

HAWKINS ADVISORY

UPCOMING RECORDKEEPING REQUIREMENT UNDER SECTION 943 OF THE DODD-FRANK ACT

OVERVIEW

On January 20, 2011, the Securities and Exchange Commission (the "SEC") adopted final rules¹ relating to disclosure and diligence responsibilities with respect to the underlying portfolios securing asset-backed securities ("ABS") pursuant to Sections 943 and 945 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").² **The Section 943 disclosure rules, for municipal issuers, have a three-year delayed compliance date, BUT require record-keeping commencing January 1, 2012.**

"Asset-backed security" is defined in Section 3(a)(77) of the Securities Exchange Act of 1934 (the "34 Act") (added by Section 941 of the Dodd-Frank Act) as follows:

[A] fixed-income or other security *collateralized by any type of self-liquidating financial asset* (including a loan, a lease, a mortgage, or a secured or unsecured receivable) that allows the holder of the security to receive payments that depend primarily on cash flow from the asset. (emphasis added)

One concern for municipal issuers is that this broad definition goes beyond what are generally considered to be securitizations, and could be read to include certain conduit financings, student loan financings, and single family housing financings, among others.³

SECTION 943

There are five key sections of the Dodd-Frank Act that apply to ABS. Only Section 943 applies at this time to municipal securities. Section 943 requires the SEC to adopt regulations on the use of representations and warranties in the market for ABS that would require any securitizer⁴ to disclose fulfilled and unfulfilled repurchase requests across all trusts aggregated by the securitizer, so that investors may identify asset originators with clear underwriting deficiencies"

The new disclosure rules under Section 943 would only apply to an ABS issue if the underlying agreements securing the ABS contained a covenant to repurchase or replace an asset that was included in the securitized asset pool in response to the noncompliance of that asset with a representation or warranty.⁵ If such a covenant is present, then the new rules will require ABS securitizers to disclose demand, repurchase and replacement history in a tabular format:

- initially, after the applicable transition period, through the EDGAR or (with respect to certain "municipal securitizers") the EMMA system, for a three-year, look-back period
- periodically thereafter, on a quarterly basis, through the EDGAR or (with respect to certain "municipal securitizers") the EMMA system, for such quarter
- upon issuance, in the body of the prospectus or Official Statement for a three-year, look-back period

¹ SEC Rel. Nos. 33-9175, 34-63741 (Jan. 20, 2011); <http://www.sec.gov/rules/final/2011/33-9175>; SEC Rel. Nos. 33-9176, 34-63742 (Jan. 20, 2011); <http://www.sec.gov/rules/final/2011/33-9176>.

² Pub. L. 111-203 (July 21, 2010).

³ Comment letter of the National Association of Bond Lawyers ("NABL") (Nov. 19, 2010).

⁴ The term "securitizer" includes any issuer of an ABS. (New Section 15G(a)(3) (A) of the 34 Act).

⁵ It should be noted that Section 943 would not be applicable to any municipal financing where the bond issuer does not undertake or covenant to repurchase or replace a loan or an asset securing the bonds. For example, it is almost always the case in conduit financings secured by a loan or loans made to one or more corporations, including hospitals, colleges and universities, and other non-profit corporations, or in municipal bond bank or pooled or composite financings, that the bond issuer does not undertake to repurchase or replace the loans or assets securing the bonds.

In each case, the information required relates to all asset pools with covenants requiring repurchase or replacement of an underlying asset in response to violation of a representation or warranty (including servicing as well as underwriting nonconformance) under which ABS were outstanding during the applicable reporting period.⁶ As explained in the adopting release:

[B]oth sponsor and depositors fall within the definition of securitizer and are thus obligated under Section 943 and the new rule to provide the disclosures. The final rule addresses commentators' requests because sponsors typically securitize assets of different classes through separate affiliated depositors for each asset class. For example, if a sponsor has two different affiliated depositors, one that securitizes auto loans and the other credit cards, the sponsor's reporting obligation would be satisfied if each of the depositors filed the required disclosures with respect to all of their respective trusts. Thus, a sponsor would not have to separately provide and file the same disclosures, if they were filed by an affiliated depositor of the same transaction.⁷

Although the generally applicable transition period requires initial reporting by February 14, 2012, with respect to a three-year, look-back period ending December 11, 2011, the SEC granted "municipal securitizers" a three year additional period before compliance is required. The new Section 943 rules will require the initial filing to be made by such "municipal securitizers" on February 14, 2015, for the three years ended December 31, 2014. Thus, municipal securitizers would need to keep records of demands, repurchases, and replacements that occurred on and after January 1, 2012. The term "municipal securitizer" is defined, solely for purposes of this delayed compliance, to include States, United States Territories, the District of Columbia and any political subdivision or public instrumentality of any of these.⁸

⁶ The SEC determined not to limit the disclosure requirement to representations and warranties concerning underwriting standards, as had been suggested by some commentators.

⁷ SEC Rel. Nos. 33-9175, 34-63741 (Jan. 20, 2011), fn. 82.

⁸ It would appear that some public finance market issuers that might be deemed securitizers under the rule may not fall within this definition; additional guidance would be desirable.

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