



## Finance ADVISORY ■

**AUGUST 28, 2014**

### SEC Adopts the First Part of Final Rules Relating to Regulation AB II

On August 27, 2014, at an open meeting, the U.S. Securities and Exchange Commission (SEC) unanimously adopted final rules substantially revising the offering process and reporting requirements for publicly issued, asset-backed securities and imposed new disclosure and reporting requirements for securities backed by residential mortgage loans, commercial mortgage loans, automobile loans or leases and corporate debt and resecuritizations of such assets.<sup>1</sup> The final rules are part of the initial rollout of comprehensive amendments to Regulation AB ("Regulation AB II"), which were first proposed four years ago. The SEC stated that other aspects of the initial rule proposal, including the extension of the asset-level disclosure requirements to privately issued structured finance products, will be forthcoming, although the exact timing was not specified. At the open meeting, the SEC also adopted, by a vote of 3-2, new rules and amendments to existing rules regulating Nationally Recognized Statistical Rating Organizations.

In April 2010, the SEC proposed Regulation AB II (the "2010 Proposing Release"),<sup>2</sup> and in July 2011, it issued a re-proposal (the "2011 Re-Proposing Release")<sup>3</sup> of certain aspects of the initial proposed rulemaking in light of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank").

#### Key Compliance Dates

1. **Rules Relating to the Issuance of Asset-Backed Securities:** Issuers will be required to comply with the new rules, forms and disclosure requirements (other than the asset-level disclosure requirements) no later than one year after the rules are published in the *Federal Register*.
2. **Asset-Level Disclosures:** Issuers of securitizations backed by residential mortgage loans, commercial mortgage loans, automobile loans or leases and corporate debt and resecuritizations of securities backed by the foregoing must comply with the asset-level disclosure requirements no later than two years after the rules are published in the *Federal Register*.

<sup>1</sup> SEC Regulation AB II Press Release/Fact Sheet (August 2014) is available at <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370542776577> ("SEC Regulation AB II Fact Sheet").

<sup>2</sup> Release 33-9117 (April 2010) available at <http://www.sec.gov/rules/proposed/2010/33-9117.pdf>.

<sup>3</sup> Release 33-9244 (July 2011) available at <http://www.sec.gov/rules/proposed/2011/33-9244.pdf>.

Below is a brief summary of the final rules adopted at the SEC open meeting.<sup>4</sup>

## Shelf Registration Eligibility Criteria & Forms

The SEC eliminated the requirement that asset-backed securities (ABS) be rated investment grade as a condition for shelf registration and replaced it with the following new requirements:

1. **CEO Certification:** The chief executive officer in charge of securitization for the depositor must make certain certifications at the time of each takedown relating to the accuracy of the disclosure in the prospectus and the structure of the securitization. In response to concerns that the original certification could be viewed as a guarantee of the future performance of the underlying assets, the SEC noted that the text of the certification reflected in the final rule will not be phrased in the form of a guarantee.
2. **Asset-Level Review Trigger:** The underlying transaction documents must permit an investor-initiated review of the underlying assets at a minimum upon a two-pronged trigger, consisting of a delinquency trigger and a vote of the investors upon the occurrence of such trigger. A report of the reviewer's findings and conclusions must be provided to the trustee and subsequently filed as an exhibit on Form 10-D.
3. **Dispute Resolutions Mechanics:** The underlying transaction documents must include dispute resolution procedures (e.g., mediation or arbitration) for asset repurchase demands.
4. **Investor Communication:** The underlying transaction documents must provide for the reporting of requests by investors to communicate with other investors in connection with the exercise of an investor's rights, and any communications must be filed as an exhibit on Form 10-D.

The SEC has also adopted two new shelf registration forms, Form SF-1 and Form SF-3. Issuers of ABS that want to register their securities on a delayed basis will use Form SF-3, and issuers who are not eligible to use shelf registration on Form SF-3 will be required to use new Form SF-1. The SEC noted that the final rules relating to the new Forms SF-1 and SF-3 will be adopted largely as initially proposed. The registrant will be permitted to pay the registration fee for securities registered on Form SF-3 on a pay-as-you-go basis.

## Offering Process

The SEC also adopted rules requiring that a preliminary prospectus, in an offering using a shelf registration statement on new Form SF-3, be filed at least three business days prior to the first sale in the offering. The SEC believes that three business days will provide investors sufficient time to conduct an analysis of the offered securities while still accommodating issuer concerns about the length of the waiting period. In the 2010 Proposing Release, the SEC initially proposed a five business day waiting period; however, in response to comments received from industry participants, the SEC shortened the period.

## Asset-Level Data Disclosure

In accordance with the mandate set forth under Section 942 of Dodd-Frank, the SEC adopted asset-level data disclosure requirements for securitizations backed by residential mortgage loans, commercial mortgage loans, automobile loans or leases and corporate debt and resecuritizations of such securities backed by the foregoing. All asset-level

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<sup>4</sup> This Alston & Bird Finance Advisory is based on comments and remarks made by the SEC commissioners and staff at the open meeting and the SEC Regulation AB II Fact Sheet.

information will be required to be filed both at the time of the offering and on an ongoing basis on Form 10-D. In addition, all information will also be required to be filed with the SEC via EDGAR to provide investors access to such information. Issuers must disclose the asset-level information in XML format, a machine-readable language the SEC believes should better enable investors to analyze the cash flows of the ABS. In adopting the asset-level disclosure requirements, the SEC noted that it coordinated with the Consumer Financial Protection Bureau, which advised on aspects of the Fair Credit Reporting Act<sup>5</sup> and other consumer privacy-related concerns. The SEC also emphasized that it revised the asset-level disclosure requirements to address privacy concerns associated with such disclosure that were raised by commenters in connection with the 2010 Proposing Release, 2011 Re-Proposing Release and the SEC memorandum issued on February 25, 2014, addressing the disclosure of asset-level data. Disclosure requirements relating to other asset classes initially proposed in the 2010 Proposing Release (e.g., equipment leases and student loans) will be addressed in a separate final rulemaking.

Although not addressed at the open meeting, the SEC released a fact sheet following the meeting and in advance of the publication of the final rule that notes the SEC has also adopted final rules relating to the following:

### **Amendments to Prospectus Disclosure Requirements**

The SEC rulemaking expands the disclosure obligations of certain transaction parties, including sponsors who will be required to disclose information about the sponsor's retained economic interest in the transaction (both the amount and the nature of the interest). Transaction parties obligated to repurchase assets under the transaction agreements will be obligated to disclose certain information about their financial condition. The rulemaking also requires the issuer to disclose any terms in the transaction agreements allowing for the modification of the underlying assets.

### **Revisions to Regulation AB**

The SEC also approved revisions to Regulation AB, including standardizing the requirements for presentation of certain static pool information in order to increase transparency and comparability and specifying disclosure (to be provided on an aggregate basis) about the type and amount of assets that do not meet the described underwriting criteria. In addition, the rulemaking amended the ABS reporting requirements to require disclosure within the body of the annual report on Form 10-K relating to any material instances of noncompliance with applicable Regulation AB servicing criteria, including identifying in the body of Form 10-K whether or not the material instances of noncompliance involve the servicing of the assets backing the ABS covered on Form 10-K.

### **What's Next**

The SEC announced that the adoption of these rules is the first step toward completing the mandated Dodd-Frank rulemakings. The proposed rules remaining on the drafting table include rules requiring issuers of structured finance products issued under Rule 144A to observe the same disclosure requirements applicable to registered offerings and mandating that transaction documents be filed in final form by the date on which the preliminary prospectus supplement is required to be filed. The SEC also stated that rules relating to risk retention are forthcoming and that it will continue to work with other regulators to finalize the rulemaking hopefully by the end of 2014.

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<sup>5</sup> See Fair Credit Reporting Act 15 U.S.C. 1681 *et seq.*

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