

[Restricted FR]

REPORT OF HOLDING COMPANY INSPECTION



HC Name: SVB Financial Group
Location: Santa Clara, California
RSSD Number: 1031449

Inspection Commenced: December 30, 2019
Inspection Concluded: January 17, 2020
Financial Data as of: September 30, 2019

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May 8, 2020

Board of Directors
SVB Financial Group
3003 Tasman Drive
Santa Clara, California 95054

Dear Members of the Board:

The Federal Reserve Bank of San Francisco (FRBSF) conducted a full-scope inspection of SVB Financial Group (SVBFG) beginning on December 30, 2019, based on September 30th financial statements. Our inspection concluded on January 17, 2020 and overall results were reviewed with management on February 6th. This Report of Inspection (ROI) concludes the 2019 supervisory cycle.

SUMMARY CONCLUSIONS

SVBFG's overall financial condition and risk management practices are satisfactory; nonbanking activities have increased, but do not present significant financial risk to Silicon Valley Bank (SVB). While the risk management program's framework design is satisfactory, implementation of an effective challenge process continues as work in progress. SVB remains under an enforcement action for compliance with Bank Secrecy Act/Anti-Money Laundering (BSA/AML) and Office of Foreign Assets Control (OFAC) requirements, and operational and technology risk governance weaknesses were noted during the cycle. Management is receptive to supervisory feedback, and the board is encouraged to continue providing resources and oversight as necessary to assist management in maintaining a risk management program commensurate with the firm's risk profile and global operations.

SCOPE

SVBFG was inspected under the authority of section 5(c) of the Bank Holding Company Act of 1956, as amended. The inspection's primary objectives were to assess the organization's overall risk management and consolidated financial condition. We assessed the parent company's ability to act as a source of strength to SVB, reviewed intercompany transactions to determine compliance with laws and regulations, and assessed management's progress in remediating outstanding supervisory issues. The inspection results also incorporate the cycle's continuous monitoring activities.

RATINGS

SVBFG remains in satisfactory condition and is rated a composite "2" according to the Federal Reserve System's Uniform Bank Holding Company rating system. Ratings are assigned on a scale from 1 to 5 in ascending order of supervisory concern.

Rating 2 (Satisfactory). Holding companies in this group are fundamentally sound but may have modest weaknesses in risk management practices or financial condition. The weaknesses could develop into conditions of greater concern but are believed correctable in the normal course of business. As such, the supervisory response is limited. Cash flow is adequate to service obligations, and the nondepository entities are unlikely to have a significant negative impact on the subsidiary depository institution.

The table below lists SVBGG's composite, component, and subcomponent RFI/C (D) ratings assigned at this inspection, as well as those assigned at the two prior inspections.

SVB Financial Group	Current Inspection 12/30/19	Prior Inspection 12/31/18	Prior Inspection 12/04/17
R – Risk Management	2	2	2
<i>Components:</i>			
Board and Senior Management Oversight	2	2	2
Policies, Procedures, and Limits	2	2	2
Risk Monitoring and MIS	3	3	3
Internal Controls	2	2	2
F – Financial Condition	2	2	2
<i>Components:</i>			
Capital	2	2	2
Asset Quality	2	2	2
Earnings	2	2	2
Liquidity	1	1	1
I – Impact of Parent and Non-Depository Subsidiaries on Depository Institution	2	2	2
C – Composite Rating	2	2	2
(D) – Depository Institution	2	2	2

MATTERS REQUIRING ATTENTION (MRA)¹

Two new MRA related to risk management were communicated following a mid-cycle target review, but no additional issues are identified at this time. The status of outstanding matters are summarized below:

SUMMARY OF OUTSTANDING FINDINGS				
Matters Requiring Attention				
Issue	Target Area	Status	Comments	Timeframe for Completion Date ²
Investment Tracking Framework	Management - Risk Management	Close	Cited at the 12/4/17 Inspection; implementation and validation of Redacted has addressed Regulation Y compliance concerns.	Closed during this inspection
ERM Controls Monitoring	Management – Risk Management	Carry Forward	Cited at 7/29/19 Corporate Governance Target; management action plan received on 12/6/19.	3/31/21
Model Overlay/ Assumption Governance	Management – Risk Management	Carry Forward	Cited at 7/29/19 Corporate Governance Target; management action plan received on 12/6/19.	9/30/20

¹ MRA are matters that are important and that the Federal Reserve expects a banking organization to address over time.

² Management's original target date for remediation of the supervisory issue (includes audit validation as applicable).

RISK MANAGEMENT – 2

Overall risk management is satisfactory. Board and senior management oversight, policies, procedures, and limits, and internal controls are satisfactory; however, risk monitoring and management information systems (MIS) is only fair. Management has not completely established a credible, independent second line of defense (SLoD) as outlined within SVBFG's risk management framework and commensurate with the firm's growth and risk profile. Risk management related to the financial risk categories continue to mature at a reasonable pace, and BSA/AML and OFAC compliance programs are improving; however, governance and controls in the areas of technology and operational risk require enhanced attention.

Board and Senior Management Oversight – 2

Board and senior management oversight is satisfactory. The board provides adequate oversight of SVBFG's consolidated business strategies, significant policies, and risk management practices through regular committee meetings complemented by a layered risk oversight structure. Bank and corporate boards are identical and stable, allowing for a high-level understanding of bank, parent, and nonbank subsidiary activities. The January 2019 acquisition of SVB Leerink acquisition and continued global expansion of SVBFG requires an increasingly sophisticated enterprise risk management (ERM) program.

Management has demonstrated a willingness and ability to operate SVBFG in a safe and sound manner, including providing resources and oversight to address problem areas. Examiners reported SVB made significant progress in 2019 to achieve compliance with internal control issues that resulted in a January 30, 2017 Memorandum of Understanding (MOU) related to the bank's BSA/AML and OFAC compliance programs. The same attention should be given to the development of a fulsome SLoD to ensure front-line management continues to operate within the board approved risk appetite statement and designed controls remain appropriate.

Policies, Procedures, and Limits – 2

Policies, procedures and limits is satisfactory. Policies and procedures provide an appropriate level of oversight for SVBFG's business activities. Limits are tracked for compliance in various reports provided with committee packages presented to the board and senior management. The ERM Policy and Procedure Office was established to strengthen policy governance and house all policies and procedures in a centralized repository. Project plans include cataloguing and performing a control assessment of existing procedures, developing monitoring and reporting processes for ERM activities, selecting a vendor solution, and developing a migration plan to an ERM-managed central repository for improved efficiency and process consistency. Board and senior management committee packages contain various reports tracking performance levels with approved risk appetite limits.

Risk Monitoring and MIS – 3

Risk monitoring and MIS remains fair. Management continues to develop and implement a risk management framework; however, further enhancements are needed to ensure the SLoD maintains adequate oversight of functional management as the organization grows in scale and complexity. In addition, operational and security metrics are limited in number and too narrowly focused to provide a holistic view of technology operations and cybersecurity risks. Consequently, risk monitoring and MIS may not provide adequate information to identify and monitor enterprise risks and control

effectiveness. Nevertheless, management reports that examiner identified weaknesses concentrated in technology and operational risk and are being addressed.

During the supervisory cycle, progress was made establishing an independent assessment of capital, market and liquidity risks. Additionally, the board approved a transition plan to move the Chief Credit Officer to the SLoD and more appropriately separate lending and credit administration activities. Additionally, the 2017 MRA requiring enhanced investment tracking was remediated and is closed.

New MRA were identified in relation to model risk management (MRM) governance practices and ERM controls monitoring. Management's action plans appear appropriate for remediation of the MRM MRA, with plans to clarify assumptions used to support results in the areas of credit risk, earnings, and capital. The additional transparency should be reflected in SVBFG's setting of capital limits and buffers. Action plans to establish a formal program supporting functional management's development and strengthening of its Control Identification, Testing, and Monitoring program also appear reasonable. As described, the program will provide SLoD oversight, validation, and monitoring to ensure that the front line is meeting program standards including control-testing requirements, managing issues, and action plans, and reporting control testing and monitoring results to the SLoD. Management has already published some core program documentation and is expected to complete remediation efforts during first quarter 2021.

Internal Controls – 2

SVBFG's system of internal controls is satisfactory and provides adequate coverage of major risks and business activities. The audit program is independent, its methodology is adequate, scopes are reasonable based upon risk assessments, and workpapers support findings and conclusions. An external audit of SVBFG's consolidated year-end 2018 financial statements resulted in an unqualified opinion. The internal credit review (ICR) function remains independent of lending activities, and regularly reports to the board. Management is evaluating ICR to ensure the function's structure, staffing and approach continue to provide effective challenge and present an informed, independent view of credit risk activities within SVB's lending activities.

FINANCIAL CONDITION – 2

SVBFG's consolidated financial condition is satisfactory.³ Capital, asset quality and earnings are rated satisfactory; liquidity is strong. SVB accounted for 94 percent of SVBFG's consolidated assets and generated 90 percent consolidated earnings; accordingly, conclusions presented in SVB's April 13th report of examination (ROE) have been leveraged for consolidated financial analysis. Additionally, SVBFG's financial position and performance is compared against the regional banking organization (RBO) peer group consisting of 88 companies with consolidated assets between \$10 billion and \$100 billion.

Capital – 2

Consolidated capital is satisfactory. Although SVBFG does not pay common dividends, share redemption activity resulted asset growth outpacing net equity growth and all capital ratios declined during the supervisory cycle. Nevertheless, as low-risk investment securities present a large portion of total assets, SVBFG's capital ratios adjusted for asset risk remain above RBO averages. The consolidated common tier

³ Unless otherwise noted, all financial information is as-of September 30, 2019 or for the nine months ended September 30, 2019, as applicable.

one equity capital, tier one capital, total capital, and tier one leverage are 12.71 percent, 12.86 percent, 13.70 percent, and 8.64 percent, respectively.

Capital planning and oversight is acceptable; stress testing practices are adequate and receiving increased attention without a prescribed supervisory scenario and reporting framework. During 2019's fourth quarter, SVBFG redeemed \$350 million in senior debt and issued a like amount of preferred stock to improve capital efficiency and bolster its tier 1 capital level. Capital levels are anticipated to increase through 2021 as the firm achieves greater efficiencies and approaches share redemptions in a conservative manner.

Asset Quality – 2

Consolidated asset quality is satisfactory; with no low quality assets outside of SVB, the ROE informs this conclusion. Loan growth remained strong at 13 percent, and foreign office loans increased from 9 to 11 percent of total loans. Consistent with other RBOs, SVBFG's criticized and adversely classified asset ratios declined during the supervisory cycle; however, the firm's 17 percent classified asset ratio exceeds the RBO peer average of 12 percent. Additionally, SVBFG's net charge-off ratio 0.26 percent of total loans remains above the RBO peer of 0.18 percent. Problem assets are at manageable levels and consist primarily of loans centered in investor dependent and leveraged loans segments, which combine for under 20 percent of loan commitments. Further mitigating SVBFG credit risk, an investment portfolio comprising 40 percent of assets is largely comprised of U.S. Treasury and agency securities.

As noted in SVB's ROE, the methodology for maintaining an allowance for loan losses is acceptable, and the allowance's level and trend is directionally consistent with the firm's portfolio quality. Management noted it will recommend implementation of the Current Expected Credit Loss methodology in 2020, and estimates the allowance will increase by a modest amount based on current economic forecasts.

Earnings – 2

Earnings is satisfactory. Though SVBFG's 1.90 percent annualized return on average assets far exceeds the RBO average of 1.37 percent, net retained earnings did not offset asset growth and capital ratios declined. The company's operating efficiency is facilitated by a business banking strategy reflecting focus on moderately earning assets funded by large, low-cost accounts maintained by clients focused on innovation investing. The benefit of higher average loan yields and low cost funding are mitigated by a low volume of loans resulting in a net interest margin that approximates the RBO peer average. SVBFG's global expansion supports core earnings as foreign activities continue significant growth, and category loan yields and funding costs are favorable to peer averages. Management expects net interest margin to flatten as interest bearing accounts are proportionally increasing and assets are repricing faster than deposits.

Improved core earnings is largely attributable to higher non-interest income, which increased from 1.36 percent of total assets to 2.01 percent, and now exceeds the peer average. Significant portions of non-interest income are generated by nonbanking sources, namely investment banking fees and venture capital revenue. With the acquisition of SVB Leerink, nonbank earnings increased from 1.75 percent to 5.37 percent of consolidated earnings during the cycle. Additionally, significant growth in client funds maintained in offshore accounts (currently \$95 billion) contributes to fee income.

Liquidity – 1

Balance sheet liquidity is strong, and funds management practices are satisfactory. Asset liquidity includes \$6 billion in cash and interest bearing bank balances and \$24 billion in unpledged investment securities, which combine for 45 percent of total assets. Core deposits represent 80 percent of total assets, and net loans are a low 56 percent of core deposits. Although categorized as core deposits, funding concentrations exist within Private Equity and Venture Capital client accounts; SVBFG's largest 25 clients account for over 11 percent of total deposits, and under 11 percent of domestic deposits are insured. Foreign office deposits are increasing, currently accounting for 8 percent of total deposits. The bank's London branch retail deposits are projected to exceed \$1 billion British pounds in 2021, which will require the office to become a formal subsidiary of SVB.

Liquidity and funding policies are adequate, and stress testing meets supervisory expectations for regional banking organizations. In response to supervisory concern, management conducted thorough analysis of the bank's volatile funds flows and implemented a significant liquidity buffer. Access to contingent liquidity is maintained as well, with over \$5 billion in secured borrowing capacity.

IMPACT – 2

The parent company and non-depository subsidiaries present limited likelihood of a significant negative impact on SVB. Risk management of parent and nonbank activities is sufficient to mitigate the impact to the bank, and the parent continues to provide financial and managerial resources to support SVB as needed. Furthermore, the parent company's financial condition remains acceptable. Finally, the parent company remains in compliance with all laws and applicable regulations, including Regulation W.

Parent Company Financial Analysis

Parent company financials present a modest impact to the overall institution. Funding the redemption of \$500 million in common stock and the January acquisition of SVB Leerink required unusually large dividends from SVB, resulting in the bank's capital ratios declining approximately 50 basis points year-over-year; however, management shared plans to maintain the bank's tier 1 leverage ratio closer to 7.5 percent going forward. With \$697 million in subordinated debt, the debt/equity ratio was well above peer; however, with a fourth quarter issuance of non-cumulative perpetual preferred debt to replace \$350 million in senior debt, the parent leverage ratio will more closely approximate the RBO peer average.

Common dividends have not been paid since 2009, and management conducts reasonable analysis prior to executing share redemptions. Parent-only liquidity remains sufficient; \$816 million in cash and marketable securities exceed foreseeable obligations over the next 2 years. The parent's liquidity and cash flow profile indicate limited risk to the subsidiary bank, but the Contingency Funding Plan can be enhanced to include the parent and non-bank entities.

Intercompany Transactions

The bank, parent company, and non-bank subsidiaries remain in compliance with Regulation W and interagency guidelines regarding income tax allocation in a holding company structure. The majority of inter-company transactions consist of employee expenses related to work performed on behalf of nonbank subsidiaries and overhead expenses. SVB employees and departments providing services to

nonbank affiliates complete a semi-annual Regulation W Cost Allocation Survey. The survey results are used to determine the allocation of personnel and occupancy expenses charged to bank affiliates. Costs are justified in expense studies performed to allocate the various expenses incurred by SVBFG, and reimbursement are made monthly. Prior internal audit findings regarding the Regulation W program were technical in nature and have been or are in the process of correction. Finally, the inter-company tax sharing agreement and payment practices comply with supervisory guidance.

Nonbanking Activities

The strategic relevance of nonbank activities are increasing as are their impact to consolidated risk management and financial condition. These activities primarily include venture capital investment and funds management under SVB Capital, and investment bank and broker dealer activities under recently purchased SVB Leerink. Nonbank activities closely align with SVBFG's strategic plans and are being integrated into the global risk management framework, with the board and senior management providing regular and appropriate top-of-the-house oversight. During the year, management implemented a scalable investments tracking framework to remediate a prior supervisory concern regarding monitoring nonbank investing activities. Management implemented an organizational redesign to establish institutional governance, and continues to refine roles and responsibilities to ensure reasonable assurance of compliance with authorities governing permissible activities, including investment and merchant banking. Following parent company provision of acquisition funding, the nonbanking activities have generated positive cash flow to the organization.

DEPOSITORY INSTITUTION – 2

As reported in the April 13th ROE, SVB remains in satisfactory condition. Capital, Asset Quality, Management, Earnings, and Sensitivity were rated satisfactory; Liquidity was rated strong. The SVB examination included no new supervisory issues, although concerns exist in relation to technology and operational risk governance and management. Additionally, the bank has not fully complied with a 2017 MOU related to legal requirements of BSA/AML and OFAC.

OTHER MATTERS

BSA/AML and OFAC Compliance Program

The bank's BSA/AML and OFAC compliance program remains less than satisfactory. The February 5th Supervisory Letter noted significant improvements; however, SVB has not achieved full compliance with the 2017 MOU, as additional progress is needed to remediate supervisory concerns related to Know Your Customer and Customer Due Diligence practices.

Consumer Compliance

The most recent FRBSF and Consumer Financial Protection Bureau (CFPB) compliance examinations have resulted in satisfactory ratings. The CFPB's October 26, 2016 report identified violations related to loan originator compensation and Home Mortgage Disclosure Act reporting, and cited MRAs to ensure that corrective action was performed to address these violations and the FRBSF concurred with these findings. The October 22, 2018 FRBSF report noted that SVB continues to build out its consumer

compliance risk management framework, and did not identify any violations related to the non-enumerated consumer laws and regulations. SVB operates under a Strategic Plan for compliance with the Community Improvement Act, and the bank's performance was assessed as Satisfactory at the October 2018 review.

Information Technology (IT)

SVB's technology and operational risk management activities are satisfactory; however, additional MRA were cited regarding technology/operational risk governance and management, and the IT Management component was rated fair at the February 25, 2019 IT examination. The organization transitioned Chief Operating Officers on April 1, 2019, and significant changes have been set in motion to modernize the firm's capabilities and formalize governance practices related to technology and operational risk and risk management.

CLOSING COMMENTS

SVBFG remains in satisfactory condition and, as no new supervisory issues are noted, a response to this ROI is not required. However, this inspection was conducted prior to recent events associated with COVID-19, and rapidly changing economic circumstances could have an adverse impact on all banking organizations. During this time, we have paused supervisory events and will monitor the firm's financial condition and risk management practices to determine the appropriate supervisory response including future examination and inspection events. Nevertheless, each director should sign the Signature of Directors page, and the board's review of this ROI should be recorded in SVBFG's corporate records. The contents of this letter are confidential and should not be made public.

Management's cooperation throughout the 2019 supervisory cycle is appreciated, and FRBSF^{Redacted} **Redacted** and I look forward to meeting with the board to discuss the report's contents. Please direct any immediate questions or concerns related to this ROI's conclusions, or any matter involving our supervision of SVBFG, to me at **Redacted** or **Redacted**.

Redacted

Redacted
Central Point of Contact

SIGNATURE OF DIRECTORS

We, the undersigned directors of SVB Financial Group, Santa Clara, California have personally reviewed the contents of the report of inspection dated December 30, 2019.

Signature of Directors	Date
_____ Greg W. Becker	_____
_____ Eric A. Benhamou	_____
_____ John S. Clendening	_____
_____ Roger F. Dunbar	_____
_____ Joel P. Friedman	_____
_____ Kimberly A. Jabal	_____
_____ Jeffrey N. Maggioncalda	_____
_____ Mary J. Miller	_____
_____ Kate D. Mitchell	_____
_____ John F. Robinson	_____
_____ Garin K. Staglin	_____

NOTE: This form should remain attached to the report of inspection and be retained in the holding company's file for review during subsequent inspections. The signature of committee members will suffice only if the committee includes outside directors and a resolution has been passed by the full board delegating the review to such committee.