchase sufficient side A coverage to protect the assets of D&O's in a worst-case scenario?

02 Is my D&O insurance coverage appropriately designed to avoid common coverage pitfalls in an insolvency or receivership context? Side A coverage should only have a very narrow conduct exclusion or no exclusions in place.

Take the Next Step:

If you're unsure whether your current policies provide sufficient coverage for scenarios like these, or if you'd like guidance tailored to your institution's specific risks, reach out to your CAC Group advisor. We're here to help you stay protected in a rapidly evolving risk environment. :

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About CAC Group

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