

# FINANCIAL INSTITUTIONS ALERT

NEWS FOR THE CLIENTS AND FRIENDS OF BASS, BERRY & SIMS PLC

## Dodd-Frank's Disclosure Requirements for Asset-Backed Securities

November 8, 2010

Under the recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act"), the Securities and Exchange Commission ("SEC") is tasked with drafting nearly 100 new rules and regulations. Currently on the SEC's plate are regulations related to offerings of Asset-Backed Securities ("ABS"). The core focus of the pertinent portion of the Act (§ 943) is to provide investors in ABS with information to "identify asset originators with clear underwriting deficiencies."<sup>1</sup> In furtherance of this objective, Section 943 requires entities that create an ABS ("securitizers") to provide certain information about the entities that originated the loans underlying the ABS ("originators"). Section 943 applies to the following scenario:

Suppose a hypothetical ABS called "Airplane Lease Trust" is securitized by Off Wall Street Investment Bank ("Off Wall Street") based on a pool of airplane leases originated by First Local Bank ("Local Bank"). Off Wall Street includes a clause in its transaction agreement that allows it to demand that Local Bank repurchase underlying pool assets that do not comply with its representations and warranties and replace the non-compliant assets with complying assets. As certain pool assets in Airplane Lease Trust begin to default, Off Wall Street learns that those assets do not comply with the representations and warranties in the transaction agreement and requests that First Local Bank repurchase those assets and replace them with complying assets.

Under Section 943, information on Off Wall Street's fulfilled and unfulfilled repurchase requests to Local Bank would be made available to investors and to the Nationally Recognized Statistical Ratings Organizations ("NRSROs") (*e.g.*, Standard & Poor's, Moody's and Fitch). The NRSROs would be required to include this information in any report accompanying a rating on Airplane Lease Trust. This information may also result in the NRSROs giving Airplane Lease Trust a lower credit rating which, in turn, would likely result in a lower market value for Airplane Lease Trust. In addition, Off Wall Street and Local Bank may suffer reputational harm.<sup>2</sup>

<sup>1</sup> Dodd-Frank Act, 111th Cong. § 943 (2010).

<sup>2</sup> For example, other securitizers may not want to work with Local Bank because its prior violations of representations and warranties could increase the securitizer's risk and decrease the value that an ABS based on Local Bank's assets would achieve in the market. Likewise, other originators may not want to work with Off Wall Street because its prior relationship with Local Bank may reflect due diligence failures by Off Wall Street, which may decrease the value of future ABS securitized by Off Wall Street. This could also reduce the value of Off Wall Street's or Local Bank's overall businesses and decrease Local Bank's lending activity.

In the 71-page SEC release containing the proposed regulation contemplated by Section 943,<sup>3</sup> the SEC has requested comment on the following nine key issues:<sup>4</sup>

- (1) whether the proposed rule clearly states what securities, persons and entities are subject to the disclosures;
- (2) whether it is appropriate and feasible to require that securitizers make their disclosures in a specific table format, and include five years of information on ABS that remain outstanding and held by non-affiliates;
- (3) whether it is appropriate to create a new form for the disclosures, and if so, what information should be included in the form;
- (4) whether the rule should be modified for foreign transactions;
- (5) whether it is appropriate to require issuers to provide three years of fulfilled and unfulfilled repurchase request history in the prospectus, and whether the issuer should also be required to provide information about the securitizer in the prospectus;
- (6) whether and how the SEC should define “similar securities” for purposes of NRSROs’ comparisons of repurchase requests in reports attached to credit ratings;
- (7) whether NRSROs and securitizers should be permitted to fulfill their disclosure requirements by referencing the disclosures in an issuer’s prospectus and periodic reports;
- (8) whether any of the proposals should be phased in or should be based on a tiered approach relating to, for example, the size of the securitizer; and
- (9) whether the proposed rule strikes an appropriate balance between the burden of the disclosures and the utility of the information provided.

Financial institutions and broker-dealers should consider commenting on the proposed regulation. We will be happy to discuss the specifics of the SEC’s proposed rule with you in greater detail and, if desired, work with you to develop comments by the SEC’s November 15, 2010 deadline.

If you have any questions regarding the information in this alert, or with respect to other provisions of this legislation, please contact any of the attorneys listed below in our business or litigation Financial Institutions Groups or in our Broker-Dealer and Financial Products Group.

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<sup>3</sup> Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Securities Act Release No. 33-9148, Exchange Act Release No. 34-63029 (Oct. 4, 2010), available at <http://www.sec.gov/rules/proposed/2010/33-9148.pdf>.

<sup>4</sup> The release also contains a blanket request for comments on any of the specific issues discussed therein.

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