

COMMERCIAL REAL ESTATE INSIGHT & NEWS

The Bowditch & Dewey Real Estate Blog

Paul Bauer Quoted in "Bank collapses bring questions of all sizes" in Massachusetts Lawyers Weekly

MARCH 28, 2023

The failure of Silicon Valley Bank (SVB) has raised a number of issues, but a less publicized aspect of the collapse is the impact it has had on the letters of credit being held by commercial landlords with SVB as the issuing bank. Depending on the size of the lease and how much "build out" they have done for their tenants, landlords may demand multi-million-dollar security deposits, which startups like SVB's customers would often satisfy with letters of credit, putting the bank on the hook if the tenant defaults. *Massachusetts Lawyers Weekly* spoke with Paul Bauer about how the process typically works:

> Paul noted that under normal circumstances, it is a "nice, clean process" benefiting all. "The idea is that if the tenant files for bankruptcy, it's an independent obligation of a bank, so it doesn't get tied up in the bankruptcy. The landlord can still send the notice to the issuing bank, and the issuing bank is obligated to forward those funds. The landlord likes it because they don't have to carry the security deposit on their books. And the tenant likes it because when they get to the end of the term, they don't have to keep nagging the landlord to give them back their money."

Unfortunately, if a bank fails then the arrangement no longer works, and while the federal government quickly guaranteed depositors that they would not lose their money, commercial landlords have yet to receive any similar assurances.

> "What we're advising landlord clients is to take an inventory," Paul said. If the tenant is in good financial standing, the landlord having a letter of credit from SVB is "more of a technical problem." In other circumstances, a tenant may not be technically failing but is not the model of fiscal health, either. Paul noted that landlords now have added incentive to keep closer watch on their tenants' financial status, "given that the letter of credit may not be as valuable as they might have thought."

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