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SVB Receivership – Considerations for Agents and Lenders

By the **Global Finance Practice**

Background

- On March 10, 2023, the California Department of Financial Protection and Innovation closed Silicon Valley Bank (SVB) and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver for SVB.
- The FDIC's press release describing the creation of the "bridge bank" Deposit Insurance National Bank of Santa Clara (DINB), the treatment of SVB's deposits and potential next steps is available at: https://www.fdic.gov/news/press-releases/2023/pr23016.html.
- The FDIC:
    1) transferred all of SVB's insured deposits (amounts up to $250,000 per customer) to DINB (which amounts are expected to be available by Monday March 13, 2023);
    2) indicated it will issue an advance dividend to uninsured depositors within the next week for all or a portion of their deposits in excess of $250,000; and
    3) indicated it will issue uninsured depositors receivership certificates for any remaining balances (which such depositors may need to request from the FDIC), which may be repaid following receipt of proceeds from any future sales of SVB's assets.
- The FDIC has published FAQs and responses related to the SVB receivership, available at: silicon-valley-faq.pdf (fdic.gov) (the "FDIC FAQs"). According to the FDIC FAQs, the FDIC froze all SVB lines of credit as of March 10, 2023.
- The FDIC auction of SVB's assets began on March 11, 2023, with final bids due by March 12, 2023. On March 13, 2023, HSBC disclosed that it would purchase Silicon Valley Bank UK Ltd. for £1.
- A joint statement issued by the Department of Treasury, Board of Governors of the Federal Reserve System and FDIC on March 12, 2023 (the "Joint Statement") announced that all depositors would have access to all of their funds (including amounts in excess of the $250,000 insured deposit cap) on March 13, 2023.

Considerations if you are Agent in a Deal and SVB is a Lender:

1) Is SVB a Defaulting Lender? How do I make this determination?

Review the definition of "Defaulting Lender" in the credit agreement.

a) One prong of the definition may include any lender that has "had appointed for it a receiver, custodian … or similar Person charged with reorganization or liquidation of its business or assets, including the Federal Deposit Insurance Corporation…" Under this provision, SVB would be a Defaulting Lender.

b) Another prong of the definition normally provides that any lender which is the subject of a proceeding under "Debtor Relief Laws" constitutes a Defaulting Lender. If "Debtor Relief Laws" do not include receiverships, this provision has not been triggered because no bankruptcy proceeding has been filed by or against SVB to date.

c) Otherwise, SVB may not be a Defaulting Lender unless (among other things likely not applicable at this time), it has (1) failed to fund loans or other amounts required to be paid by it when required under the credit agreement (usually with a 1 to 2 business day grace period), (2) notified the other parties that it does not intend to fulfil its funding obligations under the credit agreement or (3) failed to respond affirmatively to a request that it confirm that it will comply with its funding obligations.

i.) In order to trigger Defaulting Lender status, consider whether to request in writing that SVB confirm that it intends to comply with its funding obligations (especially if the credit agreement would not otherwise clearly treat SVB as a Defaulting Lender).

d) Some agreements also include a provision that would treat any lender as a Defaulting Lender if it has publicly announced that it does not intend generally to comply with its funding obligations under credit agreements. Given the current state of confusion and misinformation in the market and financial press regarding SVB, and the absence of any unambiguous press release on SVB's website, SVB is probably not a Defaulting Lender based solely on this provision.

2) Are any affirmative actions required to be taken to cause SVB to be treated as a Defaulting Lender under the loan documents?

Review the credit agreement to determine whether the parties are required to deliver any formal notice to trigger treatment of SVB as a Defaulting Lender.

a) If there is no doubt that SVB constitutes a Defaulting Lender, and the credit agreement does not require notice of this determination, then no notice is required.

b) Some agreements expressly require the Agent to provide written notice to the parties of the Agent's determination that a lender constitutes a Defaulting Lender. Under these agreements, the Agent's determination is usually conclusive (absent manifest error).

c) If it is unclear whether SVB constitutes a Defaulting Lender then the Agent could send written notice to the parties to the credit agreement designating SVB as a Defaulting Lender. Sending this notice may become useful in establishing the parties' determination of whether

SVB constitutes a Defaulting Lender, and resolving any issues that could arise in the future with respect to computation of interest due to SVB (among other things).

Assuming that written notice is required to trigger treatment of SVB as a Defaulting Lender, review the notice section of the credit agreement to determine what method of delivery is required (e.g., letter, fax, courier, etc.). Best practice would be to send an email followed by hard copy using the delivery method for notices specified in the credit agreement.

3) What impact does Defaulting Lender status trigger?

a) Reallocation – SVB's reimbursement obligations with respect to letters of credit and swingline loans may be reallocated among the revolving lenders in accordance with their pro rata shares, subject to each lender's aggregate revolving commitment. Sometimes this requires an election by the Agent. *See also* question 8 below.

i) Each non-Defaulting Lender is typically entitled to the fees accruing in respect of such reallocated exposure.

b) Payments – Payments received by the Agent for the benefit of SVB (including principal, interest, fees and other amounts) would be applied pursuant to a Defaulting Lender waterfall (or, sometimes, a provision which gives Agent authority to hold and retain the amounts for various specified purposes). *See also* question 7 below.

c) Borrower's obligation to cash collateralize – The borrower may be required (at the request of the Agent, issuing bank or swingline lender) to cash collateralize SVB's portion of the contingent reimbursement obligations owing to the issuing bank or swingline lender.

d) Fees – As a Defaulting Lender, SVB will typically not be entitled to receive commitment fees and letter of credit fees on its portion of revolving commitments.

e) Voting – *See* question 10 below.

f) Replacement by the borrower – *See* question 11 below.

g) Priority of Obligations – Occasionally the post-default waterfall in the credit agreement will subordinate the obligations owing to SVB to the obligations of the non-Defaulting Lenders.

h) Assignments – Assignments to SVB will be prohibited.

4) Is there a "stay" under applicable law related to enforcement of Defaulting Lender provisions?

Any person intending to enforce the Defaulting Lender provisions against a bank in FDIC receivership needs to analyze 12 USC 1821(e)(13)(c), which is set forth below (emphasis added). We are not aware of any cases interpreting this provision in the Defaulting Lender context and it is not certain that enforcement of the Defaulting Lender provisions is caught up by this statute, but the wording of the statute is broad.

12 USC 1821(e)(13)(c)

(C) Consent requirement
(i)In general

Except as otherwise provided by this section or section 1825 of this title, **no person may exercise any right or power to terminate, accelerate, or declare a default under any contract to which the depository institution is a party, or to obtain possession of or exercise control over any property of the institution or affect any contractual rights of the institution, without the consent of the conservator or receiver, as appropriate, during the 45-day period beginning on the date of the appointment of the conservator, or during the 90-day period beginning on the date of the appointment of the receiver, as applicable.**

(ii)Certain exceptions
No provision of this subparagraph shall apply to a director or officer liability insurance contract or a depository institution bond, to the rights of parties to certain qualified financial contracts pursuant to paragraph (8), or to the rights of parties to netting contracts pursuant to subtitle A of title IV of the Federal Deposit Insurance Corporation Improvement Act of 1991 (12 U.S.C. 4401 et seq.), or shall be construed as permitting the conservator or receiver to fail to comply with otherwise enforceable provisions of such contract.

5) Will SVB fund under its commitments contained in the credit agreement?

The FDIC will make a determination whether to disaffirm or repudiate SVB's contracts in the coming weeks. In the meantime, parties should assume that SVB will not fund, as the FDIC froze all SVB commitments on March 10, 2023.

6) Do funding notices or other information need to be sent to SVB?

Yes. Credit agreements generally do not exclude Defaulting Lenders from receiving notices (including borrowing notices) or other information delivered under the documentation. Agents should continue to send notices and other information to SVB in accordance with the terms of the loan documents.

7) Are lenders obligated to fund SVB's pro rata share of requested borrowings?

Generally, no. Lenders are obligated to fund up to their pro rata share of requested borrowings up to each lender's commitment level.

8) Should the Agent send interest, fee and/or principal payments to SVB?

Payments received by the Agent on account of SVB (including principal, interest, fees and other amounts) would typically be applied pursuant to a Defaulting Lender waterfall. Under a Defaulting Lender waterfall, the Agent may be able to withhold amounts that would have been payable to any Defaulting Lender in escrow to apply towards future obligations. For example, a Defaulting Lender waterfall may require amounts that would have otherwise been payable to SVB be used to:

- **a)** Pay any amounts owing from SVB to the agent, issuing bank(s) and/or swing line lenders,
- **b)** Fund or cash collateralize any letter of credit and swingline fronting exposure,
- **c)** Fund SVB's pro rata share of advances to the borrower, and
- **d)** Be held in a deposit account to fund future funding obligations and/or cash collateralize any issuing banks future fronting exposure with respect to letters of credit.

If the credit agreement does not contain specific treatment regarding payments to be made to Defaulting Lenders, see the FDIC FAQs, which suggest that payments should continue to be made in a manner consistent with the process in place pre-receivership.

9) What if there are letters of credit or swinglines in the deal? What are the Agent's and the other lenders' obligations?

Any outstanding letter of credit obligations and swingline obligations on the part of SVB may be reallocated to other non-Defaulting Lenders, but only to the extent that such reallocated obligations do not exceed each non-Defaulting Lender's commitment level. In addition, in certain instances, swingline loans and issuance of letters of credit may be suspended by the swingline lender(s) and/or issuing bank(s) as applicable, until they no longer have any fronting exposure.

10) SVB has issued letters of credit in the deal? Can they be drawn on?

As an entity in FDIC receivership, it is unlikely that SVB as issuing bank will honor a letter of credit draw request at this time.

11) What voting rights does SVB have in the deal?

Defaulting Lenders are typically disenfranchised, except with respect to certain "sacred rights" (e.g., increases or extensions of the tenor of SVB's commitment). In some agreements Defaulting Lenders may retain the right to vote on all matters that require unanimous lender consent or the consent of all affected lenders.

"Required Lender" votes should exclude the loans and commitments of Defaulting Lenders from the calculation of whether the "Required Lenders" have consented to an amendment.

12) Can SVB be removed as lender from the deal? How can this be accomplished?

The borrower (and occasionally the Agent) may have the right, using the "yank-a-bank" provision, to replace SVB with a lender that agrees to assume its obligations under the credit agreement. This typically involves another lender purchasing SVB's loans and commitments at par (plus accrued interest).

Occasionally credit facilities permit parties (usually the borrower), upon prior notice to Agent and subject to other conditions (such as the absence of any "Event of Default"), to terminate any unused commitments of a Defaulting Lender and/or to repay any outstanding loans of a Defaulting Lender.

13) Are funds that were held in SVB accounts "unrestricted cash" or "restricted cash" for the purposes of determining cash netting, liquidity tests and similar items?

The answer depends largely on the language in the document. For many formulations of cash netting provisions, liquidity tests and similar items that limit amounts to "unrestricted cash and Cash Equivalents", the only potential "unrestricted cash and Cash Equivalents" would be up to $250,000 of cash credited to each former SVB account (or such other amount as may be insured depending on the number of depositors, etc.), and the excess should no longer be considered "cash or Cash Equivalents" (and will ultimately be represented by a receivership certificate, which is unlikely to be picked up by most customary definitions of "Cash Equivalents"); however, once depositors have access to all funds in their SVB accounts following the Joint Statement, such amounts may once again constitute "unrestricted cash and Cash Equivalents". On the other hand, if, e.g., the test is based on a reported cash balance sheet number and not listed / required to be listed as restricted on the most recently delivered balance sheet, those amounts may still be subject to netting

14) Is there anything else Agents should be doing right now?

Agents should determine whether the borrower has bank accounts or other products with SVB and should work closely with the borrower to confirm that the borrower is proactively taking steps to maximize return and preserve assets. For example, borrowers should (i) be directing customers to make payments to non-SVB accounts, (ii) promptly open non-SVB bank accounts and (iii) follow up with the FDIC regarding their deposits at SVB. Borrowers who are SVB customers should call the FDIC toll-free at 1-866-799-0959 to register, and to ensure that contact information is accurate throughout the course of the receivership (which we understand will be managed through an online portal). In addition, borrowers who are SVB customers should ensure that all contact information is up to date with the SVB portal. Agents should follow through to take perfection steps over any new bank accounts.

Considerations if you are a Lender in a Deal and SVB is the Agent:

1) Will SVB continue to administer the borrowings, payments, interest and fee calculations and otherwise perform its duties as Agent under the credit agreement?

For so long as SVB remains the Agent, there will be operational challenges with respect to receipt of payments (and distribution thereof to the lenders), calculation of interest, making of advances and any other actions subject to agent-related determinations or notices required under the loan documentation. Unfortunately at this time, it is too early to determine what the FDIC will do under credit facilities agented by SVB. It is theoretically possible the FDIC will step in and administer the credit facilities. However, the FDIC will have the right to disaffirm or repudiate SVB contracts, including SVB's obligations under credit agreements (and therefore its duties as Agent). One thing is certain – this will take some time for the FDIC, other lenders and the borrowers to sort through.

2) Can SVB be removed as Agent?

An initial step will be to determine if and how SVB can be replaced as the Agent under the loan documentation. Some credit agreements may permit replacement of the Agent under specified circumstances or subject to a designated procedures, but others only permit replacement of the Agent (typically by the "Required Lenders" and, subject to certain exceptions, with the consent of the borrower) upon its elective resignation.

Occasionally replacement of the Agent is permitted upon the Agent becoming a "Defaulting Lender". Under such provisions, SVB could then be replaced upon notice thereof by the "Required Lenders" to the borrower (or sometimes with the consent of the borrower). Thereafter, depending on the terms of the credit agreement, the "Required Lenders" and/or borrower would then select and appoint a successor agent.

For credit facilities that do not permit replacement of the Agent under these circumstances, the lenders should determine whether the credit agreement can be amended to effect the removal of the Agent, the appointment of an additional agent (who would be selected from the lenders) or the designation of a sub-agent. Another alternative is that the lenders could consider forming an ad hoc group to request that SVB resign as agent under the loan documentation. For each of these options, the voting provisions of the credit agreement and the agency section of the credit agreement will need to be analyzed carefully to see what is permitted under the credit agreement. It is important that the lenders and borrower do not violate SVB's (or other parties') rights as set forth in the credit facilities.

Until SVB is replaced as agent, after lenders evaluate their options under the loan documentation, the lenders and borrower should discuss interim measures with respect to handling of advance requests, loans, payments and other matters that are typically handled by the administrative agent.

Other Considerations:

1) What happens to SVB's commitments under any commitment papers for deals that have not closed?

At this time, it is too early to know how the receivership may impact SVB's commitments under any commitment papers. However, the FDIC will have right to disaffirm or repudiate SVB contracts, including commitment papers. Additionally, commitment papers do not customarily contain "Defaulting Lender" provisions or other ability to remove a committing party and any amendments to commitment papers generally require ***all*** parties to approve and sign any amendments. At this time, lead arrangers and borrowers who are parties to commitment papers signed by SVB should take steps to evaluate other funding resources to prepare for a potential repudiation by the FDIC.

2) What if the borrower's accounts and cash management are held by SVB?

Depending on the nature and amount of the borrower's accounts and cash management at SVB, the borrower likely will not be able to immediately and readily access all or a portion of its funds. The borrower may be delayed in making payments not only under the credit facility, but also for payroll, other operational matters and with respect to other contractual obligations. To the extent the loan documentation includes liquidity conditions, whether to draws under the credit agreement, incurrence conditions for transactions and/or as a financial covenant, the borrower may not be able to satisfy such conditions if the borrower is relying on funds held in accounts at SVB to satisfy such liquidity requirement or test. If the borrower's accounts at SVB are subject to a control agreement in favor of the Agent, the Agent may not be able to access funds in those accounts and/or enforce any rights or remedies under such control agreement. If the borrower opens new accounts at another depository bank, new control agreements would need to be put in place with respect to those accounts.

It is very early in this receivership, and this receivership was put into place extremely quickly. As such, it is too soon to determine the full impact of the SVB receivership on credit facilities and commitment papers involving SVB as an arranger, an agent, and/or lender, and other bank products that SVB provides. In addition, the foregoing responses are subject to the review of the underlying contract to which SVB is a party (which may result in a different outcome than stated above), and subject to applicable law that may override contractual provisions. The Paul Hastings' team is available to review related loan documentation to determine various options and potential next steps.

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