Statement. Should a borrower transfer collateral funds out of a Bitcoin wallet, it is likely impossible for a creditor to recover since transactions cannot be reversed. Once again, without a control agreement, the option of sweeping the Bitcoin wallet is not available.

It remains to be seen if Bitcoin becomes widely adopted. However, as it and other payment systems evolve, creditors may find they hold valuable collateral for traditional lending transactions.

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## GOVERNMENTALLY MANDATED STANDBY LETTERS OF CREDIT: UPDATE

By Janis Penton and Jacob A. Manning

Federal, state, and local governments frequently allow standby letters of credit to be used to support a variety of obligations. Typically, those agencies become beneficiaries of the letters of credit and require that the letters of credit be issued in a mandated form that the agency drafts and includes in applicable statutes, regulations or ordinances.

The drafters of those forms are often unfamiliar with letter of credit law and practice and may simply copy a form used by another agency or draft a form without consulting someone familiar with this area of law. The results are letters of credit that are unclear, incomplete, unnecessarily burdensome and, worse still, insufficient to protect the beneficiary of the letter of credit—the very agency that dictates the terms of the form.

A project led by the Institute of International Banking Law & Practice, a non-profit educational organization, seeks to offer some guidance to these agencies. It has formed a Task Force of attorneys, bankers, and governmental representatives, which has met to discuss the issues common to these forms and to consider a draft of a model form that could be used by the governmental agencies in lieu of their existing forms. This article will summarize some of the issues that commonly arise with these governmentally mandated forms and summarize the work that has been and will be undertaken by the Task Force. The Task Force also is seeking help from members of the ABA's UCC Committee in identifying instances of governmentally mandated forms and bringing them to the Task Force's attention.

**Nature of the Problem**

A comprehensive analysis of all of the issues that arise in governmentally mandated standby letters of credit is beyond the scope of this article. Indeed, conservative estimates are that there may be thousands of such forms in existence. No single article could attempt to explain every issue with every form. Instead, what this article attempts to do is explain some of the reasons that governmentally mandated forms are problematic and give examples of those.

First, it is apparent that many governmental entities are simply inexperienced with letter of credit rules and practice and—perhaps deliberately or perhaps not—choose rules of practice that are not ideal for standby letters of credit. Most commercial letters of credit are issued subject to the Uniform Customs and Practice for Documentary Credits's ("UCP") most recent revision, UCP600.[40] The UCP was drafted to apply to commercial letters of credit and was oriented towards paying for the sale of goods. As a result, the UCP addresses the examination of documents presented in international trade such as bills of lading, drafts, other types of shipping documents, commercial invoices, and packing lists—documents which are not often found in a standby letter of credit transaction.

Although the UCP can be applicable to standby letters of credit,[41] it does not state how its articles should be applied—or modified to apply—to standby letters of credit. For that reason, among others, under the auspices of the Institute of International Banking Law & Practice, Inc., the International Standby Practices were developed in 1998 ("ISP98"). ISP98 became effective in 1999 and has been endorsed by the International Chamber of Commerce and designated Publication No. 590.

ISP98 was developed for use with standby letters of credit. Thus, it articulates standard international standby letter of credit practice, and it avoids some of the problems created by interpreting a standby letter of credit subject to UCP600. By way of example, ISP98 addresses force majeure,[42] the dates of documents,[43] and installment or partial drawings[44] in a way that is more attuned to standby letter of credit practice than does UCP600. It also anticipates some issues common to standby letter of credit practice.[45]

Unfortunately, many governmentally mandated standby letters of credit[46] are still issued subject to UCP600[47] instead of ISP98 or offer parties a choice between the two. Some do not even invoke any practice rules or instead include only a choice of law clause or a reference to Revised Article 5 of the UCC.[48] The choice between these rules of practice is significant. As such, if governmental agencies are choosing to apply UCP600 because they are unaware of ISP98, education as to the differences would be beneficial both to those agencies and the parties that seek to do business with them.

Second, some governmentally mandated standby forms evidence a misunderstanding of the nature of a letter of credit and particularly, the issuer's obligations. A letter of credit is a "definite undertaking . . . by an issuer to a beneficiary at the request or for the account of an applicant, or in the case of a financial institution, to itself or for its own account, to honor a documentary presentation by payment or deliver of an item of value."[49] "A letter of credit is revocable only if it so provides."[50] It should not be necessary to state that a letter of credit is "irrevocable" but many governmentally mandated standbys do.[51] The same can be said of the need to state that a letter of credit is "independent."[52]

Many standby forms go further than using unnecessary words such as "irrevocable" or "independent." ISP98 provides a list of redundant or otherwise undesirable terms, including several that are to be disregarded if they appear in the text of a standby.[53] For example, it is quite common for standby letters of credit to state that they are "unconditional," "absolute," and "primary," despite that these words are unnecessary.[54] And it is common for standby letters of credit to use the words "assignable," "evergreen," or "revolving" despite that these terms have no single accepted meaning and are to be disregarded under ISP98.[55]

Whether these terms are being used in standby letter of credit forms to convey something about the nature of the issuer's obligation under the letter of credit or simply out of habit or because they have been copied from another form, there are clearer alternatives that could be used in each case to describe the obligation.

Third, and finally, some agencies clearly have not thought through the drafts of their form standby letters of credit to the degree that a practitioner would. These forms are problematic not only from the standpoint of the issuer being asked to issue the letter of credit, but also from the standpoint of the governmental agency as beneficiary, which may be disadvantaged by its own drafting decisions.

Examples of such poor drafting abound. If a letter of credit states that its expiration date "shall be automatically extended for a period of <u>at least</u> one (1) year on __________ (date), and on each successive expiration date," exactly when does the letter of credit expire?[56] If a standby letter of credit indicates without more that it is issued "pursuant to" certain regulations, or that one party's actions or obligations arise "pursuant to" those regulations, what effect do those regulations have on the parties' rights and obligations?[57] And if a letter of credit is "freely negotiable at any bank" exactly what has an issuer agreed to with respect to that letter of credit?

Again, these are intended only as examples of the issues that have arisen with standby letter of credit forms mandated by governmental entities. Clearly, they are no different than the issues that would arise if any other party unfamiliar with letter of credit law and practice began drafting letter of credit forms. But given the frequency with which these issues arise in forms mandated by governmental agencies, and the importance of the obligations that they support, those issues are worthy of note and of correction where possible.

**Organization of the Task Force on Model ISP98 Governmentally Mandated Standbys**

In light of these issues and others, in early 2014, the Institute of International Banking Law & Practice ("llBLP")[58] formed the Task Force on Model ISP98 Governmentally Mandated Standbys to help draft a model form that these governmental agencies could adopt. The principal drafters of the Model Form are Prof. James E. Byrne, the Director of the llBLP, and James Barnes, of Baker & McKenzie. The Task Force is co-chaired by Fiore F. Petrassi, of JP Morgan Chase Bank, and Jacob A. Manning, of Dinsmore & Shohl, LLP.

To accomplish its goal of developing a Model Form to be used with ISP98 in situations where a government agency has mandated a form of standby letter of credit, the Task Force has brought together governmental entities such as agencies, departments, and government-owned corporations, private stakeholders such as bankers, lawyers, government contracting firms, and trade associations. The Task Force's work has been organized into three main phases.

First, the Task Force has been meeting by telephone through Spring 2014 to discuss the issues raised by governmentally mandated standbys and, particularly, to consider specific examples of such forms. The Task Force gathered sample forms from around the United States and identified issues common to those forms, and the Task Force has begun discussing how the Model Form may address those issues. The Task Force is taking into account governmental agencies' needs in requiring a standby letter of credit and proposing solutions to the issues created by the forms that still provide the agencies with the security that a standby letter of credit can provide.

In the second phase of the Task Force's work—which the Task Force is just undertaking—the Task Force will call together the various government and private stakeholders to a public meeting at which issues with current forms and the draft of the Model Form can be discussed. The public meeting is intended to provide a forum for all stakeholders to consider the draft Model Form and comment on whether that Model Form could be adopted by governmental agencies in place of existing forms. That meeting took place on June 5-6, 2014, in Washington, D.C.

Finally, in the third phase of the Task Force's work, the Task Force will consider comments made during the public meeting and thereafter, and finalize work on the draft Model Form. The Task Force's goal is to create a Model Form that governmental agencies will find suitable to meet their needs and that private stakeholders are willing to issue. Of course, part of the Task Force's work in that regard will consist of disseminating the Model Form to governmental agencies and advocating its adoption. To this end, the Task Force would appreciate the help of members of the ABA's UCC Committee in identifying governmental entities that either have mandated or plan to mandate a standby letter of credit form and, if possible, provide a copy of the form. The Letter of Credit Subcommittee, through its co-chairs, will act as a clearing house to receive any information and pass it along to the Task Force. The co-chairs are Peter Carson (PCarson@sheppardmullin.com) and Larry Safran (Larry.Safran@lw.com). Forms also may be sent to Janis Penton (janis.penton@unionbank.com), who is acting as a liaison from the Subcommittee to the Task Force.

Ultimately, the success of the project will be determined by the governmental entities that adopt the Model Form. As such, individuals interested in receiving more information or contributing to the success of the project are invited to contact Jacob Manning via email at jacob.manning@dinsmore.com or the Project Director, Nicholas Lawson, via email at nlawson@iiblp.org for more information or to provide assistance in reviewing or disseminating the Model Form.

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## CONSIDERATIONS IN NEGOTIATING AGREEMENTS AMONG LENDERS

By Daniella Garcia

An Agreement Among Lenders or "AAL" governs the rights and obligations of the agent(s) and lenders who provide a unitranche credit facility to a borrower. A unitranche facility combines what would normally be two separately documented credit facilities (whether senior and junior, first lien and second lien, or split-lien revolver and term loan) into a single credit facility. The unitranche facility is governed by one set of documents and is secured by a single lien granted to one of the agents. The AAL takes the place of a traditional intercreditor agreement and will be a confidential agreement not provided to the borrower. A unitranche facility is often preferred by borrowers looking to minimize transaction costs and shorten the time period needed to close. It may also be proposed by the lenders holding the "second-out" portion of the facility when competing to win and then syndicate a deal. In such a scenario the unitranche facility will be structured with blended pricing (i.e., a single interest rate on the entire facility and a single set of fees) allowing the borrower to better compare competing proposals. A unitranche facility will typically not be proposed by the lenders holding the "first-out" portion due to, among other things, the risk in a bankruptcy that the first-out portion of the facility is deemed under-secured. This risk arises due to the fact that there is only one lien securing both the first-out and second-out debt, so the determination of whether the facility is secured or under-secured is made based on the value of the collateral to the entirety of the debt. If the entire facility is deemed under-secured, then the first-out lenders will not receive interest and attorneys' fees accruing after commencement of the bankruptcy regardless of whether the value of the collateral was sufficient to cover all of the first-out obligations.[59] With competition among lenders becoming more and more fierce, a first-out lender will often accept this risk to avoid losing the deal to a competitor.

The form that an AAL will take is often determined by the second-out lenders, whose counsel will usually draft the agreement. Whether the AAL is more favorable to one set of lenders over the other on any given point often depends on how the deal was put together. If the deal was sourced by the first-out lenders, they may have the leverage to obtain certain benefits under the AAL. If the deal was sourced by the second-out lenders, then the AAL will be more second-out friendly. Further, most AALs are negotiated based on precedent between the two sets of lenders and the terms may be dictated, in part, by the relationship between these lenders. As such, what may be acceptable to one lender may not be acceptable to another similarly situated lender. Any lender looking to syndicate a unitranche facility should bear this in mind.

Given the confidential nature of AALs and the manner in which they are negotiated, no real "market" precedent exists for these types of agreements. That being said, most AALs will address the following issues:

*Delineation of the First-Out and Second-Out Obligations.* All revolving obligations, including bank products and hedges provided by first-out lenders, will be part of the first-out obligations. If there is a term loan A under the credit documents, it will usually be part of the first-out obligations with all other term loans being part of the second-out obligations. If the underlying credit facility does not have separate term loan tranches, then the term loan may be split into A and B pieces under the AAL.