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Dodd-Frank And Asset-Backed Securities: Implementation Of Section 943 (Rep, Warranty And Repurchase Disclosure)

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On January 20, 2011, pursuant to Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the U.S. Securities and Exchange Commission (the “SEC”) promulgated its final rules (the “Final Rules”) regulating disclosure with respect to repurchase demands and the use of representations and warranties in connection with the issuance of asset-backed securities (“ABS”). The Final Rules will become effective sixty days after publication in the Federal Register. As described in more detail below, compliance with the Final Rules is subject to differing transition periods. This article generally highlights the Final Rules.

Final Rules, Generally

The Final Rules comprise two separate rules, both of which apply to registered and unregistered transactions, and an amendment to Item 1104 of Regulation AB:

- Rule 17g-7 requires Nationally Recognized Statistical Rating Organizations (“NRSROs”) to disclose certain information about asset-level and corporate representations and warranties made in ABS for which

they provide credit ratings.

- Rule 15Ga-1 mandates disclosure of certain historical repurchase and substitution demands for assets that were purported to have breached a representation or warranty.

Item 1104 of Regulation AB was amended to mandate additional ongoing reporting as to repurchase activity.

Rule 17g-7

Rule 17g-7 imposes an obligation on NRSROs, in any report provided in connection with a credit rating, to disclose information related to:

- Asset-level and corporate representations and warranties made in the related ABS;
- The mechanism for enforcing representations and warranties; and
- How such representations and warranties differ from those afforded to “similar securities.”

The SEC did not define “similar securities,” leaving broad discretion to the NRSROs. As such, the NRSROs must use industry knowledge to determine the standards against which the NRSROs would compare the representations and warranties of ABS for which they provide ratings.

Any report issued six months after the effective date of the Final Rules must comply with Rule 17g-7.

Rule 15Ga-1

Rule 15Ga-1 requires:

- Any securitizer who has issued ABS within a designated three-year “look-back period” to initially disclose aggregate information across all ABS issued by that securitizer during the look-back period, without regard to the underlying asset classes.

- Any nonmunicipal issuer of ABS in 2009, 2010 or 2011 must file the requisite disclosure by February 14, 2012, if any of such ABS issuances are held by a nonaffiliate of the securitizer as of December 31, 2011.

- Municipal issuers have a three-year delay in obligations to comply.

- Securitizers to provide ongoing reporting with respect to repurchase and substitution demands on a quarterly basis after the initial disclosure regarding the three-year look-back period.

In disclosing information relating to demands for repurchase or substitution of assets, securitizers must display, on an originator-by-originator basis, the following information (among other items): (i) total assets in such securitizer’s ABS originated by the originator; (ii) assets subject to a repurchase demand; (iii) assets actually repurchased or replaced; (iv) assets pending replacement or repurchase; (v) demands in dispute; (vi) demands withdrawn; and (vii) demands rejected. More specifically, securi-

tizers must provide (a) the total number of assets for which demand has been made, (b) the total dollar amount represented by those assets and (c) the percentage of the principal balance of ABS that those assets account for.

Notwithstanding the foregoing, the Final Rules permit securitizers to omit information that is unknown or not reasonably available without unreasonable effort or expense.

Item 1104 Of Regulation AB

The SEC adopted a new clause (e) to Item 1104 of Regulation AB, which applies Rule 15Ga-1 on a transaction-by-transaction basis by requiring repurchase disclosure in connection with all ABS with an initial bona fide offer after February 14, 2012. Item 1104(e) requires disclosure of:

- Asset-class-level repurchase demand history in prospectuses (which information may not be aged more than 135 days); and
- Repurchase demand history for a particular transaction in all Form 10-Ds.

The SEC granted securitizers a ramp-up period for compliance by requiring only one year of repurchase demand history disclosure for prospectuses filed between February 2012 and February 2013 and two years of repurchase demand history disclosure for prospectuses filed between February 2013 and February 2014.