

Structured Finance Newsletter

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PROPOSED ABS REGULATORY CHANGES FROM THE SEC

On April 7, 2010, the Securities and Exchange Commission (SEC) approved proposed changes to the regulation of asset-backed securities in order to provide investors with sufficient information to make an investment decision and ample time to analyze the information provided. The SEC has also proposed certain changes in the retention requirements for issuers and provides for additional disclosure in private transactions in an effort to provide more transparency to the private market. These proposed regulations have been released for public comment following a 90 day period from the date of publication in the Federal Register.

Information

The proposal includes the requirement for loan level information to be provided by ABS issuers which would include certain "data points" for specific asset classes. The requirements address both disclosure at the time of the securitization and on an ongoing basis. Issuers must also produce a loan level cash flow model that allows investors to analyze the loan level data and transaction cash flows using the Python open source model.

There will be two new forms for filing asset-backed securities: SF-1 and SF-3 which will incorporate static pool information and the cash flow model by reference. Issuers will be required to post static pool information in PDF format on EDGAR. There will be a minimum 5 day waiting period following the filing of the prospectus in order to allow investors "sufficient time" to analyze the information. If there are changes to the prospectus information, then it will need to be re-filed, which starts a new 5 day waiting period.

Alignment of Interests

There will no longer be a requirement for investment grade credit ratings for a shelf registration. Instead, there will be four new eligibility criteria:

1. CEO needs to certify that the assets have characteristics that provide a reasonable basis to believe they will produce cash flows as described in the prospectus;
2. ABS sponsor would be required to maintain 5% interest in the securitization (of each tranche), net of hedging, to ensure the sponsor has "skin in the game";
3. ABS issuer would be required to provide a third party's opinion on whether the assets comply with the issuer's reps and warranties that the loans in the ABS pool were underwritten consistent with the issuer's underwriting standards;
4. ABS issuer would have to agree to file Exchange Act reports with the SEC on an ongoing basis.

Transparency in the Private Market

There will be more disclosure required in the private market as well as the public market so as not to drive ABS deals into the private market. If a transaction is private (144A or Regulation D), then issuers would have to provide investors, upon request, with the same information required for a public transaction. This information would have to be available upfront and on an ongoing basis. The ABS issuer would also have to file a public notice of the initial placement of securities sold under Rule 144A or Regulation D.

The goal of providing adequate information and time for investors to review that information is beneficial to investors and the market overall. However, some concerns regarding the proposals have been raised by the industry and include the overall expense associated with implementing these regulations for issuers on an ongoing basis and the complexity in establishing a loan level cash flow model which can be applied to different asset classes. As a result, DBRS will continue to review and comment on these proposals as well as monitor the regulation for any revisions after the comment period.

For questions or comments, please contact Rosemary Kelley at rkelley@dbrs.com.

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