Many different types of investors may wish to purchase municipal bonds in the primary market. It is the prerogative of the municipal entity issuing the bonds to determine how to prioritize orders from prospective investors in a negotiated bond offering. The issuer’s priority provisions, sometimes called the priority of orders, determine the hierarchy by which the underwriter must allocate the purchase orders for the municipal bonds. These provisions are included in the distribution plan, which is created in conjunction with the issuer’s municipal advisor, if retained, and underwriters.

**Priority of Orders**

The priority of orders provides transparency to the issuer, senior managing underwriter and the syndicate so that each knows how orders for the bonds will be filled.

The marketing plan will typically include a priority of orders proposed by the senior manager (or sole underwriter). The issuer then reviews and approves the proposed priority of orders as part of its review of the marketing plan. The priority of orders provides the issuer with an opportunity to ensure that the issuer’s bonds are marketed to its target investors and that the bond issuance supports the issuer’s goals and policies. Because most of the categories of orders that are prioritized in the typical priority of orders are compensation-based categories—categories that describe how the underwriters and/or dealers will be compensated for that particular order—the priority of orders also plays a substantial role in determining underwriter and dealer compensation.

**Establishing the Priority of Orders**

While issuers are free to structure the priority of orders in any manner that they see fit in light of their goals and objectives for the offering, the typical priority of orders provides for four different types of orders, in descending order of priority: retail orders, group net orders, net designated orders and member orders.

- **Retail Orders** — orders in which specific eligibility criteria must be met before an investor may place the order. Retail orders are commonly thought of as orders from individual retail investors such as retirees or other individuals. However, an issuer may establish any criteria it sees fit for investors that may place a retail order; thus one issuer’s retail orders may look very different from those of another issuer. If an issuer decides to give priority to retail orders, they are typically given priority over all other orders for a specified time period determined by the issuer. Read more about retail order periods in [Issuer Considerations for Reaching the Retail Investor](#).

- **Group Net Orders** — orders in which each member of the syndicate shares the commission or “takedown” on the order according to the liabilities established in the Agreement Among Underwriters (AAU), the contract...
Applicable Rules

Municipal Securities Rulemaking Board (MSRB) Rule G-11, on primary offering practices, establishes basic standards applicable to the priority of orders so that underwriters honor an issuer’s priority of order instructions. Issuers should understand this and other key rules applicable to priority provisions to be aware of underwriters’ obligations.

Among other requirements, MSRB Rule G-11 requires specific communications between the senior manager (the lead underwriter responsible for “running the order book”) and the syndicate (a group of broker-dealers formed to purchase a new issue of municipal bonds and resell them to the public). MSRB Rule G-11 requires that a dealer may not allocate municipal bonds in a manner other than in accordance with the priority provision unless the issuer permits the senior manager or managers to do so on a case-by-case basis.

MSRB Rule G-8 requires the senior manager to maintain specific books and records for all pricing information and records relating to the primary offering, including information specific to each order submitted during a retail order period.

MSRB Rule G-32 requires the reporting of basic information if an issuer has elected to give priority to retail investors during an order period.

MSRB Rule G-17 establishes that dealers, including underwriters, have a duty to deal fairly with all persons. This fair dealing obligation requires an underwriter to follow an issuer’s directions in a retail order period. It also requires underwriters to take reasonable steps to ensure that orders submitted during a retail order period in fact meet the issuer’s conditions.

These basic regulatory standards promote greater transparency and dealer accountability for adherence to an issuer’s chosen priority of orders and related requirements. Senior managers must communicate the issuer’s terms and conditions and related information to the syndicate and selling group members to permit them to solicit compliant orders. In turn, syndicate and selling group members must record and communicate to the senior manager specific information about orders placed during a retail order period in order to facilitate compliance audits by the issuer. Lastly, senior managers must retain these records and report basic information about any retail order period to assist in evaluating dealer compliance with the issuer’s requirements.

Net Designated Orders — orders in which the investor (typically an institution) directs that the takedown be shared only among particular syndicate members according to percentages specified by the investor. An issuer may decide not to follow the investor’s takedown direction if it conflicts with the issuer’s designation policy, rules establishing the firms to

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1 This document contains only a summary of the key provisions of the MSRB Rules G-32, G-17, G-11 and G-8 with respect to priority provisions as of the date of the publication of this document and should not be relied upon as a substitute for careful review of the rules themselves. The complete text of the rules is available at [http://msrb.org/Rules-and-Interpretations/MSRB-Rules.aspx](http://msrb.org/Rules-and-Interpretations/MSRB-Rules.aspx).
which takedowns may be designated and the percentage of the takedown that may be designated to each eligible firm. Investors submit designated orders to increase the likelihood that their orders will be filled. See the section on “Designation Policy” below for more information.

- **Member Orders** — orders in which the selling firm receives the entire takedown. Typically, the takedown on a member order is not divided among other syndicate members.

As with all of the matters set out in the marketing plan, the priority of orders proposed by the underwriter is simply a proposal. The issuer ultimately determines the final priority of orders, which may differ substantially from the underwriter’s proposal, may be identical to the underwriter’s proposal or may fall somewhere in between.

After bonds are marketed to the target investors and the final priority of orders is established, the order period will commence at a date and time decided by the issuer, in consultation with the underwriter and municipal advisor, if any. Once the order period commences, any co-manager or dealer that submits an order to the senior manager (or sole underwriter) will also indicate into which of the priority of order categories the order fits. This information will be necessary for determining the takedown due to each co-manager and dealer (if any) and will also be helpful in examining underwriter and dealer performance and evaluating the offering’s data post-sale.

Upon issuer approval, the senior manager must communicate the issuer’s terms and conditions, including its priority of orders, retail order period requirements and designation policy to all syndicate and selling group members. The senior manager also must communicate any change in the priority of orders to these persons. This information should also be included in the AAU.

**Designation Policy**

The priority of orders is closely tied to how underwriters will be compensated. The issuer and underwriter typically include a designation policy in the marketing plan to establish a set of rules for how “takedowns,” or compensation paid of the proceeds of the bond issuance, may be allocated among participating firms. This policy applies when a syndicate member or other dealer submits a net designated order to the senior manager (or sole underwriter). This policy may require that a minimum or maximum number of firms are designated in each order. Similarly, the designation policy may set forth a minimum and/or maximum percentage of the takedown on a net designated order that may be designated to any one firm.

The designation policy may also require that a minimum number of firms that meet particular characteristics that reflect or promote the issuer’s values or offering goals must be designated in each order. This may include firms that are historically underutilized businesses, such as a minority- or women-owned business enterprises. Any changes to the designation policy must be approved by the issuer and communicated to the co-managers and other dealers.

An issuer’s designation policy can influence the performance of syndicate members and other dealers. It also permits an issuer to reward all or particular dealers in a manner that it sees fit. As with each of the decision points leading to the pricing of the issuer’s municipal bonds, the designation policy should be guided by the issuer’s goals and any policies that it may wish to promote. For example, if one of the issuer’s goals in...
the municipal bond offering is to maximize sales of the municipal bonds to traditional retail investors, it may consider requiring in its designation policy that at least one retail-investor focused firm is designated in every net designated order.

**Liabilities and the Agreement Among Underwriters (AAU)**

The AAU is the contract between the senior manager, the lead underwriter that runs the order books, and each co-manager, other underwriters in the offering that market the issuer’s bonds and submit orders. This contract establishes the underwriting syndicate, the group of underwriters formed together for the purpose of sharing the risk associated with purchasing and selling the issuer's bonds in the primary market. The AAU typically establishes the specifics of the relationship among the syndicate members and authorizes the senior manager to act on behalf of the group in many respects.

The AAU will typically detail the priority of orders. The AAU also lays out each underwriter’s liability assignment, or the portion of share in the profits and losses of the syndicate in an amount that is either proportionate to its stated liability or a different amount expressed in the AAU.

The AAU may also address a variety of other matters relating to trade practice and applicable rules of the MSRB. Syndicate members generally return executed copies of the AAU to the senior manager approximately two days before pricing. At or about the same time, the issuer may wish to schedule a call with the senior manager (or sole underwriter) and, if desired and applicable, the co-managers to review the issuer’s goals for the bond issuance.

**Selling Group Agreement**

A group of municipal securities dealers known as a selling group also may assist in the distribution of a new issue of municipal securities. Selling group members execute a selling group agreement with the senior manager whereby the municipal securities dealers participate in the distribution of a new issue of municipal securities. However, selling group members are not members of the underwriting syndicate, and do not participate in residual syndicate profits nor share any liability for any unsold balance.