Regulatory Notice 21-40

November 11, 2021

Settlement of Syndicate Accounts

FINRA Requests Comment on Amendments to Rule 11880 Shortening the Settlement of Syndicate Accounts

Comment Period Expires: January 18, 2022

Summary

FINRA is soliciting comment on a proposal to amend FINRA Uniform Practice Code Rule 11880 (Settlement of Syndicate Accounts). The proposed amendments would reduce the maximum time for the final settlement of syndicate accounts in a public offering of corporate debt securities from 90 days to 30 days following the syndicate settlement date.

Questions concerning this *Notice* should be directed to:

- Paul Mathews, Vice President, Corporate Financing, at (240) 386-4639 or paul.mathews@finra.org;
- Kris Dailey, Vice President, Office of Financial and Operational Risk Policy, at (646) 315-8434 or kris.dailey@finra.org; or
- Cindy Friedlander, Senior Director, Fixed Income Regulation, at (202) 728-8133 or cynthia.friedlander@finra.org.

Questions concerning the Economic Impact Assessment in this *Notice* should be directed to:

- Dror Kenett, Senior Economist, Office of the Chief Economist, at (202) 728-8208 or dror.kenett@finra.org; or
- Vy Nguyen, Principal Research Analyst, Office of the Chief Economist at vy.nguyen@finra.org.

Action Requested

FINRA encourages all interested parties to comment on this request for comment. Comments must be received by January 18, 2022.

Notice Type

- Request for Comment

Suggested Routing

- Compliance
- Corporate Finance
- Legal
- Operations
- Senior Management
- Syndicate
- Underwriting

Key Topics

- Capital Raising
- Distribution of Securities
- Fixed Income
- Initial Public Offerings
- Investment Banking
- Public Offerings
- Underwriting

Referenced Rules & Notices

- FINRA Rule 11880
- MSRB Rule G-11
- Regulatory Notice 21-17
- SEA Rule 15c3-1

Comments must be submitted through one of the following methods:

- Online using FINRA's comment form for this *Notice*;
- Emailing comments to pubcom@finra.org; or
- Mailing comments in hard copy to:

  Jennifer Piorko Mitchell
  Office of the Corporate Secretary
  FINRA
  1735 K Street, NW
  Washington, DC 20006-1506

To help FINRA process comments more efficiently, persons should use only one method to comment.

Important Notes: Comments received in response to *Regulatory Notices* will be made available to the public on the FINRA website. In general, comments will be posted as they are received.[1]

Before becoming effective, a proposed rule change must be approved by the FINRA Board of Governors and filed with the Securities and Exchange Commission (SEC) pursuant to Section 19(b) of the Securities Exchange Act of 1934 (SEA).[2]

Summary

Background and Discussion

Rule 11880

To avoid lengthy settlement delays, since 1987 FINRA Rule 11880 has required the syndicate manager[3] of a selling syndicate[4] in a public offering of corporate securities to effect the final settlement of syndicate accounts within 90 days following the syndicate settlement date (the date that the issuer delivers corporate securities to or for the account of the syndicate members).[5] Underwriting groups ordinarily form syndicate accounts to process the income and expenses of the syndicate.

The syndicate manager is responsible for maintaining syndicate account records and must provide to each member of the selling syndicate an itemized statement of syndicate expenses no later than the date of the final settlement of the syndicate accounts. Syndicate managers aggregate and bill expenses related to the offering, including due diligence, legal, marketing and distribution costs. The payment that each syndicate member receives at final settlement is netted of these expenses. Syndicate members record the expected payments from the syndicate manager as "receivables" on their books and records, but may not receive the payments for up to 90 days, as the rule currently permits.

Net Capital Rule Impact

The 90-day period between the syndicate settlement date and the receipt of the final payment by a syndicate member has an impact on a syndicate member's net capital position and its ability to use the revenues it earned from its participation in the syndicate offering in its business operations.

Initially, capital charges for purposes of SEA Rule 15c3-1 (Net Capital Rule)[6] arise from the commitment to underwrite the securities of the issuer and are a percentage of the total amount of the issuance that the syndicate member has committed to purchase (referred to as open contractual commitment charges). The syndicate member takes these capital charges from the time the syndicate member is legally committed to the offering up until they have sold the securities (confirmed sales) to customers. A firm can participate in more offerings when it has more capital to sustain the open contractual commitment capital charges for such offerings.

However, a syndicate member may not treat syndicate receivables (*i.e.,* the profits the syndicate member earns from its participation in the offering that the syndicate manager has not remitted to the syndicate member) as allowable assets for the Net Capital Rule and therefore, must deduct them from its net worth in computing its net capital. As a result, while the revenue from the offering might otherwise increase a syndicate member's net capital when it records revenue earned from the syndicate, there is a corresponding deduction to net capital related to the receivable from the syndicate manager in its net capital computation, and the net effect is that its net capital remains unchanged. Hence, such syndicate members effectively are unable, in the interim, to use their earnings from the syndicate as additional net capital, to participate in new offerings, to offset expenses related to the syndicate offering or to otherwise operate their business.

Firms that are active underwriters in public offerings may have a significant amount of syndicate receivables and may be disproportionately negatively impacted by the inability to treat these receivables as allowable assets for purposes of SEA Rule 15c3-1. This may be of particular concern for smaller firms that may not be as highly capitalized as larger firms and thus may be more limited in their ability to participate in new offerings.[7]

Proposed Amendments

In light of the technological advancements since 1987 that improve the efficiency of the settlement process, FINRA is proposing amendments to Rule 11880(b) to reduce settlement delays that prolong a firm's exposure to the credit risk of the syndicate manager, among other potential benefits. Specifically, FINRA is proposing that, for a public offering of corporate debt securities, the syndicate manager must effect final settlement of syndicate accounts within 30 days following the syndicate settlement date. FINRA is requesting comment on whether 30 days is feasible for all types of corporate debt offerings or whether there are some that are more complex and would require a slightly longer timeframe, for example, an offering with an overallotment option.[8] FINRA also is requesting comment on shortening the settlement period for all other public offerings of corporate securities, including equity offerings.

FINRA notes that the Municipal Securities Rulemaking Board (MSRB) Rule G-11 (Primary Offering Practices) provides that final settlement of a syndicate or similar account for a municipal offering shall be made within 30 calendar days following the date the issuer delivers the securities to the syndicate. The MSRB shortened the settlement period from 60 days to 30 days in 2009, stating in the related rule filing that the amendments were designed to reduce the exposure of syndicate account members to the risk of potential deterioration in the credit of the syndicate manager during the pendency of account settlements.[9] The MSRB further stated that, since the rules were adopted in the 1970s, firms have adopted more efficient billing and accounting systems such that reductions in the time periods for distribution of syndicate account profits is feasible and not unduly burdensome to dealers.[10]

FINRA believes the principles the MSRB outlined with respect to final settlement of syndicate accounts for municipal offerings may apply equally with respect to final settlement of syndicate accounts for public offerings of corporate debt securities. The 90-day allowable timeframe for settling syndicate accounts impacts not only a firm's net capital—as syndicate receivables are not considered an "allowable asset" under SEA Rule 15c3-1(c)(2)(iv)(C)—but also exposes the firm to the credit risk of the syndicate manager. Since 1987, firms have implemented technology to broadly automate their back-office processes, and systems are available to similarly automate corporate debt syndicate settlement, as well as for municipal offerings. FINRA also notes that there are some differences between municipal and corporate debt syndicate practices. For example, in a municipal offering typically only the syndicate manager incurs expenses on behalf of the syndicate, and the legal expenses of the syndicate are a fixed amount known in advance. However, these differences do not appear to justify the current 60-day gap between corporate and municipal syndicate account settlement timeframes.

FINRA believes that public offerings of corporate debt securities are generally less complex than other public corporate offerings, such as an equity initial public offering. Therefore, at this time FINRA is proposing a 30-day syndicate settlement for corporate debt, while seeking comment on whether certain types of debt offerings may require a different settlement period. FINRA also seeks comment on shortening the time to settle syndicate accounts for all other corporate public offerings, including equity offerings.

Economic Impact Assessment

FINRA has analyzed the potential costs and benefits of the proposal, and the impacts on the different parties that are expected to be affected. FINRA believes that the proposal would generally benefit syndicate members that engage in public offerings of corporate debt securities. Additionally, by shortening the final settlement timeframe for syndicate accounts, the proposal could potentially reduce barriers to entry and facilitate competition in the corporate debt underwriting market.

Economic Baseline

The economic baseline for the proposed amendments is current Rule 11880, which allows 90 days for the final settlement of syndicate accounts, current industry practices for compliance and implementation of the rule, and the current competitive landscape.

FINRA has engaged with member firms, trade associations and FINRA advisory committees on the proposal. FINRA has also conducted an analysis of the primary corporate debt market to study the extent and scope of participation in corporate debt syndicates by member firms, using data from the Trade Reporting and Compliance Engine (TRACE), for the 2018 to 2020 period. FINRA estimates that approximately 393 member firms, annually, on average, participate in syndicates for corporate debt offerings and could be affected by the proposed amendments.[11] Of these firms, 25 percent, 18 percent, and 57 percent are large, mid-size and small firms, respectively.[12]

Table 1. Number of Firms Participating as Sellers in Corporate Debt Primary Market, by Firm Size, Years 2018-2020

	Number of firms	Percent of total firms
Annual Average 2018-2020	393	100%
Large (>= 500 Registered Representatives)	97	25%
Mid-Size (151-499 Registered Representatives)	71	18%
Small (1-150 Registered Representatives)	226	57%

Source: Derived from TRACE Data

The 90-day period following the syndicate settlement date allows the syndicate manager to record income and expenses incurred in connection with the offering and then distribute the net underwriting revenue due to each syndicate member. Syndicate managers tend to be large, well-capitalized firms.[13] Among other things, the syndicate manager collects the underwriting revenue for the syndicate and pays expenses. The other syndicate members, which are often smaller firms, are paid their share of the underwriting revenue, netted of expenses, from the syndicate managers by the final syndicate account settlement date.

In order to assess the magnitude of the gross revenue from underwriting public offerings of corporate debt, FINRA calculates that, on average, between 2018 and 2020, there were 30,803 U.S. dollar-denominated corporate debt offerings (excluding 144A offerings) with an average amount of $3.5 trillion raised per year (*see* Table 2). Investment grade corporate debt offerings account for 50 percent of the total issued amount, and high yield and non-rated corporate debt offerings account for the remainder (*see* Table 2).[14] A recent study shows that the average gross underwriting spread[15] is 0.65 percent for investment grade debt securities and 1.42 percent for high yield debt securities.[16] Using this spread data, FINRA estimates that the gross revenue from underwriting public offerings of corporate debt (excluding 144A offerings) would be somewhat greater than $36 billion per year.[17] A portion of the underwriting revenue, net of expenses, is distributed to other syndicate members.

Table 2. TRACE-Eligible Corporate Bonds Issued by Grade and Year (excluding 144A offerings)

	Number of Offerings	Total Issued Amount (trillion $)	Percent of annual total issued amounts
2018	**23,346**	**3.32**	**100.00%**
Investment Grade	3,063	1.60	48.17%
High Yield	574	0.29	8.63%
Non-rated	19,709	1.43	43.20%
2019	**26,272**	**3.00**	**100.00%**
Investment Grade	3,233	1.47	49.13%
High Yield	450	0.25	8.22%
Non-rated	22,589	1.28	42.65%
2020	**42,792**	**4.08**	**100.00%**
Investment Grade	3,741	2.09	51.31%
High Yield	355	0.22	5.44%
Non-rated	38,696	1.77	43.24%
Average 2018-2020	**30,803**	**3.47**	**100.00%**
Investment Grade	3,346	1.72	49.54%
High Yield	460	0.25	7.43%
Non-rated	26,998	1.49	43.03%

Source: Bloomberg for TRACE-eligible Corporate Bonds

Through its outreach efforts, FINRA understands there may be substantial differences between public offerings of debt and equity securities with respect to the settlement of syndicate accounts. Generally, the issuance process for debt is simpler than that of other types of securities, such as equity or certain preferred equity. FINRA understands that, in many instances, the income for a corporate debt offering is known by the closing date of the offering. Wang (2020) found that, in more than 95 percent of the debt offerings from 2016 to 2018, the debt security is priced, allocated to investors and starts trading in the secondary market all within the same day.[18] Thus, a large part of syndicate income for corporate debt offerings could be accounted for within days after the date of issuance.[19]

Unlike equity offerings, which FINRA understands can take more time to price, based on feedback from institutional investors, the bond issuer and the syndicate manager typically negotiate and agree on a price range, issue amount and spreads on or before the date of issuance.

FINRA understands that expenses related to an offering of corporate debt securities can be ascertained sooner than 90 days from the close of the debt offering. However, FINRA has heard anecdotally that the settlement of syndicate accounts is typically conducted at the end of the 90-day window, rather than earlier in the window, as permitted under the current rule. FINRA understands that the current industry practice of settling syndicate accounts at the end of the 90-day period, and not sooner, presents challenges for some syndicate members, but may benefit others.

Economic Impacts

The proposed amendments could potentially impact firms of different sizes that participate in corporate debt offerings in different ways. The aggregate impact is less clear, as it depends upon the extent of long-term competitive benefits and short-term cost increases.

Anticipated Benefits

A primary benefit of the proposal, particularly for smaller firms, is that syndicate receivables would become available to syndicate members sooner. Because syndicate receivables are not treated as allowable assets under SEA Rule 15c3-1, a shorter syndicate account settlement timeframe would provide syndicate members with earlier access to capital to participate in new offerings and compete with other firms, maintain business operations or use the funds for other purposes. Public information does not permit FINRA to assess directly the proportion of receivables associated with smaller firms, although, as noted above, syndicate management appears to be concentrated in a small number of large firms.[20] Through its outreach efforts, however, as well as comments received in response to FINRA *Regulatory Notice 21-17*, FINRA believes that such potential benefits would be more pronounced for small firms with lower capital levels.[21]

The proposed amendments could lower barriers to enter the corporate debt underwriting market and thereby increase the supply of underwriters. This could ultimately result in lower costs for corporate debt issuers and investors. Lowering costs to issuers and investors may increase the size and frequency of new corporate debt offerings, benefiting all member firms engaged in the underwriting process. The extent of this potential gain in market competitiveness cannot be fully and accurately estimated.

Shortening the syndicate account settlement period could lead to a transfer of some of the interest earned on the syndicate's underwriting revenue—*i.e.,* from the syndicate manager to other syndicate members—because the syndicate manager would be required to remit payment to the syndicate members sooner.[22] Under the proposed amendments, if the underwriting revenue is paid earlier, the syndicate manager would forego the earned interest on the amount to be distributed to syndicate members over the 60-day period—the difference between the 90-day baseline and proposed 30-day settlement time frame. Other syndicate members, likely smaller firms, would have the opportunity to earn that interest. Additionally, the shorter syndicate account settlement period would mitigate the counterparty risks for syndicate members that expect to receive a payment from the syndicate manager.

Finally, FINRA believes the proposal would provide some benefits to joint members with respect to potential regulatory alignment with the MSRB. FINRA understands that, while differences exist between municipal bonds and corporate debt instruments and their offering processes, potentially aligning the syndicate account settlement period in Rule 11880 with that in MSRB Rule G-11, where appropriate, could ultimately reduce compliance and supervisory program costs associated with different compliance regimes.

Anticipated Costs

FINRA believes the proposal could result in some direct costs to member firms, particularly those that serve as syndicate managers in public offerings of corporate debt. These firms could experience increased costs to adapt their accounting, compliance, supervision and management systems, and may need to hire additional staff to accommodate a shorter syndicate account settlement cycle. Firms may adopt better technology and greater automation of accounting and recordkeeping processes to settle syndicate accounts more quickly. FINRA understands that firms may also incur increased legal or other fees due to the demands of an accelerated timeframe. FINRA also understands that the magnitude of such associated costs, specifically staff and related human and technology resources, could increase with the volume and frequency of offerings in which firms participate as syndicate managers. Syndicate managers could absorb such costs or pass them on to the syndicate members or the issuers.

Through its firm engagement efforts, FINRA understands that, under the current system, syndicate managers may receive late invoices after the final settlement of syndicate accounts. FINRA understands that syndicate managers prefer to avoid this scenario as much as possible and indicated that collecting invoices and expenses in a shortened time-period may be challenging. FINRA cannot currently estimate whether or how much syndicate manager costs would increase if the syndicate account settlement timeframe was reduced.

Request for Comment

FINRA requests comment on all aspects of the proposal. FINRA requests that commenters provide empirical data or other factual support for their comments whenever possible. FINRA specifically requests comments concerning the following issues:

1. In addition to the economic impacts identified in this proposal:
   a. Are there other significant sources of impacts, including direct or indirect costs and benefits, of the proposed amendments to firms, issuers and investors?
   b. What are these economic impacts and what factors contribute to them?
   c. What would be the magnitude of these costs and benefits?
   d. Would such economic impacts differ across firm size or business model?

   Please provide data or other supporting evidence.

2. FINRA could consider defining a "corporate debt security" as a type of "TRACE-Eligible Security" that is United States ("U.S.") dollar-denominated and issued by a U.S. or foreign private issuer. Is this the appropriate definition of "corporate debt security" for purposes of this proposal? Why or why not? Should the definition exclude a "Securitized Product," as defined in Rule 6710(m)? Please explain.
3. What are the various syndicate manager activities, processes and related timing that must precede the final settlement of syndicate accounts? Are there specific procedures or other measures used to address unresolved or uncertain expenses? How do these activities, processes and related timing considerations differ between various types of corporate public offerings?
4. FINRA is proposing to shorten the syndicate account settlement cycle for public offerings of corporate debt securities from 90 days to 30 days. Is 30 days the most appropriate shortened timeframe? Is a shorter timeframe feasible?
5. Are there certain types of offering costs that a syndicate manager may be unable to itemize within 30 days? For example, are fees for legal services always determined within 30 days of the syndicate settlement date? If not, when are such fees finalized? Could legal fees increase where the syndicate manager is required to settle syndicate accounts in a shorter period of time?
6. Are there some types of corporate debt offerings that could not settle in 30 days? If so, what are the specific types of corporate debt offerings and the reasons 30 days is not feasible? For example, is the feasibility of a 30-day settlement impacted by the type of corporate debt security, whether the security is investment grade or non-investment grade; the number of tranches in the offering; or other factors? Please specify.

7. As stated above, the MSRB shortened the syndicate account settlement period for municipal offerings from 60 days to 30 days in 2009. Are there differences between municipal and corporate debt security offerings that justify a longer syndicate account settlement timeframe for corporates? For example, to what degree are corporate debt security offerings more or less complex or time-consuming from a syndicate account settlement perspective and how do these differences impact the time needed to settle syndicate accounts? Are there circumstances in which it is not possible to completely settle all expenses of the syndicate in a municipal offering within 30 days, and if so, how is that handled?
8. How do the billing and payment processes for public offerings of corporate debt securities that involve international participants affect the timeframe for settlement of syndicate accounts for corporate offerings?
9. What technology has emerged that can support syndicate managers in syndicate account settlement billing and payment for corporate debt securities?
10. What systems, process or other changes must firms make to implement the proposed amendments? Will these changes affect the costs of the capital raising process for corporate debt securities?
11. Should the period permitted for the final settlement of syndicate accounts for public offerings of corporate equity securities be shortened? If so, what time frame is feasible? What impact, if any, would the exercise period for overallotment options have on shortening the period for final settlement of syndicate accounts for equity offerings?
12. FINRA understands that overallotment options are less commonly used in public offerings of debt securities because they could increase the issued amount, making it difficult to assess the debt rating and negotiate the offering price.[23] Please provide comment on the frequency of use of overallotment options in connection with corporate debt offerings and what impact, if any, the exercise period for overallotment options would have on shortening the period for final settlement of syndicate accounts.
13. An SEC staff interpretation under the Net Capital Rules provides that syndicate receivables may be considered an allowable asset to the extent a creditor issues a sole recourse loan to the syndicate member secured by the syndicate receivable.[24] Is adopting this approach feasible? What are the impacts of adopting this approach?
14. Are there additional approaches that FINRA should consider to accomplish the goals of this proposal? For example, what are commenters' views on a two-stage syndicate account settlement approach—whereby the syndicate manager must remit a percentage of the gross underwriting spread from the offering within 30 days of the syndicate settlement date, with the balance due to syndicate members on a later date between 30 days and 90 days of the syndicate settlement date? If FINRA takes such an approach, what percentage should be required to be paid by the syndicate manager within the first 30 days? Please describe any other alternatives that FINRA should consider and why they are better suited?

15. Are there any potential risks to member firms, the investor community or others, associated with the existing 90-day settlement period? Could such risks decrease or increase by shortening the settlement period?
16. Will shortening the period for the final settlement of syndicate accounts lead to an increase or decrease in member firm participation in syndicate debt offerings?

Endnotes

1. Parties should submit in their comments only personally identifiable information, such as phone numbers and addresses, that they wish to make available publicly. FINRA, however, reserves the right to redact or edit personally identifiable information from comment submissions. FINRA also reserves the right to redact, remove or decline to post comments that are inappropriate for publication, such as vulgar, abusive or potentially fraudulent comment letters.

2. *See* SEA Section 19 and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the *Federal Register*. Certain limited types of proposed rule changes take effect upon filing with the SEC. *See* SEA Section 19(b)(3) and SEA Rule 19b-4.

3. Rule 11880(a)(2) defines "syndicate manager" as "the member of the selling syndicate that is responsible for maintenance of the syndicate account records." A "syndicate account" is defined in Rule 11880(a)(3) as "the account formed by members of the selling syndicate for the purpose of purchasing and distributing the corporate securities of a public offering."

4. A "selling syndicate" is defined in Rule 11880(a)(1) as "any syndicate formed in connection with a public offering to distribute all or part of an issue of corporate securities by sales made directly to the public by or through participants in such syndicate."

5. *See* Securities Exchange Act Release No. 22238 (July 15, 1985), 50 FR 29503 (July 19, 1985) (Approval Order of SR-NASD-85-14). Initially the rule required that final settlement of syndicate accounts be closed out within 120 days after the syndicate settlement date. The time was reduced to 90 days in 1987. *See* Securities Exchange Act Release No. 24290 (April 1, 1987), 52 FR 11148 (April 7, 1987) (Approval order of SR-NASD-87-7).

6. *See* SEA Rule 15c3-1(c)(2)(iv)(C), which provides that syndicate receivables are not an allowable asset, except that receivables due to municipal securities underwriting syndicates are allowable for 60 days from the settlement of the underwriting with the issuer. An SEC staff interpretation provides that syndicate profit receivables must be deducted unless the asset: (1) adequately secures (*see* definition at SEA Rule 15c3-1(c)(5)) a fixed liability and are the sole recourse of the creditor for nonpayment of the liability, and (2) the loan agreement has been submitted to and found acceptable by the Exchange. (SEC Staff to NYSE) (No. 88-14, August 1988). *See* Interpretations of Financial and Operational Rules, SEA Rule 15c3-1(c)(2)(iv)(E)/011 Syndicate Receivables.

7. FINRA recently solicited comment on supporting diversity and inclusion in the broker-dealer industry in *Regulatory Notice 21-17*. FINRA received a comment indicating that the combined effect of Rule 11880 and the Net Capital Rule hurts minority-, women-, and veteran-owned broker-dealers (MWVBDs) because they frequently serve as co-managers and, thus, often have significant syndicate receivables that are not allowable as good capital. *See* letter from Kenneth E. Bentsen, Jr., SIFMA President and CEO to Jennifer Piorko Mitchell, FINRA (June 28, 2021).

   In addition, working with the Bond Dealers of America (BDA), a coalition of MWVBDs have raised concerns regarding the impact of Rule 11880 and the Net Capital Rule on MWVBDs to the SEC Chair, Gary Gensler. *See* letter from Chance Mims, Academy Securities, Inc. Founder and CEO; David R. Jones, CastleOak Securities, L.P. President and CEO; Juan D. Espinosa, Apto Partners, LLC Founder and CEO; Candace King Weir, C.L. King & Associates Inc. President; Eric V. Standifer, Blaylock Van, LLC President and CEO; Anthony Felice, Drexel

Hamilton, LLC CEO; Martin Cabrera, Cabrera Capital Markets, LLC Founder and CEO; James Reynolds, Jr., Loop Capital Markets LLC Chairman and CEO; George Ramirez, MFR Securities, Inc. CEO; Christopher J. Williams, Siebert Williams Shank and Co., LLC Chairman; George Madrigal, Penserra Securities LLC Founder and CEO; Pepe Finn, Stern Brokers & Co. Chairperson and CEO; Annie Seelaus, R. Seelaus & Co., Inc. CEO; Cynthia DiBartolo, Esq., Tigress Financial Partners LLC Founder and CEO; Samuel A. Ramirez, Samuel A. Ramirez & Company, Inc. President and CEO; Cynthia DiBartolo & Alexis Thomas, Diversity Broker-Dealer Coalition Chairperson and Vice Chairperson to Gary Gensler, SEC (May 1, 2021), available here on the BDA's website.

8. Overallotment options typically have an exercise term of 30 days and may have legal and other expenses associated with their exercise and subsequent closing. Such options are typically granted in listed offerings and permit the syndicate to purchase additional securities from the issuer at the public offering price to cover overallotments incurred during the distribution.

9. *See* Securities Exchange Act Release No. 60487 (August 12, 2009), 74 FR 41771 (August 18, 2009) (Notice of filing of SR-MSRB-2009-12) at 41771 and Securities Exchange Act Release No. 60725 (September 28, 2009), 74 FR 50855 (October 1, 2009) (Order approving SR-MSRB-2009-12).

10. *See id*. In addition, the MSRB noted that many fees are agreed upon in advance or can be estimated with considerable accuracy soon after settlement.

11. The extent of firm participation in primary corporate debt market was approximated using TRACE data. The primary market is where issuers sell new stocks and bonds to the public for the first time, such as with an initial public offering (IPO). The data displayed here is limited to the primary market sellers for corporate debt offerings.

12. For definitions of firm sizes, *see* Table 1; *see also* FINRA 2021 Industry Snapshot.

13. For example, *see* Hendrik Bessembinder, Stacey E. Jacobsen, William F. Maxwell and Kumar Venkataraman, "Syndicate Structure, Overallocation, and Secondary Market Outcomes in Corporate Bond Offerings" (May 18, 2021). SMU Cox School of Business Research Paper No. 20-04. The authors developed a sample of 5,573 bond offerings that were issued between 2010 and 2018, based upon primary allocation data FINRA collected through TRACE. They found that only 10 firms were syndicate managers and that the most frequent bookrunners (manager and co-managers) were large firms. This finding is consistent with FINRA's findings from its outreach efforts.

14. While members are required to report revenue from underwriting on Financial and Operational Combined Uniform Single (FOCUS) and Supplemental Statement of Income (SSOI) reports, the data is in aggregate form and thus FINRA is unable to determine underwriting revenue for public offerings of corporate debt securities.

15. The gross revenue from an underwriting is the difference between the price the syndicate pays the issuer for the securities and the initial price at which the syndicate sells them to the public. This is also called the "gross underwriting spread." The spread generally accounts for management fees paid to lead underwriters, underwriting fees and the sales credits paid to syndicate members for selling the securities. As a rule, gross revenue from a public offering is directly related to the size of the offering.

16. *See supra* note 13.

17. For a sample of municipal bond offerings between 1997 and 2001, Butler (2008) found that the absence of a rating increases underwriting gross spreads by about 40 basis points after controlling for bond rating and other characteristics. *See* Alexander W. Butler, 2008. "Distance Still Matters: Evidence from Municipal Bond Underwriting." The Review of Financial Studies 763-784.

    Information on gross spreads for unrated corporate bonds is harder to find. Altman, Bharath and Saunders (2002) found the default rate among unrated institutional loans issued by US publicly owned companies was comparable to that of rated high yield loans. *See* Edward I. Altman, Sreedhar T. Bharath and Anthony Saunders, 2002. "Credit ratings and the BIS capital." Journal of Banking & Finance 909–921. These findings indicate that that the gross spread for unrated corporate bonds is likely somewhat greater than that for high yield corporate bonds.

    Based on these assumptions, the gross underwriting revenue from public offerings of corporate debt would be somewhat greater than $36B (= 0.0065 * 1.72*10^12 + 0.0142 *(0.25 + 1.49)*10^12).

18. *See* L. Wang, Lifting the veil: The price formation of corporate bond offerings, Journal of Financial Economics.

19. FINRA understands that, in the absence of an overallotment option, syndicate managers may over-allocate an offering to stabilize secondary market prices—effectively creating a syndicate short position. Profits or losses from these transactions are considered part of syndicate's revenues or expenses and depend on secondary market price movements, which cannot be estimated before the public offering. Research has found, however, that average profit/loss from covering overallocations relative to corporate debt underwriting revenue is very small, and most of the overallocations are offset within a few days of the date of issuance. Bessembinder et. al. (2021) found that over 70 percent of the issues with overallocations in their sample are offset within two days after issuance (*see supra* note 13). By day 15, about 80 percent of the issues have the overallocation fully (100 percent) offset. According to the authors, the mean net position for covering overallotment short-transactions and round-trip trades in the secondary market ranges from a $240,967 loss per high yield issue with a large overallocation to a $161,578 gain per high yield issue with a non-large overallocation.

20. *See supra* note 13.

21. *See supra* note 7.

22. The magnitude of such benefit is conditional on the existing interest rate environment. In low interest rate environments, such benefit is expected to be small.

23. *See supra* note 19.

24. *See supra* note 6.