

January 18, 2022

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

Transmitted electronically

Comments on FINRA Regulatory Notice 21-40

Dear Ms. Mitchell,

The Bond Dealers of America (BDA) is pleased to comment on FINRA Regulatory Notice 21-40, “FINRA Requests Comment on Amendments to Rule 11880 Shortening the Settlement of Syndicate Accounts” (the “Notice”). BDA is the only DC-based organization exclusively representing the interests of securities dealers and banks focused on the US fixed income markets. This letter represents the views not only of BDA’s member firms but also a coalition of minority-, women-, and veteran-owned broker-dealers with whom we are working on this issue.

Rule 11880 regulates the activity of syndicate managers<sup>1</sup> closing syndicate accounts, distributing revenue from transactions to comanagers, and related activities. The Rule currently requires senior managers, or bookrunners, to close syndicate accounts within 90 days of the transaction closing. The 90-day deadline has been the FINRA standard governing this activity since 1987. In the last 35 years there have been enormous strides in messaging and payment technologies that have increased the speed and lowered the cost at which syndicate invoices can be received and paid. In that time the Municipal Securities Rulemaking Board amended its Rule G-11 to shorten the time for syndicate settlement on municipal securities underwritings to 30 days, and revenue derived from customer designations must be paid within 10 days, changes adopted with no ill effects. Yet the FINRA Rule maintains the 90-day deadline. It is appropriate for FINRA to examine shortening this timeframe.

As the Notice recognizes, the 90-day deadline in Rule 11880 affects comanagers’ regulatory capital calculation under Securities Exchange Act Rule 15c3-1, the Net Capital Rule. As long as comanagers’ funds are tied up at the bookrunner, the comanager not only loses the use of those funds, but it also cannot count that receivable asset as regulatory capital until it is received in cash. BDA supports FINRA’s proposal in the Notice to shorten the syndicate closing deadline and we urge you to adopt the proposal as soon as practicable. Issues raised about the Notice are addressed herein.

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<sup>1</sup> The terms “syndicate manager,” “lead manager,” “senior manager” and “bookrunner” are used interchangeably in this letter.

### ***Economic costs and benefits***

The two principal economic benefits that would accrue to comanagers from the Notice's proposed amendments are the ability to count funds earned in an underwriting transaction as regulatory capital and the ability to earn float on or otherwise gain use of their funds within 30 days after deal closing. Currently, for the 90 days after deal closing, bookrunners earn the float on comanagers' funds. More capital for regional and mid-size firms means more capacity to underwrite new issues and provide liquidity to customers in the secondary market.

We also agree with the Notice that the proposed change to Rule 11880 would significantly "lower barriers to enter the corporate debt underwriting market and thereby increase the supply of underwriters." This is especially true for minority-, women-, and veteran-owned broker dealers (MWVBDs) because after years of education and advocacy, corporate bond issuers are beginning to recognize the value of diversity in their underwriting syndicates and are increasingly inviting MWVBDs into syndicates that were previously closed to new entrants. The ability of MWVBDs to accept these invitations depends to a significant degree on their access to capital. The faster that bookrunners pay out deal revenue to comanagers, thereby adding to their capital, the greater the ability of MWVBDs to participate in more underwritings.

The Notice's proposed 30-day deadline for closing syndicate accounts would also provide the benefit of significantly reducing counterparty risk exposure. A receivable owed by a bookrunner represents a default risk for comanagers in the event that the bookrunner becomes insolvent before paying comanagers. While this risk is small, it is not zero, and the longer the comanager is exposed to the bookrunner, the greater the risk. Reducing the syndicate closing deadline to 30 days would mitigate this exposure.

### ***Definition of corporate debt security***

We agree with the definition of "corporate debt security" in the Notice as "a type of 'TRACE-Eligible Security' that is United States dollar-denominated and issued by a U.S. or foreign private issuer." We believe this definition generally captures the universe of corporate bonds—investment grade and high yield—for which a move to a 30-day syndicate closing deadline would be easily achievable. We do not believe the definition should exclude securitized products as defined in Rule 6710(m). The process for managing the syndicate account, paying vendors, and releasing deal revenue to comanagers is virtually the same for both corporate bonds and securitized products.

### ***Steps necessary to close syndicate accounts***

As the Notice states, the time allotted to settle syndicate accounts in Rule 11880 is designed to allow bookrunners to "aggregate and bill expenses related to the offering, including due diligence, legal, marketing and distribution costs." In our members' experience when serving as bookrunners, law firms and other vendors are not shy about sending out timely invoices, especially if they are prompted by regulatory deadline. Moreover, many of the services provided to the syndicate by law firms and other vendors are based on pre-negotiated, fixed fees, not variable hourly charges, making billing and payments within 30 days even easier. The steps and processes associated with settling syndicate expenses do not vary widely among types of corporate bond offerings, even transactions which are offered to investors outside the US.

### ***Appropriate deadline for the Rule***

The Notice proposes to amend Rule 11880 to reduce the time to settle syndicate accounts from 90 to 30 days. We believe 30 days is an appropriate standard. A 30-day deadline would give bookrunners sufficient time to collect and pay syndicate invoices, perform syndicate accounting tasks, and pay out revenue to comanagers. It is the standard established in MSRB Rule G-11, and bookrunners on municipal securities transactions have settled syndicate accounts within 30 days since 2009 without issue. Indeed, revenue derived from designated customer orders is paid to comanagers within 10 days of the sale under MSRB Rule G-11(g)(iv).

When the MSRB was considering shortening their deadline for syndicate closings in 2009, large broker-dealers argued that 30 days was insufficient time to settle all syndicate expenses. “All the syndicate’s expenses may not be final within 30 calendar days after the issuer delivers the securities to the syndicate,” stated SIFMA’s comment letter at the time.<sup>2</sup> “Final bills from underwriters’ counsel may take many weeks to arrive, and the receipt of such bills are out of the direct control of the senior manager,” SIFMA argued. We expect FINRA will hear similar arguments from large broker-dealers in reaction to the Notice. We point out, however, that despite the concerns of large underwriters in 2009, the 30-day deadline for closing syndicate accounts and the 10-day deadline for paying the proceeds of designated orders were implemented without problem by bookrunners after the MSRB’s 2009 amendments took effect. The same will be true for the amendments in the Notice.

### ***Expenses outside the 30-day window***

It is a rare occurrence for syndicate expenses to be incurred outside the 30-day deadline proposed in the Notice. It can happen, however. Indeed, even under current rules, syndicate invoices can, on rare occasions, appear outside the 90-day window. Standard practice in those cases is for the bookrunner to bill comanagers for their share of the late-arriving expenses. Given that late expenses are such a rarity, current practice is not disruptive whatsoever. Under the Notice, if the bookrunner receives an invoice for expenses outside the proposed 30-day deadline, they will simply bill the syndicate. In underwritings of new equity issues, late syndicate expenses related to stability pricing and hedging may be more common. However, those expenses generally do not apply to debt transactions.

### ***Financings where a 30-day deadline may not be possible***

There are no categories of corporate bonds of US issuers offered for sale to US investors where it is not possible to collect and pay syndicate expenses within 30 days. The process for processing syndicate expenses and closing syndicate accounts is the same no matter the size of the issue, the credit rating of the issuer, the identities of the buyers, or any other variable. As discussed above, rare occasions may arise where expenses arrive late for a single transaction, but not on a categorical basis.

FINRA may hear the argument that new issues of US bonds marketed to international investors require more time to settle. In our experience, however, invoices from law firms and other vendors in Europe tend to arrive even faster than from vendors in the US. Moreover, taxable securities sold to international investors have become much more prevalent in the municipal market in recent years, and

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<sup>2</sup> Letter from Leslie M. Norwood, SIFMA, to Margaret C. Henry, MSRB, June 29, 2009, [msrb.org/-/media/Files/RFC/2009/2009-20/SIFMAG11.ashx](http://msrb.org/-/media/Files/RFC/2009/2009-20/SIFMAG11.ashx).

international distribution has not affected the ability of municipal bookrunners to settle accounts according to MSRB requirements.

Traditionally, most municipal issuers sell bonds where the interest is exempt from federal income tax for most US investors, generally reducing an issuer's capital cost. Tax-exempt municipal bonds do not appeal to non-US investors because they have no need for the federal tax-exemption. In recent years, however, state and local governments have been increasingly selling taxable bonds in lieu of tax-exempts. Long-term taxable municipal issuance has gone from less than eight percent of new-issue volume in 2014 to over 30 percent in 2020.<sup>3</sup> Taxable municipal issues do appeal to global investors, and many taxable municipal transactions include international distribution. This does not, however, affect the ability of municipal bookrunners to close syndicate accounts within 30 days as MSRB Rule G-11 requires and would not affect the ability to close corporate syndicate accounts under the 30-day deadline proposed in the Notice.

### ***Differences between municipal and corporate transactions***

There are not substantial differences between syndicate management and accounting for municipal and corporate debt transactions that affect the ability of bookrunners to settle syndicate accounts within 30 days. There is nothing about the complexity of corporate bonds that would limit the ability of a bookrunner to collect and pay syndicate invoices within 30 days. The processes for processing and paying syndicate expenses are very similar in both markets. And as described previously, if the syndicate incurs expenses or receives invoices after the syndicate account closing deadline—currently 30 days for municipals and 90 days for corporates—the bookrunning manager simply bills comanagers for their shares of the expense. This happens from time to time in the municipal market, especially in competitive issuances, which are not used by corporate issuers.

Processing revenue and invoices for a municipal securities transaction is arguably more complicated than for a corporate transaction. Virtually all corporate syndicates distribute revenue among members on the basis of “group net,” meaning members share revenue based on predetermined allocations, not which firm generated which customer orders. While some municipal syndicates operate on a group net basis, most are based on a “net designated” approach to revenue sharing where individual syndicate members receive credit for the customer orders they generate. That means the lead manager must track orders on a firm by firm basis and pay out revenue based on each firm's orders. That step generally is not necessary in corporate underwritings.

Also, corporate underwritings almost never have unsold balances at the time the transaction closes, due in large part to the bullet maturity structure used by most corporate issuers. Municipal issuers tend to use serial maturities where a transaction is split among many tranches, each with different, sequential maturities. Because some maturities are often easier to sell than others, it is not unusual for a syndicate to be left with remaining balances of bonds, which must be addressed by the bookrunner at syndicate closing, another step generally not necessary in corporate syndicates.

### ***Technology that can facilitate faster syndicate closings***

There obviously have been a plethora of technologies that have emerged since 1987 which facilitate faster syndicate settlements. Instead of snail mail, physical checks, and faxes, we have email, electronic

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<sup>3</sup> The Bond Buyer, “A Decade of Municipal Bond Finance,” [www.bondbuyer.com/broker/bond-buyer-data](http://www.bondbuyer.com/broker/bond-buyer-data).

messaging, and electronic funds transfer. In addition, the emergence of electronic order entry and accounting systems has facilitated significant improvements in the efficiency of managing syndicate accounts. These systems, certainly not available in 1987 when the current 90-day deadline in Rule 11880 was established, allow syndicate members to communicate with each other quickly and efficiently, view unsold balances, and conduct other functions. Technology has streamlined syndicate accounting generally and would help facilitate the transition to 30-day syndicate account closings.

#### ***Transitioning to a 30-day deadline***

We do not believe that compliance with a 30-day deadline for syndicate account closings would require a significant technology investment among bookrunners. Most of the transition would involve changes in processes. Professionals at bookrunning managers would need to more closely monitor the receipt and payment of invoices and proactively request invoices that have not arrived. Once law firms and other vendors become accustomed to shortened deadlines, the process of settling accounts within 30 days will become as seamless as the current 90-day process for corporates and the 30-day process for municipals.

#### ***Syndicate deadline for equity underwriting***

We believe it is appropriate for FINRA to periodically examine dated rules to ensure the terms remain relevant, and in that respect, we encourage FINRA to explore the question of an appropriate syndicate closing standard for equity underwritings. However, BDA does not have a position on whether a 30-day deadline for equities is currently feasible.

#### ***Over-allotment and syndicate closings***

As the Notice recognizes, over-allotments “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.” Over-allotments effectively do not exist in corporate bond transactions and would not be a hurdle to transitioning to a 30-day syndicate closing deadline.

#### ***Sole recourse loans and receivables due from bookrunners***

The Notice references “an SEC staff interpretation under the Net Capital Rules [which] 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.” We are not aware of any market for providing sole recourse loans backed by receivables owed by bookrunners to comanagers. None of our members has ever obtained sole recourse loans backed by these receivables, and we do not believe such a borrowing option exists generally. Moreover, the lender in a sole recourse loan would undoubtedly charge interest to the borrower, resulting in a situation where a comanager would need to incur a liability, including interest expenses and the associated capital charge, for access to its own capital. And this solution would not address the loss of float experienced by comanagers while their funds are tied up at the bookrunner. For these reasons, sole recourse loans are not a workable solution to the issues raised in the Notice.

#### ***Alternatives to a 30-day deadline***

The Notice raises the prospect of “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.” While receiving the bulk of their funds within 30 days would be a better outcome for comanagers than the current Rule, we do not see a justification for bookrunners withholding a portion of comanagers’ funds for perhaps months longer. Bookrunning managers do not need more than 30 days to settle syndicate accounts. Providing more time to return even a portion of comanagers’ funds would be unnecessary and would undercut the benefits of the amendments.

### ***Risks associated with the current 90-day deadline***

As discussed above, the biggest risk faced by comanagers associated with the current 90-day deadline is counterparty credit risk, or the risk that the bookrunning manager could fail to pay comanagers their funds when due. While remote, as anyone who lived through the 2008 financial crisis knows, that risk is real. For example, one firm reported to us that in 2008 they were a comanager on a corporate underwriting which closed in May 2008 lead managed by Lehman Brothers. The comanager finally received their funds from the transaction just days before Lehman declared bankruptcy in September 2008. Another example is Refco, the financial services firm which became insolvent in 2005. Refco was the lead manager in corporate syndicates in as late as August 2005, and they entered bankruptcy in October 2005. Shortening the 90-day deadline to 30 days would mitigate the counterparty credit risk associated with syndicate closings because it would shorten the time that comanagers are exposed to bookrunners.

### ***Effect on new entrants***

Shortening the syndicate closing deadline would undoubtedly lower barriers to entry for broker-dealers seeking to participate in the new-issue corporate underwriting business. This is especially true for smaller broker-dealers and, as discussed above, minority-, women-, and veteran-owned firms. As SIFMA noted in a recent comment letter to FINRA, “the combined effect of FINRA Uniform Practice Rule 11880, which allows syndicate bookrunning managers 90 days to settle syndicate accounts, and the Net Capital Rule, which prevents co-managers from treating syndicate receivables as good capital if they are aged more than 30 days, hurts MWVBDs because they frequently serve as comanagers and, thus, often have significant syndicate receivables.”<sup>4</sup> We agree with SIFMA on this point and we support the amendments in the Notice as the best solution to address this issue.

It is necessary and appropriate for FINRA to review old rules from time to time to ensure they are still relevant and workable. The 35-year-old 90-day deadline for syndicate closings in Rule 11880 is ripe for that review. In 1985 the then-NASD adopted the first syndicate closing rule establishing a deadline for settling accounts and paying comanagers, stating in the adopting release “delays in settling these [syndicate] accounts can result in unnecessary outlays of time and money by syndicate participants.”<sup>5</sup>

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<sup>4</sup> Letter from Kenneth E. Bentsen, SIFMA, to Jennifer Piorko Mitchell, FINRA, June 28, 2021, [www.finra.org/sites/default/files/NoticeComment/Kenneth%20E.%20Bentsen%2C%20Jr.\\_%5BSIFMA%5D\\_6.28.2021%20-%20Comment%20on%20RN%2021-17%20%28June%2028%2C%202021%29.pdf](http://www.finra.org/sites/default/files/NoticeComment/Kenneth%20E.%20Bentsen%2C%20Jr._%5BSIFMA%5D_6.28.2021%20-%20Comment%20on%20RN%2021-17%20%28June%2028%2C%202021%29.pdf).

<sup>5</sup> National Association of Securities Dealers, “NASD Notice 85-59: Effectiveness of Amendment to the Uniform Practice Code to Require Prompt Settlement of Syndicate Accounts,” January 1, 1985.

That is as true today as it was in 1985. The current 90-day deadline represents an unnecessary and risky delay in settling syndicate accounts, and the time has come to modernize the Rule.

We commend FINRA for identifying the issue of a longer-than-necessary syndicate closing deadline for corporate bond underwritings and we fully support the solution offered in the Notice, to shorten the syndicate settlement deadline to 30 days. We urge FINRA to quickly seek approval for this amendment, and we look forward to working with regulators and stakeholders to implement this change. Please do not hesitate to call or write if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael Decker". The signature is fluid and cursive, with the first name "Michael" being more prominent than the last name "Decker".

Michael Decker  
Senior Vice President