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SEC Guidance and No-Action Address 436(g) Repeal Issues

Melissa Klein Aguilar

The Securities and Exchange Commission has taken swift action to address one of the undoubtedly long list of issues stemming from the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

The staff of the Division of Corporation Finance has issued guidance and no-action relief to deal with an issue stemming from the Act's repeal of Rule 436(g) under the Securities Act of 1933, which threatened to effectively freeze asset-backed securities markets and cause a major disruption in the fixed income markets.

The Securities Act requires written consent of an "expert" (any person named in a registration statement or prospectus as having prepared or certified a portion of the registration statement or prospectus) to be filed with the SEC, and subjects those experts to a higher standard of liability.

Rule 436(g) had exempted nationally recognized statistical rating organizations like Moody's from being considered "experts" if their ratings were included in a Securities Act registration statement or prospectus, but its repeal under the Dodd-Frank Act took effect July 22.

That became a problem when Moody's, Standard & Poor's, and Fitch all announced that they wouldn't consent to the use of their ratings in registration statements because of the potential added liability.

"Most corporate debt issuers include their credit ratings somewhere in their offering terms sheets and periodic reports," which are incorporated by reference into Securities Act registration statements and prospectuses, says **Eric Blanchard**, a partner in the law firm **Dewey & LeBoeuf**, and co-author of an alert on the topic. The trouble was worse for asset-backed securities issuers, because they're required under Regulation AB to disclose the ratings and identity of the NRSROs in their registration statements.

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“Without the relief of the SEC no-action letter, those issuers wouldn’t be able to conduct any deals,” says Blanchard.

He says the repeal apparently caught the industry by surprise because while “it had been on the table,” it wasn’t included in the Senate-passed version of the legislation, but was slipped in later.

A July 22 no-action letter issued by the Division of Corporation Finance staff in response to a request by Ford Motor Credit Co. provides broad relief to asset-backed issuers, allowing them to avoid an enforcement action for omitting the credit ratings disclosure from registration statements filed under Regulation AB.

However, Blanchard notes that the staff no-action relief expires in six months, so those issuers will have to stay tuned to see what long-term fix is worked out.

For corporate debt issuers, the staff published five Compliance & Disclosure Interpretations (see New Question 233.04, New Question 233.05, New Question 233.06, New Question 233.07, and New Question 233.08) which Blanchard says “essentially bless common practice followed by most corporate debt issuers.”

The July 22 C&DIs confirm that consent by a credit rating agency is required if ratings information, other than issuer disclosure-related ratings information, is included in, or incorporated by reference into, a Securities Act registration statement, a prospectus, or prospectus supplement first filed on or after July 22, 2010. However, that consent isn’t required if the rating information is included only for the purpose of satisfying disclosure requirements—for example, if the disclosure is related only to changes to a credit rating, liquidity, the cost of funds for a registrant, or the terms of agreements that refer to credit ratings.

The interpretations also confirm that rating information included in Rule 433 free writing prospectuses or in term sheets or press releases that comply with Securities Act Rule 134 doesn’t require consent. The staff also issued an interpretation that grandfathers in the continued use of registration statements on Form S-3 or Form F-3 declared effective before July 22, 2010, that include ratings information without a consent.