

Regulation AB: New Rules for Publicly Issued Asset-Backed Securities

Skadden

January 2015

This article is from Skadden's *2015 Insights* and is available at skadden.com/insights.

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In August 2014, the Securities and Exchange Commission revised the existing regulations that govern the offering process and the disclosure and periodic reporting requirements for publicly offered asset-backed securities (ABS) under Regulation AB. For publicly issued asset-backed securities, the new rules will put speed bumps in the offering process, introduce new parties to ABS transactions and require certain asset classes to provide significantly more information with respect to the underlying asset pool. The new rules were originally proposed in 2010 — before the enactment of the Dodd-Frank Act — but have been modified to address certain requirements of Dodd-Frank.

Shelf Eligibility

The new rules replace requirements for eligibility to use a shelf registration statement — including that the securities offered be rated investment-grade by a nationally recognized statistical rating organization (NRSRO) — with provisions that require:

- a certification from the depositor's CEO covering familiarity with the prospectus, the assets, the structure and the material transaction documents and stating that the CEO has a reasonable basis to conclude that the securitization is structured to produce cash flows in amounts sufficient to service scheduled payments. Issuers will need to implement new procedures for preparing CEOs to provide this certification and will be required to file this certification in connection with each offering of the notes;
- that transaction documents provide for the appointment of an "asset representations reviewer," which would conduct a review of compliance with representations and warranties made with respect to the pool assets if delinquencies were to exceed a threshold level. The SEC allows issuers to determine the delinquency trigger and engage the asset representation reviewer, but given that this is a new role, many aspects of this requirement remain to be clarified, including the procedures to be undertaken by the reviewer and how the reviewer will be compensated; and
- that transaction documents include a dispute resolution mechanism and provisions to accommodate requests by investors to communicate with other investors.

The new rules require the filing of a preliminary prospectus at least three business days prior to the first sale of securities in the offering. This provision will slow down current market practices and may cause most ABS securities to be offered on the same schedule with preliminary prospectuses being circulated on Mondays or Tuesdays and pricings on Thursdays or Fridays.

Asset-Level Data

The new rules also require issuers of ABS backed by residential mortgages, commercial mortgages, auto loans, auto leases and debt securities (including resecuritizations) to provide standardized asset-level data in both prospectuses and periodic reports. The amount of data required is significantly greater than the amount disclosed under current requirements and market practices for most asset classes. As such, the rules will require significant effort on the part of issuers to assemble and verify the required information.

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Other Provisions

Additional requirements of the new rules include:

- New Forms SF-1 and SF-3, which have disclosure requirements specific to ABS, are to be used by ABS issuers in lieu of Forms S-1 and S-3;
- Final transaction documents must be filed not later than the date the final prospectus is filed rather than at or after closing, as is common under current market practice;
- Registration fees can be paid on a pay-as-you-go basis; and
- A single prospectus must be used rather than a base prospectus and a supplement, as is common currently for shelf offerings.

Implementation Timeline

Issuers of publicly registered ABS will be required to use new Forms SF-1 and SF-3 and comply with new disclosure requirement and shelf eligibility criteria applicable to registered ABS offerings beginning no later than November 23, 2015. Offerings of ABS backed by residential and commercial mortgages, auto loans and leases, and debt securities must comply with asset-level disclosure requirements no later than November 23, 2016.

Items Not Addressed

The SEC indicated in the implementing release that it still intends to address certain items that were proposed in 2010 but were not covered in the final rules, including:

- asset-level data requirements for asset classes that are not subject to this requirement in the final rule and grouped account data requirements for credit card ABS;
- disclosure requirements for private offerings of ABS; and
- a waterfall computer program reflecting the cash flow provisions for each ABS transaction.

The SEC has indicated to market participants that it is focusing on implementing rules addressing these remaining items, so additional new rules for the ABS market may be forthcoming in 2015.