PAGES 1-16
Market Update

PAGES 17-19
Regulatory Updates

PAGES 19-20
Litigation Developments

PAGES 20-21
Restructuring Updates

PAGES 22-23
Other Developments

PAGES 23-24
Updates on LIBOR Transition

Cravath Quarterly Review

FINANCE AND CAPITAL MARKETS

Market Update

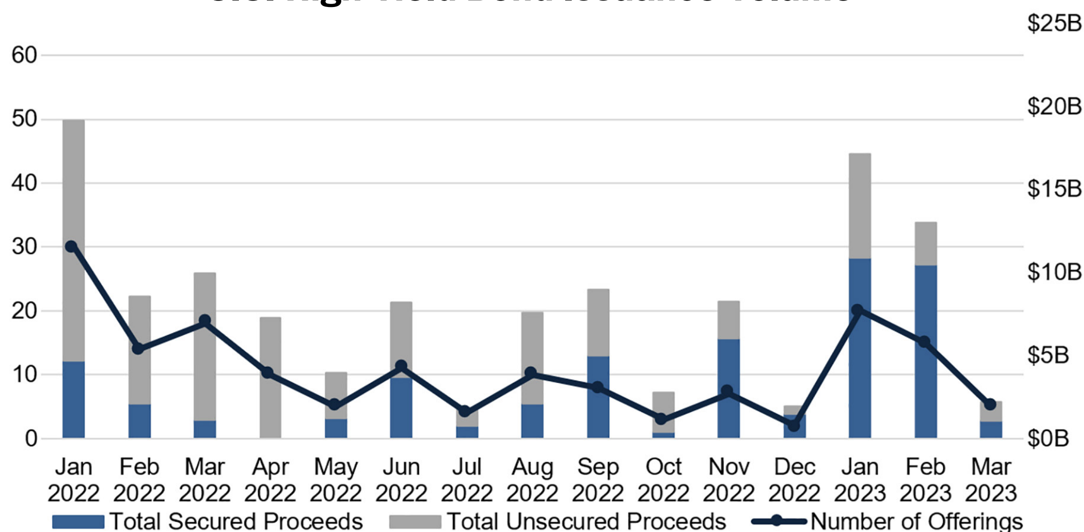
GENERAL TRENDS

Macroeconomic headwinds persisted in the first quarter of 2023, continuing the trend set in the second half of 2022 of increased financing costs and reduced overall financing activity as compared to the historic highs of 2020 and 2021. High-yield and investment-grade bond volumes for the quarter remained well below 2021 levels, although total proceeds from both rebounded considerably as compared to quarterly levels in the second half of 2022. Activity in the U.S. leveraged loan market (including the leveraged buyout market) picked up slightly in the first quarter of 2023 as compared to the fourth quarter of 2022, but remained well below the levels in the first quarter of 2022. While financing volumes were elevated in January and February as compared to the lows of the second half of 2022, deal activity slowed down in March following the failures of Silicon Valley Bank on March 10 and Signature Bank on March 12, as well as the government-brokered deal for UBS to take over Credit Suisse, announced on March 15.

BONDS

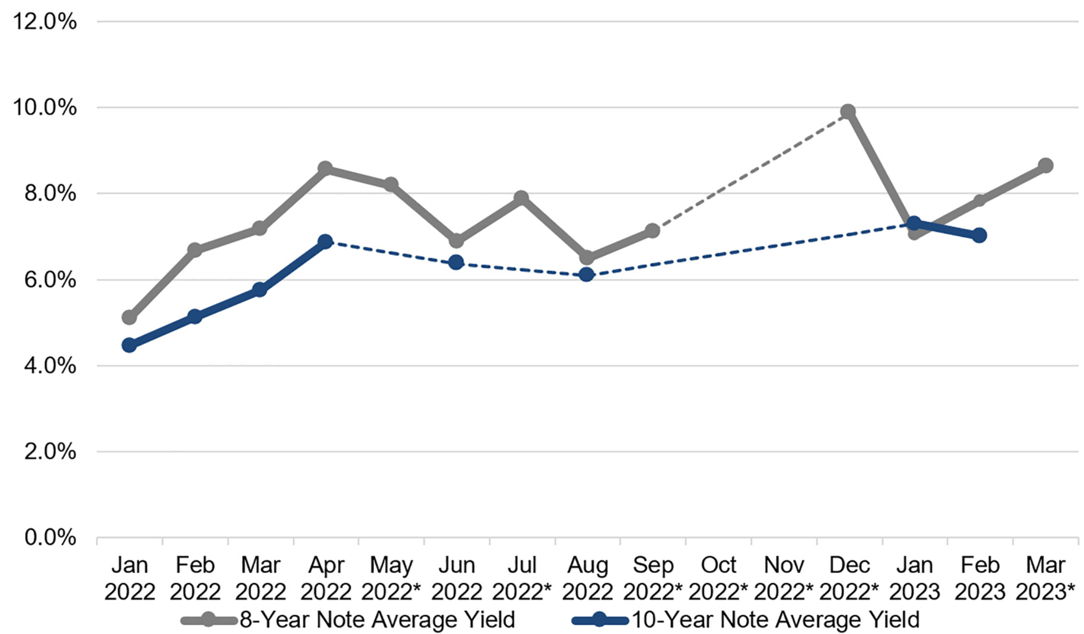
U.S. High-Yield Bonds

Total proceeds from U.S. high-yield bond issuances were $32.4B in the first quarter of 2023, up 148.5% as compared to the fourth quarter of 2022 ($13.0B) and down 14.2% as compared to the first quarter of 2022 ($37.7B). The volume of U.S. high-yield issuances increased in January ($17.2B in total proceeds), only to decrease in February ($13.0B in total proceeds) and March ($2.2B in total proceeds). Total proceeds from secured bonds were $22.4B in the first quarter of 2023, up 184.1% as compared to $7.9B in the fourth quarter of 2022.



DATA SOURCE Leveraged Commentary & Data (LCD)

The average yield on high-yield 8-year notes was 7.8% in the first quarter of 2023, down 20.7% from the average yield of 9.9% in December of 2022 and up 23.9% from the average yield of 6.3% in the first quarter of 2022. The average yield on high-yield 10-year notes was 7.2% in January and February of 2023, up 39.9% from the average yield of 5.1% in the first quarter of 2022.

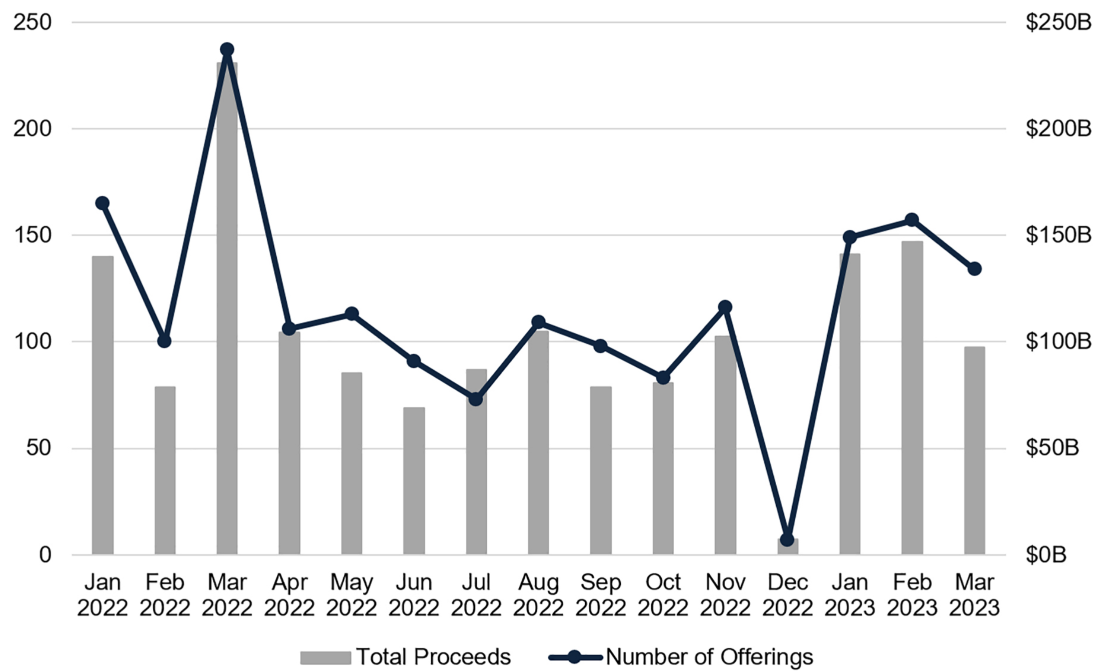


* No high-yield bonds with a 10-year maturity were issued in May, July, September, October, November or December 2022, or March 2023. No high-yield bonds with an 8-year maturity were issued in October or November 2022.

DATA SOURCE Leveraged Commentary & Data (LCD)

U.S. Investment-Grade Bonds

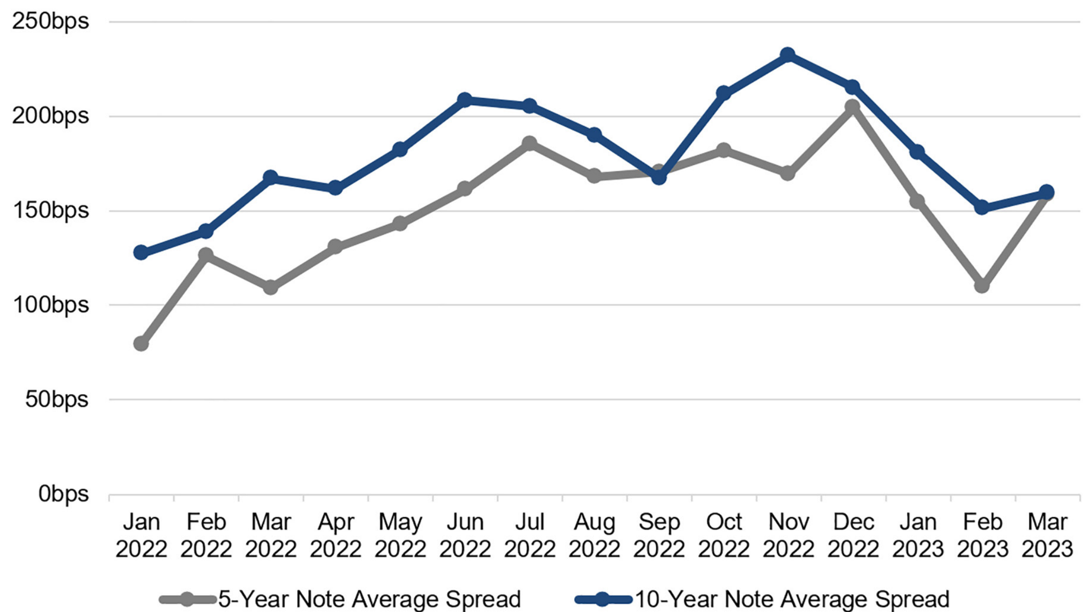
Total proceeds from U.S. investment-grade issuances were $385.3B in the first quarter of 2023, up 102.2% as compared to the fourth quarter of 2022 ($190.6B) and down 14.3% from the first quarter of 2022 ($449.4B). Notably, U.S. investment-grade issuances in February 2023 generated $146.9B in total proceeds, which set an all-time high for the month of February, up 37.7% as compared to the previous record for February ($106.7B, set in February 2021).



DATA SOURCE Leveraged Commentary & Data (LCD)

The average pricing spread (measured over the comparable Treasury) on U.S. issuances of 5-year investment-grade notes in the first quarter of 2023 decreased 23.8% as compared to the average pricing spread for the fourth quarter of 2022 and increased 34.6% as compared to the average pricing spread for the first quarter of 2022.

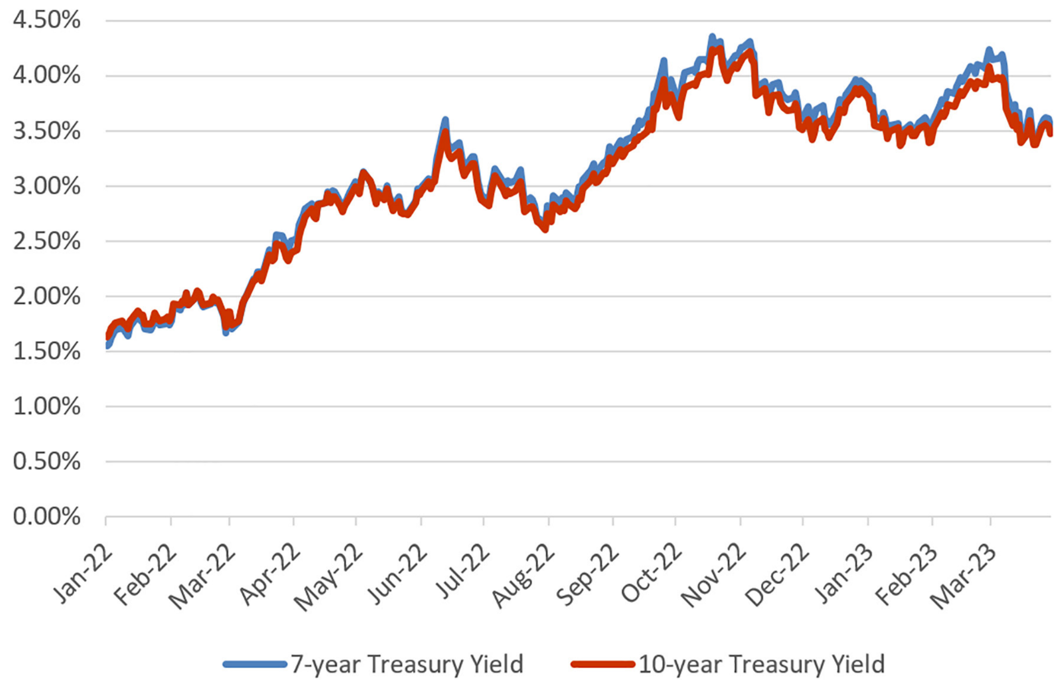
The average pricing spread (measured over the comparable Treasury) on U.S. issuances of 10-year investment-grade notes in the first quarter of 2023 decreased 25.4% as compared to the average pricing spread for the fourth quarter of 2022 and increased of 13.4% as compared to the average pricing spread for the first quarter of 2022.



DATA SOURCE Leveraged Commentary & Data (LCD)

U.S. Treasury 7-Year and 10-Year Yields

Since the Federal Reserve began aggressively increasing interest rates in March 2022, U.S. Treasury yields (which form the basis for bond pricing) have significantly increased. U.S. Treasury 7-year and 10-year rates in the first quarter of 2023 increased 115 bps and 116 bps, respectively, as compared to the end of the first quarter of 2022, representing an increase of 47.9% and 50.0%, respectively. However, the trend abated somewhat in the first quarter of 2023, with U.S. Treasury 7-year and 10-year rates ending the quarter down by 41 bps and 40 bps, respectively, as compared to the end of 2022, representing a decrease of 10.4% and 10.3%, respectively.

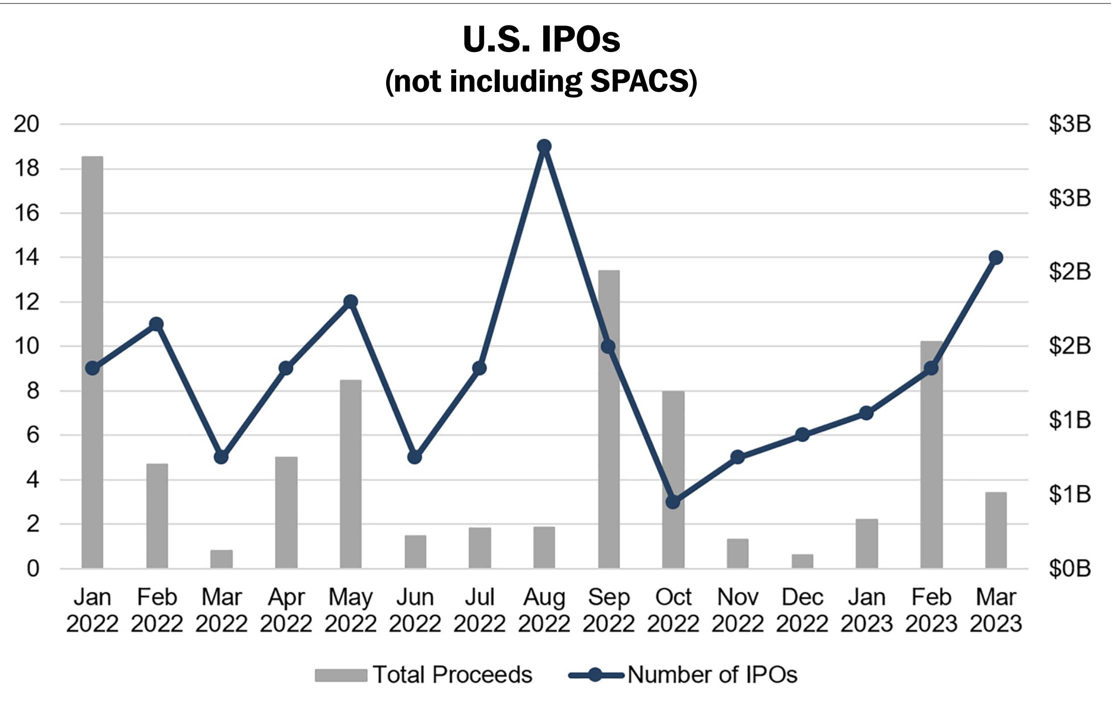


DATA SOURCE U.S. Department of the Treasury

EQUITY

U.S. IPOs

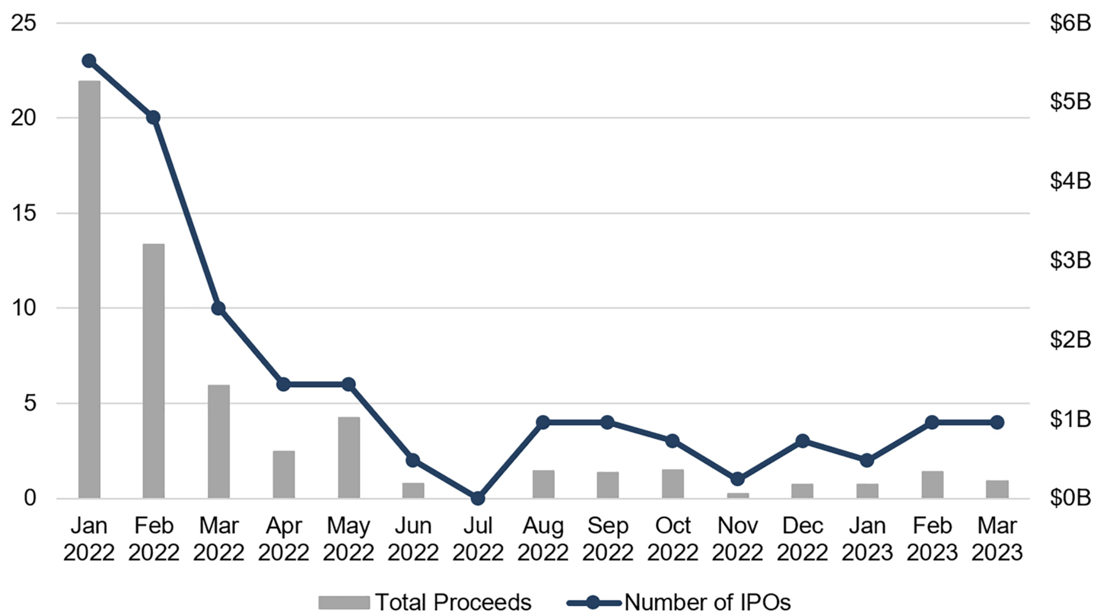
The U.S. IPO market in the first quarter of 2023 remained far less active compared to the record-setting levels seen in 2021, but at times showed signs of rebounding from the general decline throughout the second half of 2022. The $2.4B of total proceeds from U.S. IPOs (not including SPACs) for the first quarter of 2023 was up 60.9% as compared to the fourth quarter of 2022 ($1.5B) and down 34.1% as compared to the first quarter of 2022 ($3.6B). As of the end of the first quarter of 2023, there have still been no primary direct listings on either the NYSE or Nasdaq, notwithstanding the December 2022 SEC approval of amended rules relaxing price range limitations for primary direct listings on the NYSE and Nasdaq.



DATA SOURCE Refinitiv, an LSEG Business

U.S. SPACs

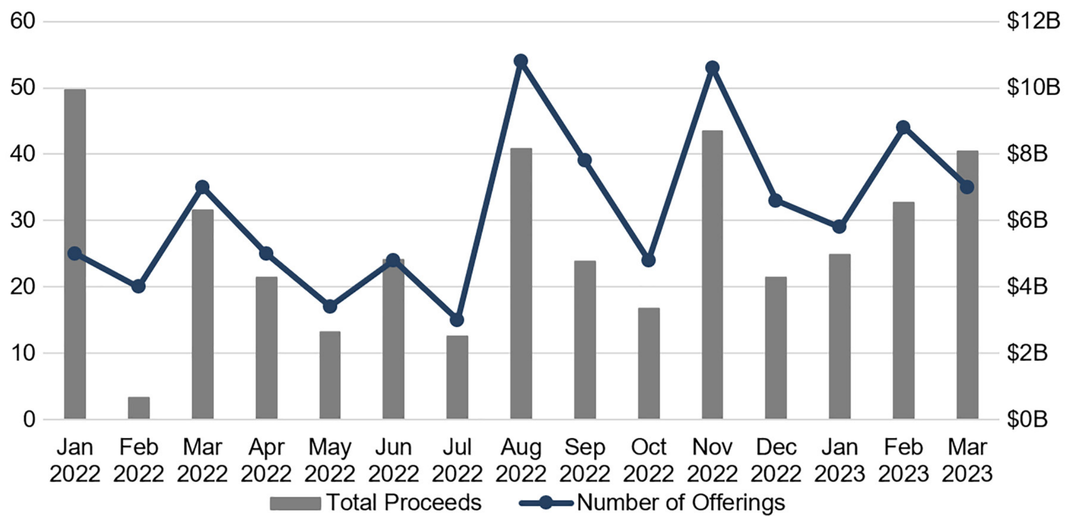
The U.S. SPAC market remained depressed during the first quarter of 2023 in comparison to record-high levels in 2021. The $737M of total proceeds from U.S. SPAC IPOs for the first quarter of 2023 was down 92.6% as compared to the first quarter of 2022 ($9.9B), driven by similar factors as those at work in 2022, including (i) the regulatory landscape, (ii) the generally poor performance of de-SPAC companies, (iii) high redemption rates in connection with de-SPAC business combinations (which make de-SPAC transactions harder to consummate) and (iv) an increase in the risk-free rate of return. Nevertheless, there has been a recent uptick in U.S. SPAC IPO activity, as the $737M in total proceeds in the first quarter of 2023 represented an increase of 24.2% as compared to the fourth quarter of 2022 ($594M).



DATA SOURCE Refinitiv, an LSEG Business

U.S. Follow-On Offerings

The $19.6B in proceeds from U.S. follow-on equity offerings for the first quarter of 2023 was up 19.8% as compared to the fourth quarter of 2022 ($16.4B) and 15.9% as compared to the first quarter of 2022 ($16.9B).

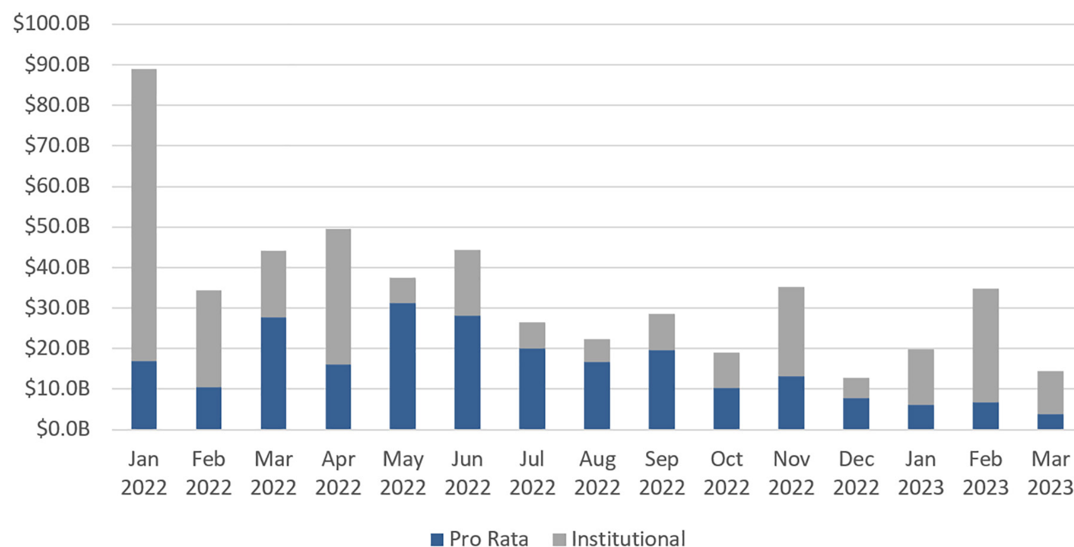


DATA SOURCE Refinitiv, an LSEG Business

LOANS

U.S. Leveraged Loan Issuances

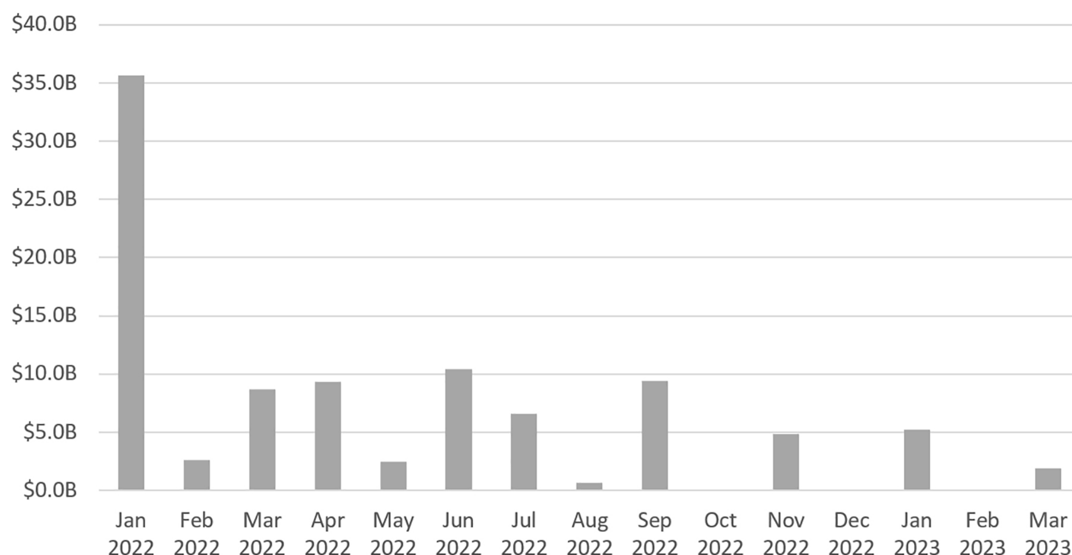
Activity in the U.S. leveraged loan market picked up slightly in the first quarter of 2023, with total volume up 3% as compared to the fourth quarter of 2022 (but down 59% as compared to the first quarter of 2022). Institutional term loan volume was $52.5B in the first quarter of 2023, up 47% compared to the fourth quarter of 2022 (but down 53% as compared to the first quarter of 2022). After an increase in 2022, the share of pro rata loan volume decreased to 24% of total loan volume in the first quarter of 2023, down from 47% in the fourth quarter of 2022 and from 33% in the first quarter of 2022.



DATA SOURCE Leveraged Commentary & Data (LCD)

U.S. LBO Loan Volume

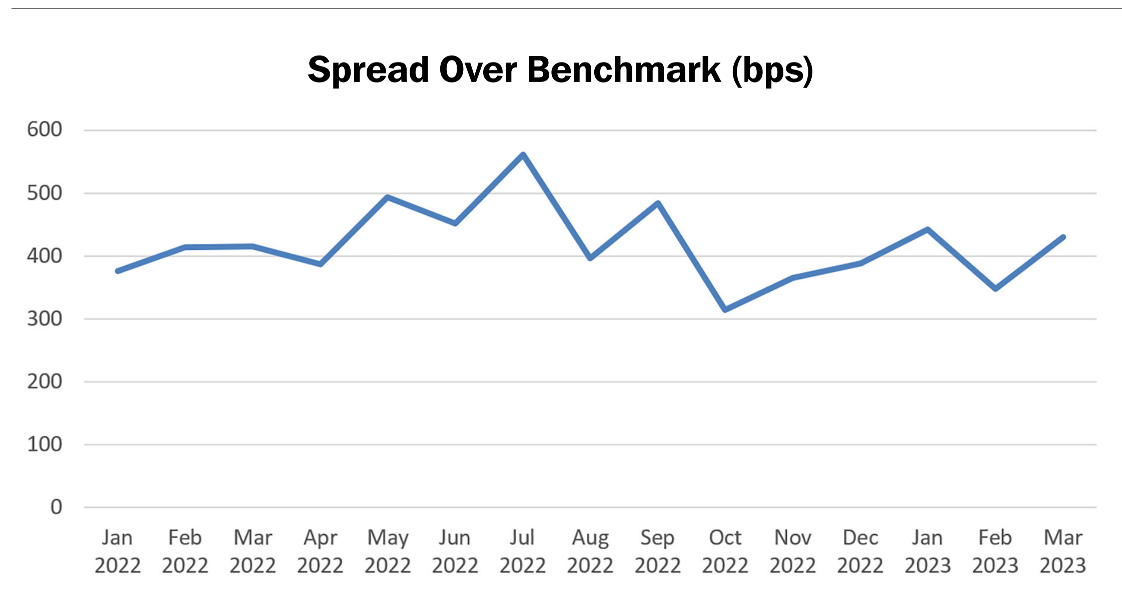
In the first quarter of 2023, there were $7.1B of U.S. LBO loans issued, an increase of 47% as compared to $4.9B in the fourth quarter of 2022 (but a decrease of 85% from $47.0B in the first quarter of 2022). As of April 20, 2023, LCD reported no U.S. LBO loans issued in February 2023.



DATA SOURCE Leveraged Commentary & Data (LCD)

Primary Market Institutional First-Lien Loan Spreads

Average spreads over benchmark rates on first lien institutional loans for large corporate leveraged loan transactions were 387 bps in the first quarter of 2023, 13 bps tighter than the 400 bps average spread in the trailing 12-month period.

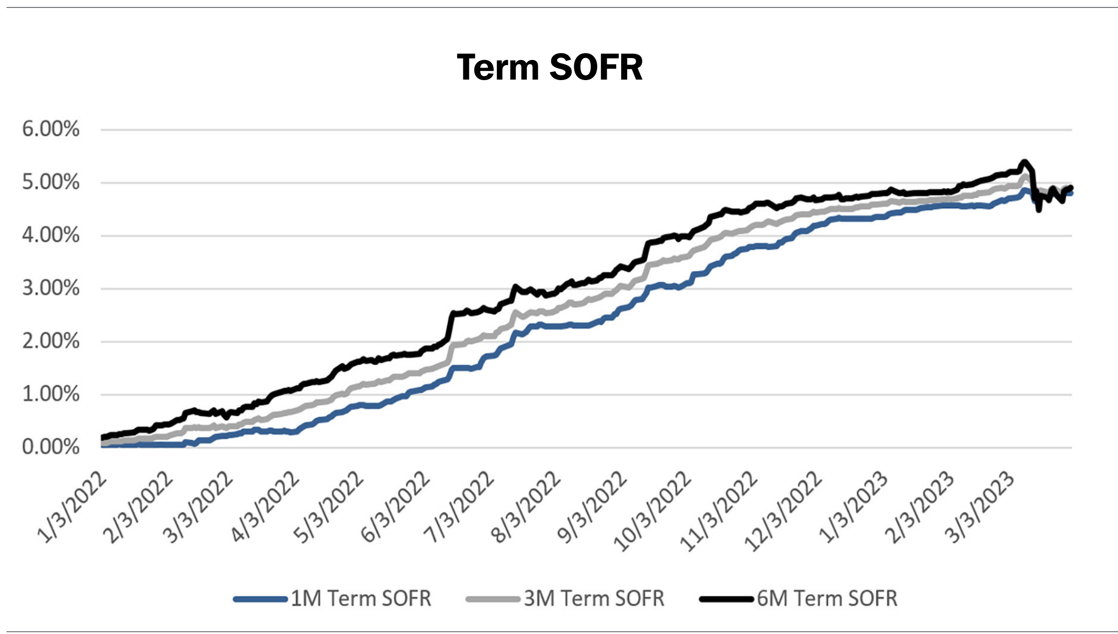


Note: Large corporate borrowers are defined as borrowers with an annual EBITDA of at least $50mm. Average spreads are dollar-weighted based on reported spreads, and do not reflect credit spread adjustments.

DATA SOURCE Leveraged Commentary & Data (LCD)

Term SOFR Reference Rate

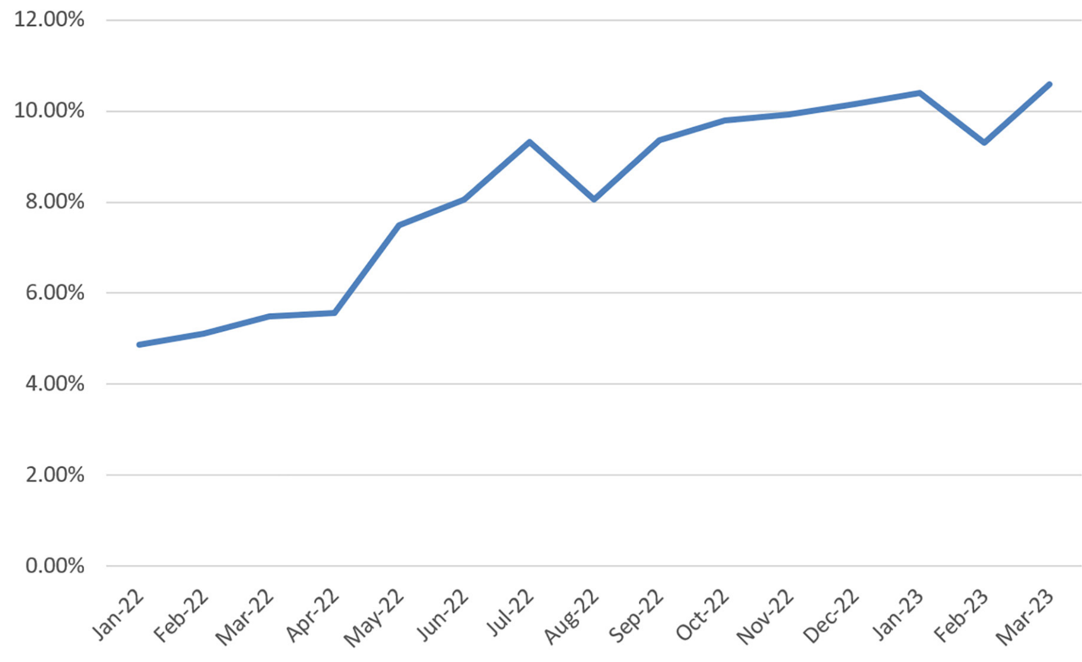
Term SOFR ended the first quarter of 2023 at 4.80%, 4.91% and 4.90% for the one-month, three-month and six-month tenors, respectively, for an increase of 44 bps, 32 bps and 12 bps, respectively, compared with the end of the fourth quarter of 2022. Notably, in March 2023, Term SOFR for the six-month tenor dropped below the Term SOFR for both the one-month and three-month tenors — on March 16, 2023, Term SOFR for the six-month tenor was 4.48%, compared to Term SOFR for the one-month and three-month tenors of 4.69% and 4.73%, respectively.



SOURCE Bloomberg Finance L.P.

Primary Market Institutional First-Lien Loan Yields

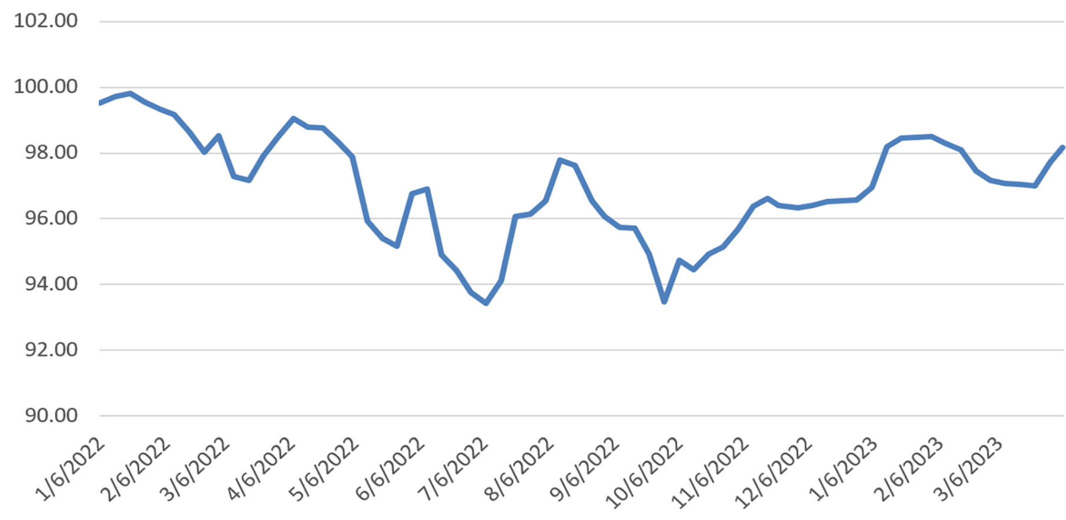
Yields on new-issue institutional first lien term loans held steady overall in the first quarter of 2023. The average yield rose to 10.4% in January 2023 for an increase of approximately 554 bps year-over-year and was 10.60% in March 2023 for an increase of approximately 511 bps year-over-year. While average yield dipped to 9.31% in February 2023, this still represented an increase of approximately 420 bps year-over-year.



DATA SOURCE Leveraged Commentary & Data (LCD)

Secondary Market Pricing

The average bid price of the LCD Flow Name Index increased by 202 bps in the first quarter of 2023 as compared to the fourth quarter of 2022, though it remained below the average bid price of $98.70 in the first quarter of 2022.



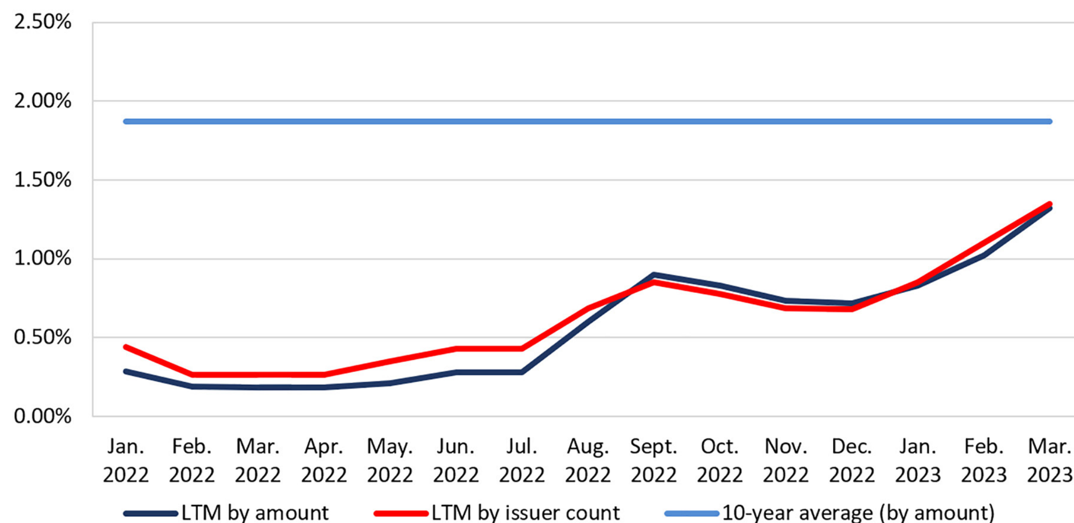
DATA SOURCE Leveraged Commentary & Data (LCD)[1]

1 The LCD Flow Name Index is a composite index of 15 institutional borrower names published on a twice-weekly basis by Leveraged Commentary & Data (LCD).

RESTRUCTURING

U.S. Leveraged Loan Default Rate

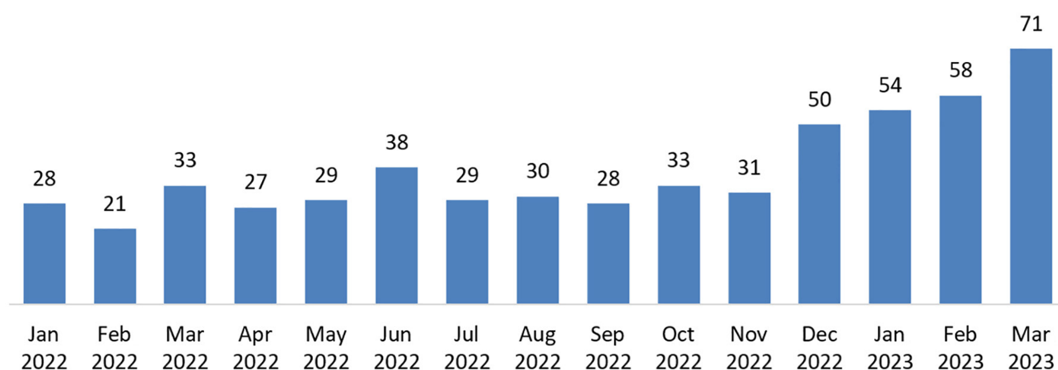
The default rate for U.S. leveraged loans increased significantly in the first quarter. The default rate was 1.32% by amount and 1.35% by issuer count for the LTM period ending March 31, 2023, compared to 0.72% by amount and 0.68% by issuer count for the LTM period ending December 31, 2022. As reflected on the following chart, the upward trend is rising towards the 10-year average default rate (by amount).



DATA SOURCE Leveraged Commentary & Data (LCD); Morningstar LSTA U.S. Leveraged Loan Index

U.S. Bankruptcy Filings

The number of U.S. bankruptcy filings increased throughout the first quarter with the most significant increase in March, leading to the highest level of U.S. bankruptcy filings for the first three months of a year since 2010. The consumer discretionary sector had the most filings in the quarter, while the financials sector accounted for much of the increase in March.



Note: Bankruptcy filing data limited to public companies or private companies with public debt where either assets or liabilities at the time of the bankruptcy filing are greater than or equal to $2 million, or private companies where either assets or liabilities at the time of the bankruptcy filing are greater than or equal to $10 million.

DATA SOURCE S&P Global Market Intelligence

Regulatory Updates

Continued Focus on Rule 10b5-1 Plans

As discussed in the Q4 2022 edition of this newsletter, amendments to Rule 10b5-1 under the Securities Exchange Act of 1934 (the "Exchange Act") became effective on February 27, 2023. These amendments, among other things, impose additional conditions on the ability to rely on the affirmative defense provided by that rule to violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. One such condition is a requirement that Rule 10b5-1 plans include a cooling-off period for officers and directors that expires at least 90 days after the plan's adoption or, if later, two business days following the disclosure of the issuer's financial results covering the fiscal quarter in which the plan was adopted in a Report on Form 10-Q or 10-K, or in a Report on Form 6-K or 20-F for foreign private issuers, up to a maximum of 120 days after adoption.

Prior to the effectiveness of these amendments, and as evidence of the continuing focus on Rule 10b5-1 plans, on February 24, 2023, the U.S. Department of Justice ("DOJ") brought the first criminal case for insider trading under a Rule 10b5-1 plan, alleging that the Chairman of the Board of Directors of Ontrak, Inc. ("Ontrak") fraudulently used Rule 10b5-1 plans to trade Ontrak stock when he established two Rule 10b5-1 plans after learning that Ontrak's contract with Cigna, Ontrak's biggest customer, was likely to be terminated. Notably, there were no "cooling-off" periods under the plans. The Chairman allegedly established his first Rule 10b5-1 plan in May 2021 upon learning that the relationship between Ontrak and Cigna was deteriorating and entered into his second Rule 10b5-1 plan in August 2021 when he learned that Cigna confirmed an intent to terminate the contract with Ontrak. Then, on August 19, 2021, just six days after the Chairman adopted his second Rule 10b5-1 plan, Ontrak publicly announced that it had lost Cigna as a customer, and the stock price of Ontrak dropped by 44%. By selling his shares before the public announcement pursuant to the two Rule 10b5-1 plans, the Chairman allegedly avoided $12.5 million in losses.

Moreover, as part of the investigation by the SEC and DOJ into the failure of Silicon Valley Bank ("SVB"), the SEC and DOJ are reviewing sales of SVB shares by SVB's executives that were allegedly made during the week before SVB's collapse. SVB's executives allegedly made such sales pursuant to Rule 10b5-1 plans, only 30 days after such plans were adopted. At issue is whether the executives were aware of material non-public information when they entered into the Rule 10b5-1 plans, which would undercut their ability to claim the 10b5-1 affirmative defense against insider trading liability.

The Rule 10b5-1 plans and sales of securities of Ontrak and SVB described above would be flatly prohibited under the amended Rule 10b5-1 due to their lack of compliance with the "cooling off" requirement.

SEC Proposes Changes to Regulation S-P, Proposes New Cybersecurity Risk Management Rule and Reopens Comment Period for Proposed Cybersecurity Risk Management Rules and Amendments for Registered Investment Advisers and Funds

On March 15, 2023, the SEC took a number of steps related to cybersecurity, one of its top current priorities. First, the SEC proposed amendments to Section 248.30 of Regulation S-P that would, among other things, require broker-dealers, investment companies, registered investment advisers and transfer agents to adopt and maintain written policies and procedures to address unauthorized access of customer information; to provide notice, with certain exceptions, no later than 30 days after becoming aware of unauthorized access to individuals whose customer information was or is reasonably likely to have been accessed without

authorization; and to require their service providers to take appropriate measures to protect customer information against unauthorized access.

Also on March 15, 2023, the SEC proposed Rule 10 under the Exchange Act, which would require broker-dealers, clearing agencies, national securities associations, national securities exchanges, transfer agents and other market participants to address their cybersecurity risks. Specifically, the proposal would require these entities to implement cybersecurity policies and procedures, review at least annually the effectiveness of such policies and notify the SEC of any significant cybersecurity incidents. The public comment period will remain open until 60 days after the date of publication of the proposing release in the Federal Register.

Finally, the SEC reopened the comment period on proposed rules and amendments related to cybersecurity risk management and cybersecurity-related disclosure for registered investment advisers, registered investment companies and business development companies that were originally proposed by the SEC on February 9, 2022. The initial comment period ended on April 11, 2022. The SEC reopened the comment period in light of other regulatory developments regarding cybersecurity risk management, to allow interested persons additional time to analyze whether there would be any effects of other SEC proposals and disclosure that the SEC should consider.

SEC Considers Requiring Increased Disclosures from Private Companies

In January 2022, the *Wall Street Journal* reported that the SEC had begun drafting regulations that would require private companies that are valued at $1 billion or more to routinely disclose financial and operational information. In the first quarter of 2023, the SEC included in its regulatory agenda potential heightened disclosure requirements for private companies relying on Regulation D in connection with securities offerings.

A proposal for amending Regulation D may be introduced as early as the second quarter of 2023, but it is currently unclear what the scope of that proposal will be or whether the SEC will put forth a proposal at all. The SEC's agenda item describing this issue is brief, stating that the SEC's Division of Corporation Finance is "considering recommending that the Commission propose amendments to Regulation D, including updates to the accredited investor definition, and Form D to improve protections for investors".

On January 30, 2023, SEC Commissioner Caroline Crenshaw offered ideas for amending Regulation D during a speech that she delivered at the 50th Annual Securities Regulation Institute in Washington, D.C. Crenshaw recommended that Form D be amended to require more substantive information from companies (*e.g.*, information regarding the issuer's total assets, investors, employees, revenues and financial condition, as well as additional details about the securities offering itself). Similar to the SEC's Regulation A exemption, larger offerings would require additional information, including audited financial statements. Lastly, Crenshaw recommended that companies be required to file a Form D before the offering, rather than the current rule which requires a filing within 15 days after the date of first sale.

Kraken Forced to Terminate its Cryptocurrency Staking-As-A-Service Program

The SEC filed charges on February 9, 2023 against cryptocurrency exchange Payward Ventures, Inc. and Payward Trading Ltd. (doing business as "Kraken"), alleging violations of Section 5 of the Securities Act for Kraken's failure to register its "staking-as-a-service" ("StaaS") program as a securities offering. Blockchains validate and record transaction data through a

consensus mechanism. StaaS is a program that allows users to stake and participate in the consensus mechanism and earn staking awards on a more user-friendly interface as compared to the popular Proof-of-Stake consensus mechanism. Kraken's StaaS model was different from most because it did not provide for a direct relation between the customer's reward payout and the rewards earned by Kraken because Kraken specified the amount of customers' cryptocurrency to be staked, took custody of its customers' crypto assets and offered customers a fixed reward at an estimated rate (and Kraken retained any earnings above such rate).

The SEC's complaint states that Kraken's StaaS model is a passive investment opportunity and involves an offering or sale of securities under Section 5 of the Securities Act, based on the 1946 U.S. Supreme Court decision *SEC v. W.J. Howey Co.* SEC chair Gary Gensler stated that the SEC's "action should make clear to the marketplace that staking-as-a-service providers must register and provide full, fair, and truthful disclosure and investor protection."

The SEC's action against Kraken, although specific to Kraken's staking services, has the potential to influence future actions the agency may take against other blockchain-service providers. The SEC's focus on the specific facts surrounding Kraken's program provides a data point for StaaS providers to consider when analyzing their own StaaS programs. Our memorandum describing this matter in more detail is available here.

Litigation Developments

In re McDonald's Corporation Stockholder Derivative Litigation, C.A. No. 2021-0324-JTL (Del. Ch. Jan. 26, 2023).

In January 2023, the Delaware Court of Chancery held for the first time that non-director corporate officers owe stockholders a fiduciary duty of oversight similar to the duties owed by directors under the *Caremark* doctrine.

In *McDonald's*, stockholders brought a derivative action against the former Global Chief People Officer of McDonald's Corporation ("*McDonald's*") for a breach of the fiduciary duty of oversight, alleging that he failed to report upward red flags regarding sexual harassment and misconduct at McDonald's. The defendant moved to dismiss the complaint, contending that Delaware law does not impose a duty of oversight upon officers. The Court denied the defendant's motion and adopted the plaintiffs' reasoning when it held that the plaintiffs pleaded facts sufficient to support an inference that the defendant acted in bad faith by consciously ignoring red flags regarding sexual harassment, supporting the plaintiffs' claim that he breached his duty of oversight.

The Court advanced four rationales in support of its holding: (1) officers are best situated to gather information and provide timely updates to the Board; (2) Delaware law and other authorities have previously equated the fiduciary duties of officers with those of directors; (3) officers have duties as agents of the Board; and (4) the oversight duties of officers facilitate the Board's exercise of its oversight duties.

The Court noted that the oversight duties of officers may be narrower and more context-specific than those of directors, with officers generally being charged with monitoring and reporting red flags in their areas of responsibility as opposed to the corporation as a whole. However, the Court made clear that officers

cannot consciously ignore red flags that are brought to their attention, even if outside their area of responsibility.

In a subsequent decision in March 2023, the Court dismissed all claims brought against the directors of McDonald's, including for alleged breaches of fiduciary duty. Applying the business judgment rule, the Court held that the directors did not breach their fiduciary duties when they took personnel actions in good faith in response to allegations of misconduct by company officers, even if those actions were, with the benefit of hindsight, overly lenient.

Kirschner v. JPMorgan Chase Bank, N.A.

On March 9, 2023, the United States Court of Appeals for the Second Circuit (the "2nd Circuit") held oral arguments in the *Kirschner v. JPMorgan Chase Bank* case to decide whether the syndicated term loans at issue are securities and are therefore subject to state and federal securities laws and regulations—a decision that could have dramatic ramifications on the $1.4 trillion syndicated loan market. The claim arises from the bankruptcy of Millennium Laboratories LLC, in which the plaintiff, as trustee of Millennium Claim Trust, sued the banks that arranged a $1.775 billion syndicated term loan for Millennium, which closed on April 16, 2014. The plaintiff claimed that the arranger banks violated "Blue Sky Laws", the state equivalent of the federal securities laws, by fraudulently selling debt obligations to approximately 70 institutional investors and, in the process, making misstatements and omissions to the investors.

The appeal seeks to overturn a decision issued by Judge Paul Gardephe of the U.S. District Court for the Southern District of New York on May 22, 2020, which applied the four-factor "family resemblance" test set forth in the Supreme Court's *Reves v. Ernst & Young* decision and held that the term loans sold to investors were not "securities", and thus not subject to state and federal securities laws. Judge Gardephe concluded that the limited number of highly sophisticated purchasers of the loans would not have reasonably classified them as "securities" and that it would have been reasonable for such sophisticated institutional buyers to believe that they were lending money, with all of the associated risks, without the disclosure and other protections associated with the issuance of securities.

If the 2nd Circuit finds that syndicated loans are "securities" for purposes of U.S. securities laws, the impacts on the $1.4 trillion syndicated loan market could be very consequential—from higher compliance costs to a wide range of practical issues.

On March 16, 2023, after hearing the oral arguments, the 2nd Circuit solicited the SEC's views on the issue. On March 28, 2023, the SEC confirmed that they intend to comment, and filed an unopposed motion requesting an extension until June 27, 2023 to file a response to the 2nd Circuit's request.

Restructuring Updates

Uptier Transaction Litigation Developments: In re Serta Simmons Bedding, LLC

On March 28, 2023, Southern District of Texas Bankruptcy Judge David R. Jones issued an oral ruling on motions for summary judgment regarding Serta's "uptier" transaction (the "Transaction"). As further described below, the court ruled that that the priming exchange transaction entered into among Serta and a majority group of secured lenders was "very clearly" an "open market purchase" and therefore not prohibited by provisions in Serta's credit facilities requiring payments by Serta (excluding open market purchases) to be distributed pro rata among lenders.

In early 2020, Serta's business was in decline and the company needed additional liquidity to fund

operations and reduce interest expense attributable to, among other things, its outstanding $1.95 billion first lien facilities and $450 million second-lien facility. In order to alleviate these issues, Serta entered into a series of complex transactions with a majority of its existing lender group in June 2020.

The Transaction consisted of two steps:

1. First, Serta and the majority lenders amended the existing credit agreement to permit the incurrence of new priming debt under a separate credit agreement (the "PTL Credit Agreement").

2. Second, with the existing credit agreement amended, Serta then incurred (i) $200 million of super-priority first-out term loans for new money and (ii) $850 million of super-priority second-out term loans in exchange for the participating majority lenders' existing first and second lien loans under the PTL Credit Agreement.

Like most syndicated credit agreements, the existing credit agreement contained a provision requiring that any payment from Serta to any lender be distributed pro rata among all lenders, which could not be amended without the unanimous consent of the lenders. However, this "sacred right" was subject to exceptions, including a provision allowing Serta to engage in "open market purchases" of loans. Serta used this exception to obtain $200 million of new money through new first-out term loans and effectuate the exchange of existing first-lien and second-lien debt for super-priority debt, which reduced Serta's overall debt load by $400 million. The minority lenders, who were not given the opportunity to participate in the Transaction, then found that what had been first-lien debt was now subordinated to over $1 billion of super-priority loans. The Transaction was challenged and litigation has since continued in state and federal courts.

Throughout these lawsuits, the minority lenders challenged the Transaction on the grounds that it was a privately negotiated, structured and cashless debt exchange, which did not qualify as an "open market purchase" under the existing credit agreement and was therefore required to comply with the pro rata sharing requirements set forth therein. One group of lenders achieved a favorable ruling in March 2022, when Judge Katherine Polk Failla of the United States District Court for the Southern District of New York denied a motion to dismiss filed by Serta on the basis that the definition of "open market purchase" was ambiguous in its application to the Transaction.

On January 23, 2023, Serta filed for bankruptcy in the Southern District of Texas and on the same day filed an adversary proceeding seeking a declaratory judgment that the Transaction was permitted under the credit agreement. The case was assigned to Judge Jones, who quickly set a briefing schedule for summary judgment motions as to whether the Transaction constituted an "open market purchase".

On March 28, 2023, Judge Jones heard oral argument and quickly held in an oral ruling that, notwithstanding Judge Failla's earlier decision, the Transaction was unambiguously an open market purchase.

The case is not fully resolved, as minority lenders have filed notices of appeal, and Judge Jones did not hold that the Transaction was compliant with all provisions of the credit facilities—just that it constituted an open market purchase. However, in the event that the matter is ultimately resolved in a manner that is favorable to Serta and the majority lenders, it is foreseeable that other distressed businesses that have engaged in liability management transactions that have become subject to litigation will seek to have the transactions approved in bankruptcy court, especially in cases where the debtor is likely to require a restructuring in any event.

Other Developments

The Failure of Silicon Valley Bank and Signature Bank

On March 10, 2023, Silicon Valley Bank ("SVB") was placed into receivership. Two days later, Signature Bank ("Signature") was placed into receivership and the Federal Deposit Insurance Corporation (the "FDIC") established a "bridge bank" for SVB and for Signature. These bridge banks, chartered national banks supervised by the FDIC, were temporarily created to allow the failed banks to continue to serve their customers in the ordinary course while the FDIC either finds buyers for or liquidates the failed banks or their assets and liabilities. Following the establishment of the bridge banks, the FDIC promptly transferred the former assets and liabilities of SVB and Signature to the newly formed bridge banks, so that all bank deposits, both insured and uninsured, would be fully protected (note that the FDIC is empowered to transfer assets and liabilities of a failed bank to a bridge bank without third-party approvals or consents).

These bank failures immediately raised the question of how SVB and Signature would be treated for purposes of syndicated credit agreements for which they were lenders, in particular as to the operation of the "Defaulting Lender" provisions in typical credit agreements. Defaulting lender provisions are customary in U.S. syndicated credit agreements as protection from lenders who fail to perform their funding obligations and establish procedures for treatment of such defaulting lenders' loans and commitments. The "Defaulting Lender" provisions in most credit agreements include a prong for lenders for which a receiver has been appointed, including the FDIC.

However, SVB and Signature were not subject to the typical Defaulting Lender provisions for two primary reasons. First, while SVB and Signature became "Defaulting Lenders" as defined in most credit agreements, the Federal Deposit Insurance Act contains anti-"ipso-facto" provisions that render ineffective and unenforceable contractual provisions in credit agreements that would affect the rights and obligations of the "Defaulting Lender". The mere appointment of FDIC as the receiver and the assignment and transfer of loans and commitments to the bridge banks thus could not trigger the repercussions provided for in typical Defaulting Lender provisions. Second, the bridge banks themselves were not operating under FDIC receivership, and, as a result, the FDIC takes the position that the bridge banks were not Defaulting Lenders absent independent grounds for determining them as such (*i.e.*, the bridge banks' own non-performance).

SEC Finalizes Rule Shortening the Securities Transaction Settlement Cycle

On February 15, 2023, the SEC adopted final rules to shorten the standard settlement cycle for most broker-dealer transactions in securities from two business days after the trade date (T+2) to one (T+1). The compliance date for the final rules is May 28, 2024. The amended rules retain many of the same exceptions as the existing rules, including transactions involving exempted securities, government securities, municipal securities, commercial paper, bankers' acceptances, commercial bills and security-based swaps.

SEC Staff Posts New CDIs Related to Clawback Disclosure and Pay Versus Performance

The SEC's Division of Corporation Finance issued new clawback-related Compliance and Disclosure Interpretations ("CDIs") on January 27, 2023 and Pay Versus Performance CDIs on February 10, 2023. Specifically, the Clawback Disclosure CDIs, 121H.01 – 121H.04, clarify the SEC's expectations regarding a set of new checkboxes that have been added to the cover pages of Form 10-K, Form 20-F and Form 40-F.

The Pay Versus Performance CDIs, 128D.01 – 128D.13 and 228D.01 – 228D.02, address various topics under new Item 402(v) of Regulation S-K, including, among other things, calculating compensation actually paid, footnote disclosure describing deductions, peer group presentation, the requirement of net income within the 402(v) table, company-selected measures and "bonus pools".

SEC Enhances Tender Offer Rules & Schedules CDIs

On March 31, 2023, the staff of the SEC's Division of Corporate Finance issued 34 CDIs interpreting the tender offer rules. Several CDIs replace interpretations published previously in the Tender Offer Rules and Schedules Manual of Publicly Available Telephone Interpretations. These CDIs address a wide range of interpretive issues, consolidating existing guidance regarding tender offers into a single location. The CDIs are available here.

SEC Proposes to Modernize the Submission of Certain Forms, Filings and Materials

On March 22, 2023, the SEC proposed requiring electronic filing or submission of certain forms, filings or submissions that are required to be filed with or submitted to the SEC under the Exchange Act, including certain forms filed or submitted by self-regulatory organizations and certain reports and notices provided by broker-dealers, security-based swap dealers and major security-based swap participants. The rule would require electronic submission to the SEC's Electronic Data Gathering, Analysis, and Retrieval ("EDGAR") system. The public comment period will remain open for 30 days after publication in the Federal Register or until May 22, 2023, whichever is later.

SEC Issues Fee Rate Advisory for Fiscal Year 2023

On January 23, 2023, the SEC announced that, starting on February 27, 2023, the fee rate applicable to most securities transactions is to be set at $8.00 per million dollars of transaction value. On March 1, 2023, the SEC determined that it would not be issuing a mid-year adjustment to the fee rate for fiscal year 2023. The $8.00 per million dollars rate will therefore remain in place until September 30, 2023, or 60 days after the enactment of a regular FY 2024 appropriation, whichever is later.

SEC Provides Additional CDIs for Non-GAAP Financial Measures

As discussed in the Q4 2022 edition of this newsletter, in December 2022 the Division of Corporate Finance updated its non-GAAP financial measures CDIs, centralizing and formalizing certain principles that had been previously articulated by the SEC staff in a number of comment letters and speeches related to non-GAAP measures. During the first quarter of 2023, the presentation of non-GAAP financial measures and related disclosure controls and procedures continued to be a key focus area for the SEC, as underscored by the SEC's announcement in March 2023 that it had settled charges against an issuer for making misleading disclosures of non-GAAP measures over several reporting periods and failing to maintain adequate disclosure controls and procedures related to non-GAAP measures. Our memorandum providing additional information regarding the non-GAAP financial measures CDIs and the enforcement action, as well as recommendations in light of the SEC's focus on non-GAAP measures, is available here.

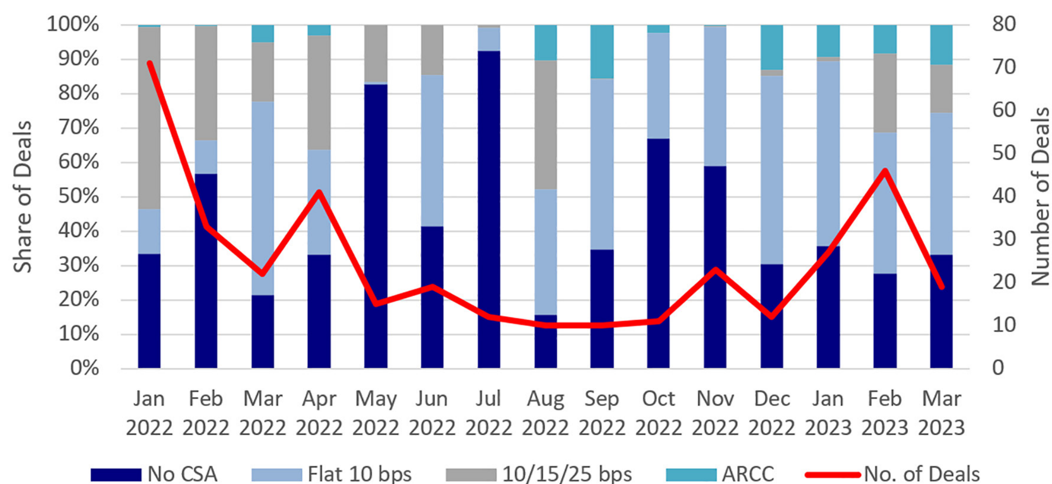
Updates on LIBOR Transition

FINAL LIBOR TRANSITION RULE:

In the fourth quarter of 2022, the Federal Reserve Board (the "Board") adopted its final rule implementing the Adjustable Interest Rate ("LIBOR") Act by identifying benchmark rates based on SOFR to replace overnight, one-month, three-month, six-month and 12-month LIBOR in contracts subject to the LIBOR Act. These contracts include U.S. contracts that do not mature before LIBOR ceases to be published on June 30, 2023 and that lack adequate fallback provisions that would replace LIBOR with a replacement benchmark rate. Consistent with this announcement, the final rule codified safe harbor protections for selection or use of SOFR as a replacement benchmark. The Board also confirmed that LIBOR contracts containing fallback provisions that identify a benchmark replacement are outside of the scope of the LIBOR Act. This rule became effective as of February 27, 2023.

CREDIT SPREAD ADJUSTMENTS:

Credit spread adjustments ("CSAs"), which are designed to account for the fact that SOFR, as a secured risk-free rate, is generally lower than LIBOR, continue to be a topic of discussion and negotiation between borrowers and arrangers in the first quarter of 2023. According to data from Leveraged Commentary & Data (through March 31, 2023), less than half of new institutional deals on a dollar-weighted basis in the first quarter of 2023 had no CSA (30.5%), a decrease as compared to the third quarter (47.2%) and the fourth quarter (57.9%) of 2022.



DATA SOURCE Leveraged Commentary & Data (LCD). Deal share calculated on a dollar-weighted basis.

SYNTHETIC LIBOR:

On November 23, 2022, the UK's Financial Conduct Authority ("FCA") opened a consultation on its proposal to require "synthetic" dollar-denominated LIBOR for one-, three- and six-month tenors to continue to be published after June 30, 2023. On April 3, 2023, the FCA formally announced that it will require the ICE Benchmark Association ("ICA") to publish an unrepresentative "synthetic" U.S. dollar LIBOR for a temporary period effective from July 1, 2023 through September 30, 2024, intended solely for use in legacy contracts, to help ensure an orderly wind-down of LIBOR. To calculate such "synthetic" dollar-denominated LIBOR, the ICA will be required to use the relevant CME Term SOFR Reference Rate plus the ARRC-recommended CSAs of 11.448/26.161/42.826 bps for one-, three- and six-month Term SOFR. Synthetic LIBOR would not affect more recent loan agreements with fallback language including a "non-representative" trigger (*i.e.*, a fallback trigger in the event that LIBOR is no longer "representative"), but would affect loan agreements with fallback language without a non-representative trigger or without any fallback language at all.

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