



Costs Associated with Issuing Municipal Securities

UNDERSTANDING THE COMPONENTS OF GROSS SPREAD

Certain costs and fees may be incurred in connection with a new issuance of municipal securities. Issuers should understand the types of expenses typically associated with issuing municipal securities so that they can make informed decisions when determining transaction expenses. These costs and fees may vary depending on the type and structure of the financing, among other factors. This document provides an overview of the components of gross spread, which is the difference between the price paid by the underwriter to the issuer of municipal securities for a new issue and the price at which the securities are sold to investors.

Gross spread is sometimes referred to as the underwriter's discount or underwriting spread. The gross spread is allocated to the various expenses incurred during a new issue and the components typically include: takedown, management fee, underwriter expenses, and net to underwriters.

Takedown

Takedown is the compensation to the underwriter for selling the securities. It is generally payable from the proceeds of the new issue and is normally the largest component of the gross spread. The amount of the takedown generally increases as the maturity of the bonds increase. If securities are sold by a member of an underwriting syndicate, (that is, a group of underwriters formed to purchase a new issue of municipal securities from the issuer and offer it for resale to the general public), the syndicate is entitled to the full takedown.

Management Fee

The management fee is an amount paid in a negotiated sale to the lead manager of a syndicate for investment banking services, managing the affairs of the syndicate

and/or structuring the new issue. This fee also is sometimes referred to as a structuring fee. It is payable from the proceeds of the new issue and at the issuer's discretion. In the instance of a syndicate, the lead manager typically receives the management fee, although the issuer may split the fee among certain other members of the syndicate.

Underwriter Expenses

Underwriter expenses are the costs of executing the new issuance (which may include out-of-pocket expenses incurred for managing the syndicate) for which the lead manager may be reimbursed by the issuer. Such expenses typically are payable from the proceeds of the issuance.

Net to Underwriters

The net to underwriters is the amount determined by the senior manager in a competitive sale to offset any potential risk of unsold bonds the syndicate may be liable for at the time of sale. This fee is sometimes referred to as the underwriting fee or risk fee. Any unused portion of this fee is split between the syndicate

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members proportionately to their final liability in the transaction.

Generally, these expenses include:

- Underwriter's counsel fees;
- DTC fees (to utilize the settlement and clearance services of the Depository Trust and Clearing Corporation);
- CUSIP fees (to obtain CUSIP numbers—or unique identifiers for securities—from CUSIP Global Services);
- Cost of Syndicate wires platform used to communicate pricing information with dealers and the issuer;
- Fee for Electronic order monitoring systems;
- Day loan fee (to cover the period between the early morning wire transfer of funds and settlement on the day of closing);
- Investor road show expenses; and
- Out-of-pocket expenses for issue-related travel costs.

Gross Spread and Competitive vs. Negotiated Sales

In a competitive sale, the gross spread is the difference between the price an underwriter pays the issuer and the price at which the underwriter sells bonds to investors. A quote of the gross spread is typically included in an underwriting bid in a competitive sale. Spreads are usually quoted in terms of dollars or points per thousand bonds. For example, a gross spread of

\$5.00/\$1,000 bond on a \$30 million issuance would be \$150,000: $[(\$30 \text{ million} / \$1,000) * \$5.00]$. In a negotiated sale, the gross spread is agreed upon between the issuer and the underwriter.

Gross spreads have historically averaged less for competitive sales than negotiated sales. However, spreads between the two types of offerings are not readily comparable. For example, in a negotiated sale the cost of the underwriter structuring and sizing the deal and performing other tasks is typically included in the management fee whereas in a competitive sale the cost of a financial adviser would be part of the cost of issuance.

Other expenses associated with a new issuance that are generally paid by the issuer are typically known as the costs of issuance¹ and do not factor into the gross spread. Such expenses may include:

- Financial/municipal advisory fees;
- Bond counsel fees;
- Disclosure counsel fees;
- Rating agency fees;
- Bond insurance premiums or credit enhancement fees;
- Trustee fees;
- Escrow agent fees;
- Feasibility study, engineer's report or environmental study; and
- Auditor's fees.

¹ The legal treatment of costs of issuance expenses may be governed by bond resolutions, local ordinances, governing state statutes and federal tax law. Issuers should consult their relevant documents and discuss the treatment of issuance costs and expenses with their financial professionals.

About the MSRB

The Municipal Securities Rulemaking Board (MSRB) protects and strengthens the municipal bond market, enabling access to capital, economic growth, and societal progress in tens of thousands of communities across the country. The MSRB fulfills this mission by creating trust in our market through informed regulation of dealers and municipal advisors that protects investors, issuers and the public interest; building technology systems that power our market and provide transparency for issuers, institutions, and the investing public; and serving as the steward of market data that empowers better decisions and fuels innovation for the future. The MSRB is a self-regulatory organization governed by a board of directors that has a majority of public members, in addition to representatives of regulated entities. The MSRB is overseen by the Securities and Exchange Commission and Congress.

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