Overview of the Securities Act of 1933 as Applied to Private Label Mortgage-Backed Securities

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Summary

Mortgage-backed securities that are packaged and issued by private industry participants are required to comply with the Securities Act of 1933. Issuers of so-called private label mortgage-backed securities must either register these securities pursuant to the rules the Securities and Exchange Commission has set forth, or obtain an exemption from registration. Failure to register or fall under an exemption could result in liability for the issuer and other parties involved in the offering. Furthermore, material misstatements or omissions in the offering materials may also result in liability under the Securities Act. This report will provide an overview of the Securities Act of 1933 as it may be applied to mortgage-backed securities issued by private industry participants.

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Introduction

Generally speaking, there are two types of mortgage-backed securities (MBSs). The first are those securities that are packaged and issued by government sponsored entities (GSEs) — the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac") — and a wholly owned government corporation, the Government National Mortgage Association ("Ginnie Mae"). The second are those MBSs that are packaged and issued by private market participants (i.e., mortgage companies, savings and loans, and commercial banks), known as private label MBSs.

The laws governing the issuance of these two types of MBSs are different. MBSs offered by the GSEs and Ginnie Mae are exempt from the registration requirements and ongoing disclosure obligations contained in the federal securities laws.[1] Private label MBSs do not enjoy a blanket exemption from the federal securities laws and are classified by the Securities and Exchange Commission as a type of "asset-backed security" (ABS) that must register under the Securities Act of 1933 ('33 Act or Securities Act) or obtain an exemption and provide continuing disclosures required by the Securities Exchange Act of 1934 ('34 Act or Exchange Act).[2]

This report will provide an overview of the registration requirements for private label MBSs under the Securities Act. It also highlights the most frequently used exemptions for private label MBSs. It outlines potential liability for fraud and/or material misstatements in the required disclosures and the consequences for failure to register when required by federal securities laws. This report will not discuss reporting requirements or liability for MBSs under the Exchange Act of 1934.[3]

[1] Ginnie Mae is a wholly owned corporation of the U.S. government and the securities it guarantees are exempt securities under Section 3(a)(2) of the Securities Act of 1933 (15 U.S.C. § 77c(a)(2)) and Section 3(a)(12) of the Securities Exchange Act of 1934 (15 U.S.C. § 78c(a)(12)). The Federal National Mortgage Association Charter Act provides that securities guaranteed by Fannie Mae will be exempt securities in the same manner as those guaranteed by Ginnie Mae. 12 U.S.C. § 1723c. A similar exemption for Freddie Mac-guaranteed securities is contained in the Federal Home Loan Mortgage Corporation Act. 12 U.S.C. § 1455g. It is worth noting that these exemptions do not exempt these securities from all of the antifraud provisions. For instance, Section 10(b) of the Exchange Act and Rule 10b-5 apply to all issuers of securities whether or not the security was registered. 15 U.S.C. §78j; 17 C.F.R. § 10b-5.

[2] Securities Act Release No. 33-8518; 34-5095, 70 Fed. Reg. 1506 (Jan. 7, 2005) ("Final Rule in Regulation AB"). Codified at 17 C.F.R. Parts 210, 228, 229 *et al*.

[3] Many MBS issuers are able to suspend their reporting obligations under the Exchange Act, because the offerings typically have such a small number of record holders. *See* Final Rule in Regulation AB, *supra* note 2, §III D. Section 15(d) of the Exchange Act suspends reporting requirements each year so long as there are fewer than 300 record holders at the beginning of the year. 15 U.S.C. §78o(d). This assumes that the MBS is not trading on a national securities exchange or automated quotation system (which MBSs, again typically, do not), because such trading would trigger registration requirements under Section 12 of the Exchange Act. 15 U.S.C. §78*l*. Suspension of reporting requirements does not mean exemption from liability under other portions of the Exchange Act. *See e.g.*, 15 U.S.C. §78j.

Securities Act Registration for Private Label Mortgage-Backed Securities

The Securities Act requires issuers of all types of securities to register the offering with the Securities and Exchange Commission (SEC) or to qualify for an exemption from the registration requirements.[4] A registration statement consists of two parts: a prospectus, which must be delivered with every offer to sell the securities and contain the information outlined in Section 10 of the Securities Act,[5] and other information which need not be provided to potential purchasers but must be on file with the SEC and available for public inspection.[6] Failure to file a registration statement when one is required results in a violation of Section 5 of the '33 Act and strict liability under Section 12(a)(1).[7]

The Registration Statement for Private Label MBSs

Sections 4 and 5 of the Securities Act require issuers of securities to register the offerings and provide prospectuses for sales that are not exempt.[8] Sections 7 and 10 of the Securities Act prescribe the information required in the registration statements and prospectuses that are issued pursuant to offerings under Sections 4 and 5.[9] Section 7 requires the registration statement to contain the information and documents outlined in Schedule A (15 U.S.C. §77aa), which is the Schedule under which all issuers that are not foreign governments must file.[10] Section 7 grants the Commission the power to prescribe rules and regulations describing the information and documents to be contained in registration statements if the Commission deems them to be "necessary or appropriate in the public interest or for the protection of investors."[11]

Pursuant to this authority, the Commission has designed registration statements, which correspond to the various types of securities and types of issuers of securities. For private label MBSs, issuers must use either registration statement Form S-1 or Form S-3.[12] Form S-3 is the preferable registration statement type for most issuers because it is considered to be less burdensome than other types of registration statements. In order to be eligible for Form S-3, in most cases, the registrant must already have a class of securities registered pursuant to Sections 12(b) or 12(g) of the Exchange Act (15 U.S.C. §78*l*), or be required to file reports pursuant to

[4] *See* Sections 3(b), 4, 5, 7 of Securities Act, 15 U.S.C. §77b-g.

[5] 15 U.S.C. § 77j.

[6] Section 7 of Securities Act, 15 U.S.C. §77g.

[7] Section 12(a)(1) of the Securities Act states that any person who sells a security in violation of Section 5 (15 U.S.C. §77e) is liable to the person purchasing the securities from him for the purchase price with interest, less any income received from the security or for damages if the purchaser no longer owns the security.

[8] 15 U.S.C. §§ 77d – 77e.

[9] 15 U.S.C. §§ 77g, 77j.

[10] Section 7 of Securities Act, 15 U.S.C. §77g. A Section 10 prospectus is required to contain much of the information contained in the registration statement, unless the prospectus is of a type permitted by the Commission that summarizes or omits information contained in the base prospectus. Furthermore, the Commission may require more information to be provided in prospectuses by rule or regulation. 15 U.S.C. §77j.

[11] *Id.*

[12] Final Rule in Regulation AB, *supra* note 2, §III B.

Section 15(d) of the Exchange Act for at least the preceding 12 months (15 U.S.C. §78o).[13] The Commission included this requirement under the theory that information contained in the disclosures required by these sections could be incorporated by reference into the new MBS registration, thereby reducing the work required to prepare a new MBS registration statement.[14] The registrant must also have filed all reports required in a timely manner within the previous 12 months.[15]

If the MBS offering qualifies as an offering of investment grade securities, however, the requirements for use of Form S-3 are slightly different. A non-convertible security (such as an MBS) may qualify as an investment grade security if, at the time of sale, "at least one nationally recognized statistical rating organization ... has rated the security in one of its generic rating categories which signifies investment grade; typically, the four highest rating categories (within which there may be sub-categories or gradations indicating relative standing) signify investment grade."[16] An offering of investment grade MBSs occurs when MBSs that qualify as investment grade are offered for cash and delinquent assets within the asset pool do not constitute 20% or more of the pool (measured in dollar volume).[17]

If the offering is an offering of investment grade MBSs, the registrant is not required to have securities registered pursuant to Sections 12(b) or 12(g) of the Exchange Act (15 U.S.C. §78*l*) or be subject to the reporting requirements of Section 15(d) of the Exchange Act (15 U.S.C. §78o) in order to register using Form S-3.[18] The issuer of an offering of investment grade MBSs still must have filed all reports required in the previous 12 calendar months in a timely fashion to qualify to use Form S-3.

If the MBS offering does not qualify to use Form S-3, then the offering must be registered on Form S-1, which is the form all registrants must use if they do not qualify to register on another form.[19]

Shelf-Registration

Shelf-registration allows an issuer to file a registration statement and, instead of selling the securities immediately following the effective date, place the securities on a "shelf" to be sold when the issuer believes the time to be right.[20] This is a popular method of registration for private label MBSs. Mortgage related securities, a subset of MBSs, automatically qualify for "shelf-registration."[21] Even if the private label MBS offering in question is not a mortgage related security, the private label MBS offering may qualify for shelf-registration nonetheless.[22]

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[13] 17 C.F.R. § 239.13.

[14] *See* Item 12, Form S-3, 17 C.F.R. § 239.13.

[15] 17 C.F.R. § 239.13.

[16] 17 C.F.R. § 239.13 (b)(2). A non-convertible security is a security that cannot be converted into some other security.

[17] 17 C.F.R. § 239.13 (b)(5).

[18] 17 C.F.R. § 239.13 (a)(4).

[19] 17 C.F.R. § 239.11.

[20] *See* Wilmarth, Jr., Arthur E., The Transformation of the U.S. Financial Services Industry, 1975-2000: Competition Consolidation and Increased Risk, 2002 U. Ill. L. Rev. 215, 410 ("A shelf registration permits a qualified issuer to sell securities at any time during an extended offering [period].").

[21] Rule 415 under the Securities Act, 17 C.F.R. §230.415 (a)(vii). In order to be considered a "mortgage related (continued...)

For private label MBS offerings, the securities may remain on the "shelf" for up to three years from the initial effective date.[23] Once the company "takes down" the securities for sale, if there has been a change involving the structural features of the MBSs, credit enhancement or other aspects of the MBSs that were not described in the base prospectus, a new registration statement, or post-effective amendment may be required.[24] Some changes do not warrant such labor intensive disclosure, however, and the changes may be described in the final prospectus filed with the SEC.[25] If the securities have not been sold by the end of the original three-year period, another registration statement may be filed.[26]

Regulation AB

Private label MBSs are required to file registration statements that comply with Regulation AB.[27] Regulation AB is tailored specifically to various types of asset-backed securities (like MBSs).[28] The Commission realized that disclosures required by other SEC regulations were not properly tailored to elicit useful information for MBS investors.[29] Other regulations required too much information irrelevant to MBSs and little or no information about other aspects of MBSs that investors needed in order to make informed investment decisions. Therefore, Regulation AB requires more information about the assets in a particular securitized pool, delinquent assets in the pool, the structure of the transaction, the experience of the servicer of the asset pool as well as other parties involved in administering the particular asset pool at issue, and other information unique to offerings of asset-backed securities (like credit enhancements on the asset pool).[30] Information with respect to the registrant (management of the registrant company, performance of the registrant company's stock) may be omitted for MBS offerings because this information does not necessarily inform the investor about the potential performance of the asset pool.[31]

Exemptions

Certain offerings of private label MBSs may be exempt from registration under the Securities Act. The most common exemptions for MBS offerings are described below.

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security" the security must be rated in one of the top two ratings by at least one nationally recognized statistical rating organization. 15 U.S.C. § 78c(a)(41).

[22] 17 C.F.R. §230.415 (a). The rule allows for shelf-registration of securities that are registered on form S-3.

[23] Rule 415(b), 17 C.F.R. §230.415.

[24] *See* Final Rule in Regulation AB, *supra* note 2, §III.

[25] Securities Act Rule 424, 17 C.F.R. §230.424.

[26] Rule 415(b), 17 C.F.R. §230.415.

[27] *See* 17 CFR §§ 229.110 – 229.1123.

[28] "Asset-backed security means a security that is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distributions of proceeds to the security holders ... " 17 C.F.R. § 229.1101(c). The definition is intentionally broad, because the Commission intended to create a principals based approach to disclosure relating to these types of assets rather than a set of rigid rules for each different type of ABS. *See* Final Rule in Regulation AB, *supra* note 2.

[29] *See* Final Rule in Regulation AB, *supra* note 2.

[30] *See* 17 CFR §§ 229.110 – 229.1123.

[31] *See* Final Rule in Regulation AB, *supra* note 2.

Private Placement Offerings (Regulation D)

The most common exemption from registration for MBSs is the exemption for so-called "private placement offerings." Section 4(2) of the Securities Act exempts "transactions by an issuer not involving any public offering."[32] Section 3(b) allows the Commission to exempt certain offerings, not in excess of a specified dollar amount, from registration by rule or regulation. Pursuant to its authority in these two sections, the Commission adopted Regulation D.[33] Regulation D, found in Rules 501 through 508 under the Securities Act, provides guidance to issuers regarding which offerings would not be considered "public offerings."[34] The issuer must file notice with the SEC of any sales pursuant to Regulation D.[35]

Rule 504

Under Rule 504, an issuer (except an issuer that is an investment company) may sell up to $1 million worth of private label MBSs in any 12-month period to any number of purchasers, regardless of their accreditation.[36] No information is required to be provided to investors purchasing securities pursuant to this exemption.[37]

Rule 505

An issuer may sell up $5 million worth of private label MBSs in a 12 month period to any number of accredited investors and up to 35 other purchasers.[38] Accredited investors are defined to include large, frequent market participants that are presumed to have the ability to independently obtain the information that they need.[39] If the securities are offered to unaccredited investors, some disclosure is required under Rule 502, but a full registration statement is not required.[40]

Rule 506

Rule 506 is likely the most common exemption from registration for MBSs. Under this rule, an issuer may sell any amount of securities to any number of accredited investors[41] and up to 35 so-

[32] 15 U.S.C. §77d.

[33] 15 U.S.C. §77c (b).

[34] 17 C.F.R. §§ 230.501-508.

[35] 17 C.F.R. § 230.503.

[36] 17 C.F.R. § 230.504.

[37] *Id.*

[38] 17 C.F.R. § 230.505. However, in order to calculate the number of purchasers of securities, one must refer to Rule 501 (e), which exempts accredited investors from the total number of purchasers when calculating that number for purpose of exemptions under Rules 505(b) and 506(b). 17 C.F.R. § 230.501(e).

[39] They are, for example, banks, insurance companies, investment companies, employee benefit plans, business development companies, large charitable and educational institutions, directors, executive officers, and general partners of the issuer, persons with a net worth about $1 million, persons with an annual income of more than $200,000, and any trust valued over $5 million that is run by a sophisticated person. 17 C.F.R. § 230.501(a).

[40] 17 C.F.R. § 230.502(b).

[41] *See* 17 C.F.R. § 230.501(a).

called "sophisticated investors."[42] In order for the unaccredited investors to be considered "sophisticated," the issuer must reasonably believe that those investors (or their representatives) are capable of evaluating the merits and risks of the securities offered.[43] If the securities are offered to unaccredited investors, some disclosure is required under Rule 502, but a full registration statement is not required.[44]

Section 4(6) of the Securities Act

This section exempts sales of up to $5 million from registration if the sales are made to accredited investors.[45] To qualify for this exemption, the issuer may not publicly advertise the sale of the securities, nor may the issuer publicly solicit buyers. The issuer must also file notice with the Commission of the sale, a requirement similar to that of Regulation D.

Rule 144A

Rule 144A allows the unlimited resale of securities that were never registered pursuant to the Securities Act so long as the purchaser is a "qualified institutional buyer" (QIB).[46] QIBs are defined as enumerated types of institutional investors (i.e., insurance companies or employee benefit plans) that own over $100 million in securities unaffiliated with the entity making the offering.[47] Because the market for private label MBSs consists primarily of QIBs, Rule 144A is commonly used.[48]

Section 28

Section 28 of the Securities Act gives the Commission the authority to, conditionally or unconditionally, "exempt any person, security, or transaction, or any class of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation issued under this title, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors."[49] The Commission, therefore, has wide discretion to create exemptions from the registration requirements of the Securities Act.

[42] 17 C.F.R. § 230.506. Rule 506 actually says that there may be no more than 35 purchasers for an offering to qualify under this section. *See* 17 C.F.R. § 230.506(2)(i). However, in order to calculate the number of purchasers of securities, one must refer to Rule 501 (e), which exempts accredited investors from the total number of purchasers when calculating that number for purpose of exemptions under Rules 505(b) and 506(b). 17 C.F.R. § 230.501(e).

[43] 17 C.F.R. § 230.506 (b)(2)(ii).

[44] 17 C.F.R. § 230.502(b).

[45] 15 U.S.C. § 77d(6).

[46] 17 C.F.R. § 230.144A.

[47] 17 C.F.R. § 230.144A(a).

[48] *See* Final Rule in Regulation AB, *supra* note 2.

[49] 15 U.S.C § 77z-3.

Private Rights of Action Under the Securities Act

Sections 11 and 12 of the Securities Act provide private causes of actions for material misstatements or omissions contained in the registration of private label MBS securities.[50] Section 15 of the act creates liability for controlling persons. These causes of action are described in this section.

Section 11 Civil Liability for a False Registration Statement

Section 11 creates a private right of action for purchasers of securities issued pursuant to a false or materially misleading registration statement.[51] To establish liability, a plaintiff must show that the registration statement, at the time it became effective, contained a material misstatement or omission.[52] A statement is material if "an average prudent investor ought reasonably to be informed [of the information] before purchasing the security registered."[53] For the purposes of Section 11, a statement is material if, had it been stated correctly or disclosed, it "would have deterred or tended to deter the average prudent investor from purchasing the securities in question."[54] Because Section 11 requires an effective registration statement in order to apply, securities that are sold pursuant to an exemption from registration are not subject to liability for violations of Section 11.[55]

Liability for violations may include

- the difference between the amount paid for the security and the value at the time the suit is brought, or
- the difference between the amount paid for the security and the price at which the security was sold in the market before the suit, or
- the difference between the amount paid for the security and the price at which it was sold after suit, but before judgment is entered, if that amount is less than the damages representing the difference between the amount paid for the security and the value at the time the suit was brought.[56]

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[50] It is important to note that these causes of action apply only to public offerings (Section 12) and offerings made pursuant to an effective registration statement (Section 11). They do not apply to many offerings that are exempted from registration requirements. As a result, in order to recover for fraud and other deceptive practices related to the sale of exempted securities, investors likely would need to allege violations of Section 10b of the Exchange Act and Rule 10b-5 (15 U.S.C. §78j; 17 C.F.R. § 10b-5).

[51] 15 U.S.C. § 77k.

[52] *Id.* Unlike claims for violations of Rule 10b-5 under the Exchange Act, plaintiffs do not need to allege or prove scienter (i.e., knowledge on the part of the defendant) for violations of Section 11 of the Securities Act. *See* Alaska Elec. Pension Fund v. Pharmacia Corp., 554 F.3d 342, 348 n.4 (3d. Cir. 2009); J&R Mktg. v. GMC, 549 F.3d 384, 392 (6th Cir. 2008). Because claims for violations of Section 11 "sound in fraud," plaintiffs must comply with Rule 9(b) of the Federal Rules of Civil Procedure. Rule 9(b) requires a plaintiff to "state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally." Fed. R. Civ. Pro. 9(b).

[53] Rule 405 under the Securities Act, 17 C.F.R. § 230.405.

[54] Escott v. BarChris Constr Corp., 283 F. Supp. 643, 681 (S.D.N.Y. 1968).

[55] 15 U.S.C. § 77k.

[56] 15 U.S.C. § 77k(a).

MBS Suits

A number of lawsuits have been filed by investors against issuers of MBSs alleging violations of Section 11 of the Securities Act. Alleged violations include failure to comply with the underwriting standards described in the offering documents, failure to disclose true risks of default on loans, and misrepresentations that the assets backed by the securities were, in fact, "investment grade."[57] As these cases move through the courts, issues facing the causes of action will become more clear.

Defenses

A claim of liability under Section 11 may always be defeated by proof that the purchaser knew of the untruth or omission at the time the security was acquired.[58] Furthermore, if a defendant can prove that "any portion or all [of the damages suffered by the plaintiff] represents other than the depreciation in value of such security resulting from" the misstatement in the registration statement, that portion of the damages is not recoverable.[59] In other words, if a defendant can show that it was not the misstatement or omission in the registration statement that caused the value of the shares to fall, but some other market force, the plaintiff cannot recover the loss of value represented by the extraneous influence.

The issuer has absolute liability under Section 11.[60] Section 11 allows other individuals, besides the issuer, to be sued for violations, including corporate executives and others who signed the registration statement.[61] These defendants may assert the "due diligence" defense.[62] For the purposes of this defense, there are two portions of a registration statement: the "expert" portions and the "unexpert" portions. For example, in MBS offerings, the portion describing the pooling and servicing agreement for the underlying asset pool is prepared and signed by experts in accounting and auditing.[63]

Defendants, other than the expert that prepared the "expert" section at issue, may assert a due diligence defense to the preparation of the expert portions if the defendants can show that, after a reasonable investigation, they "had no reasonable grounds to believe and did not believe" there to be any material misstatements or omissions in the expert portion of the registration statement.[64] "Reasonable investigation" means that which is required of a reasonable man in the care of his

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[57] *See*, Public Employees Retirement System of Mississippi v. Goldman Sachs Group, Inc., Case No. 09-CV-1110 (S.D.N.Y. February, 2009); Public Employees Retirement System of Mississippi v. Morgan Stanley, Case No. _____ (Cal. Sup. Ct. December, 2008); Boilermaker-Blacksmith National Pension Trust v. Wells Fargo Mortgage-Backed Securities 2006-AR1 Trust, Case No. 09-CV-833 (S.D.N.Y. January, 2009); Boilermaker-Blacksmith National Pension Trust v. WAMU Mortgage Pass Through Certificates, Series 2006-AR1, Case No. C-09-0037 (W.D. WA January, 2009).

[58] 15 U.S.C. § 77k(a).

[59] 15 U.S.C. § 77k(e).

[60] 15 U.S.C. § 77k(b).

[61] 15 U.S.C. § 77k(a). These persons or entities are principal executive officers, principal financial officers, controllers or principal accounting officers, directors, persons that are about to become directors, those who prepared and signed the expert portions of the registration statement, and underwriters.

[62] *See* 15 U.S.C. § 77k(b)(3).

[63] *See, e.g.*, Form S-3, Sun Real Estate Trust (August 29, 2007), available at http://www.sec.gov/Archives/edgar/data/1407749/000137468007000006/forms3.txt.

[64] 15 U.S.C. § 77k(b)(3)(A).

own property.[65] In other words, those who sign the registration statement are entitled to trust the experts paid to prepare the expert portions, absent any red flags.[66]

With respect to the unexpert portions (and to the expert portions for the expert charged with preparing and signing those portions), defendants may assert the due diligence defense if they can show that, after a reasonable investigation the defendants had reasonable grounds to believe and did believe that there was no material misstatement or omission.[67] This is a higher standard than the standard described in the preceding paragraph.[68] Those signing the registration statement are not entitled to assume all information in it is correct because they trust those who prepared the statement. The defendants must, at the least, have read the registration statement and taken into account all knowledge available to them to gauge the statements accuracy.[69]

Section 12 Civil Liability Arising in Connection with Prospectuses and Communications

Section 12 applies to two different scenarios, each of which may apply to the issuance of private label MBSs. Both are briefly described below.

Section 12(a)(1)

Under Section 12(a)(1), a seller[70] is strictly liable for selling securities in violation of Section 5. To establish a claim under this subsection, a plaintiff need only show that he bought securities and that the securities were not registered.[71] The burden is on the defendant to show that there was an exemption for the offering.

Section 12(a)(2)

Section 12(a)(2) creates liability for any person who sells securities pursuant to a prospectus or oral communication that contains a material misstatement or omission.[72] Liability under this section is not strict liability, however. A defendant who can prove that "he did not know, and in the exercise of reasonable care could not have known of such untruth or omission" will not be held liable.[73] A defendant may reduce his liability under 12(a)(2) to the extent that he can show the decrease in the securities' value was caused by factors other than the alleged misstatement or omission in the prospectus or oral communication.[74] Furthermore, this section only applies to

[65] 15 U.S.C. § 77k(c).

[66] *BarChris Constr Corp.*, 283 F. Supp. at 687.

[67] 15 U.S.C. § 77k(b)(3)(B)-(C).

[68] *See BarChris Constr Corp.*, 283 F. Supp. at 688.

[69] *Id.*

[70] More persons than the issuer may be included in the definition of "seller." "Sellers" may include individuals such as solicitors and others who may be financially motivated to sell a security. *See* Pinter v. Dahl, 486 U.S. 622 (1988).

[71] 15 U.S.C. § 77*l*(a)(1).

[72] 15 U.S.C. § 77*l*(a)(2).

[73] *Id.*

[74] 15 U.S.C. § 77*l*(b).

public offerings; private placements, such as those accomplished under Rules 506, are not covered.[75]

MBS Suits

Many of the suits filed alleging violations of Section 11 in the registration and sale of MBSs, also allege violations of Section 12(a)(2).[76] As these cases move through the courts, issues facing the causes of action will become more clear.

Section 15 Liability of Controlling Persons

Section 15 makes those persons or entities that, through stock ownership or other arrangement, control the persons or entities that are liable under Sections 11 and 12 jointly and severably liable for violations of those sections. [77] This provision could become important for the purposes of private label MBS liability. Issuers of MBSs are typically specially created for the purposes of a specific offering.[78] Therefore, in order to recover for violations of Section 11 and 12 in MBS offerings, it may be necessary to sue the persons controlling the entities making the offering.

SEC Enforcement of the Securities Act

The Commission has the statutory authority to bring an action for violation of the Securities Act, as well as any violation of the rules and regulations issued by the Commission pursuant to the act.[79] Whenever the Commission believes a person has violated or is about to violate the provisions of the Securities Act, the Commission has the power to issue a cease and desist order.[80] Pursuant to any cease and desist order, the Commission has the authority to order accounting and disgorgement.[81] The Commission may also bring civil or criminal actions for violations of the act.[82]

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[75] Gustafson v. Alloyd Co., 513 U.S. 561 (1995).

[76] *See*, Public Employees Retirement System of Mississippi, v. Goldman Sachs Group, Inc., Case No. 09-CV-1110 (S.D.N.Y. February, 2009); Public Employees Retirement System of Mississippi v. Morgan Stanley, Case No. _____ (Cal. Sup. Ct. December, 2008); Boilermaker-Blacksmith National Pension Trust v. Wells Fargo Mortgage-Backed Securities 2006-AR1 Trust, Case No. 09-CV-833 (S.D.N.Y. January, 2009); Boilermaker-Blacksmith National Pension Trust v. WAMU Mortgage Pass Through Certificates, Series 2006-AR1, Case No. C-09-0037 (W.D.WA January, 2009).

[77] 15 U.S.C § 77*o*.

[78] *See* Final Rule in Regulation AB, *supra* note 2, §III B. *See, e.g.*, Public Employees Retirement System of Mississippi, v. Goldman Sachs Group, Inc., Case No. 09-CV-1110 (S.D.N.Y. February, 2009); Public Employees Retirement System of Mississippi v. Morgan Stanley, Case No. _____ (Cal. Sup. Ct. December, 2008); Boilermaker-Blacksmith National Pension Trust v. Wells Fargo Mortgage-Backed Securities 2006-AR1 Trust, Case No. 09-CV-833 (S.D.N.Y. January, 2009); Boilermaker-Blacksmith National Pension Trust v. WAMU Mortgage Pass Through Certificates, Series 2006-AR1, Case No. C-09-0037 (WD.WA. January, 2009).

[79] Sections 19, 20(a) of the Securities Act, 15 U.S.C. §§77s, 77t.

[80] 15 U.S.C § 77h-1.

[81] *Id.*

[82] 15 U.S.C. §77t.

In conjunction with the enforcement described above, the Commission may bring an action for violation of Section 17 of the Securities Act. Section 17 is a general antifraud provision. It prohibits any individual, in the offer or sale of securities, from employing various means or devices of fraud.[83] Some courts have held that there is an implied private right of action under Section 17 (similar to that of Rule 10b-5 of the Exchange Act), but the Supreme Court has yet to rule on this question.[84]

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[83] 15 U.S.C. § 77q.

[84] Herman & Maclean v. Huddleston, 459 U.S. 375, 378 n. 2 (1983).

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