

SEC Rule Casts 2-Year Compliance Shadow

Securitization professionals are trying to get a better handle on how to comply with new regulations on price quotes for fixed-income securities.

The controls, initiated via an update to the **SEC's** Rule 15c2-11, prohibit broker-dealers from electronically displaying prices for over-the-counter bond offerings unless current financial information about the issuers is publicly available.

But for securitizations, such documents often are unavailable or irrelevant. And that has industry participants looking at alternative ways to satisfy the SEC, with some vendors spotting opportunities in the change as well.

Rule 15c2-11, part of the Securities and Exchange Act of 1934, originally was intended to combat fraudulent activity in pink-sheet stocks. A 2020 amendment, meanwhile, broadened enforcement into secondary fixed-income trades but went little noticed until just before it was set to take effect in September 2021.

Amid last-minute lobbying from trade groups including **Sifma** and the **Structured Finance Association**, the SEC then pushed back the initial compliance deadline to Jan. 3 — meaning industry participants still are relatively early in the process of sorting out which steps are appropriate.

Another hiccup: Under the SEC's guidance, dealers have three years to phase in their compliance practices, but only for securities that are SEC registered or issued under Rule 144A. Bonds that priced via private placements still are subject to the measure from day one.

To be sure, the impact on those securities likely will be limited because they often reside with buy-and-hold investors and rarely appear on the secondary market. "If done properly, your buyers never sell," said a warehouse lender who finances student loans intended for privately placed securitizations.

Even for registered securities, however, it's still unclear what constitutes compliance. SEC guidance suggests that servicer reports would be acceptable substitutes for the types of financial disclosures required of operating companies, at least initially.

During an initial compliance phase that lasts until January 2023, dealers must reasonably believe the issuer will provide the specified information upon request. To that end, **Patrick Dolan**, a partner at law firm **Norton Rose** and a member of an SFA committee studying the rule, believes a password-protected website with servicer reports likely would suffice.

During a second phase that lasts until January 2024, dealers could publish quotes on securities only if current financial information about issuers is publicly available. That could require another disclosure medium.

The third and final phase would entail steps unrelated to securitization, but could mark a point at which servicer reports no longer suffice for those deals.

Regardless of how that process turns out dealers attempting to comply with the rule are likely to incur costs that they might attempt to pass along to trading counterparties through the prices of the securities.

That's where vendors come in. **Bloomberg** and possibly others already are developing software that would help dealers fulfill the SEC's requirements by aggregating disclosures.

As originally written, the Rule 15c2-11 update would have required dealers listing prices on a quotation medium such as an electronic trading system to review information such as issuer balance sheets and profit-and-loss statements. But those documents don't exist in the same formats for the bankruptcy-remote vehicles used in securitization.

Even if they were available, "this information is not meaningful to investors in securitizations, who are primarily focused on information regarding the performance of the underlying financial assets backing the asset-backed bonds," Dolan said.

The upshot: Had the requirement gone into effect as planned, the secondary market for securitized products likely would have slowed substantially as dealers resorted to supplying price quotes by telephone, substantially reducing transparency and liquidity. ❖