International Organization of Securities Commissions (IOSCO)
(Attn: Alp Eroglu)
Calle Oquendo 12
28006 Madrid
Spain

(*Submitted by e-mail to consultation-05-2019@iosco.org*)

14 February 2020

Dear Sir/Madam,

ICMA public comment on IOSCO's December 2019 Consultation Report: *Conflicts of interest and associated conduct risks during the debt capital raising process (CR05/2019)*

The International Capital Market Association (ICMA)[1] welcomes IOSCO's Consultation Report and sets out its response to it in the annexes to this letter.

ICMA is a not-for-profit membership association, headquartered in Switzerland, that serves the needs of its wide range of member firms in global capital markets. As at October 2019 it has more than 580 members in 62 countries. Among its members are private and public sector issuers, banks and securities houses, asset managers and other investors, capital market infrastructure providers, central banks, law firms and others. See: www.icmagroup.org.

This response is primarily drafted on behalf of ICMA's primary market constituency comprised of underwriters that lead-manage cross-border syndicated bond issuance transactions throughout Europe and beyond. This constituency deliberates principally through:

- the ICMA Primary Market Practices Committee, which gathers the heads / senior members of such lead-managers' syndicate desks; and
- the ICMA Legal and Documentation Committee, which gathers the heads / senior members of such lead-managers' legal documentation / transaction management teams.

ICMA would be pleased to discuss its response at IOSCO's convenience.

Yours faithfully,

Ruari Ewing
Senior Director, Primary Markets
ruari.ewing@icmagroup.org
+44 20 7213 0316

[1] European Transparency Register #0223480577-59

Annex 1 – Main response

General comments

1. **Limited consultation time** – It is helpful that IOSCO has allowed eight weeks. Whilst this would seem quite short a period to generate granular feedback across the wide range of different domestic and international debt capital markets nominally under this consultation heading, this response is able to focus on a specific market segment (as outlined in #3 below) and draw on prior published materials in this respect.

2. **Unclear which market segments the Consultation Report is describing** – Much of IOSCO's current view of debt capital raising, as set out in the Consultation Report, seems to be based on 20 survey responses from among IOSCO's 129 national regulator members (with only a handful of responding countries being at times identified). Many aspects are listed as based on feedback from just *"some"* or *"small number of"* IOSCO members, so it is unclear how firm many of the views in the Consultation Report are (in terms of representing any initial/tentative consensus among IOSCO members) or even to which product/geographic market segments they relate to (bearing in mind that dynamics can vary enormously between segments).

3. **International investment grade syndication market segments** – However, this response covers only debt capital raising in the form that ICMA focuses on: international/cross-border ('Euromarket') investment grade book-built syndicated issuance transactions, mainly across Europe and the MENA and Asia-Pacific regions (transactions in the Americas tend to follow US-style practices) and with an essentially institutional-only investor base. The EMEA market segment involved had a turnover of circa $2.2 trillion in new capital raising in 2019.[2] This response does not thus address domestic, auction, high-yield, private placement, asset-backed securitisation, structured-product and/or mass retail market segments that have very distinct characteristics (though ICMA does focus to an extent on many of them). Significant differences can arise even in the context of cross-border syndication – notably between transactions by frequent issuers (representing most transactions) vs. infrequent/debut issuers. From a terminology perspective one should distinguish retail-inclusive public offers, institutional-only public offers and 'invitation-only' private placements (whether purely bilateral or involving a small 'club' of usually institutional-only investors).

4. **Consultation Report extends beyond nominal conflicts of interest** – Aspects of the Consultation Report also relate to initial disclosure (prospectuses) and market abuse (soundings) regulations and so technically beyond the formal regulatory 'conflict of interest' of interest heading.

<u>**Description of the debt capital raising process**</u> *(Question: "Do you agree that there are conflicts of interest in the debt capital raising process and, if so, what are they?")*

5. Underwriting and placing are complex services – Lead-managers work to ensure transactions are executed as smoothly and as efficiently as possible, whilst meeting their issuer client's size, maturity, pricing and distribution objectives and taking into account possible secondary market performance and a professional investor base willing to participate in the current transaction and in subsequent transactions.

6. Annex 2 to this response letter sets out a description of international syndication (mainly based on the materials highlighted in ICMA's March 2018 *Public comment on IOSCO's Consultation*

[2] Source: Dealogic 2019 full-year EMEA DCM volume.

Report on conflicts of interest and associated conduct risks in equity capital raising). Further narrative on pre-sounding, bookbuilding and allocations is set out in the ICMA Primary Market Handbook (at Appendix A12) and is reproduced for convenience in Annex 3 to this letter. Some narrative can also be found in the World Bank Group's *Issuing International Bonds - A Guidance Note*[3].

7. The description of debt capital raising in the Consultation Report is, regarding international syndication, correct in many respects – though with a few notable distinctions set under paragraphs 8-11 below (and grouped by theme).

8. **Transaction disclosure** (*"Quality of information available to investors"*)

   (a) Connected research is not produced and any existing equity-related research would be focused on equity considerations (growth/profitability prospects) rather than debt considerations (insolvency risk / ability to honour bond terms).

   (b) Investor terms sheets (distinct from issuer term sheets) are more characteristic to just the very technical structuring directly negotiated with investors arising in some asset-backed securitisation and structured-product contexts.

   (c) Publication timing of final standalone prospectuses (or programme drawdown pricing supplements / final terms) tends to relate to listing requirements and so occurs between execution/pricing and closing/settlement.

   (d) Use of proceeds disclosure is often limited to general corporate purposes (green 'intended use of proceeds' bonds being a notable exception).

   (e) Risk factor disclosure may also cover the issuer's jurisdiction.

   (f) Any roadshow information/presentations should be consistent with related prospectus disclosure. Also, whilst roadshow attendance may be nominally invitation based, such invitations are effectively addressed to all relevant[4] investors that underwriters have a communication channel with – and the scheduling of the roadshow is often also publicly announced.

   (g) Institutional investors are (bearing in mind their fiduciary and regulatory obligations) able to decide whether they have had sufficient time to analyse the available information to decide to place an order – consequently an issuer needs merely as a practical matter to ensure that sufficient time has elapsed to achieve the orderbook it desires (and some investors choose to look to sources of information other than the issuer's prospectus).

9. **Allocations**

   (a) It is unsurprising that there is a *"significant difference in the allocations process for private placements and public or listed offerings"* since 'private placement' is a wide concept (including invitation-only transactions sized to demand) and so it is not possible to comment on any specific differences without further detail context (however the 'time-priority' basis cited in the consultation is unknown to Euromarket participants).

   (b) An underwriter's investor relationship (including prior duration and the prospect of future business) are not allocation considerations, though prior participation in similar debt capital raisings might well be (in terms of evidencing commitment to the issuer concerned or to its market segment).

[3] Discussion Paper, MTI Global Practice / No. 13 / April 2019 (Patrick B. G. van der Wansem / Lars Jessen / Diego Rivetti).

[4] So for example perhaps excluding retail or avoiding HY specialist investors on investment grade transactions.

(c) Allocations to connected entities (such as asset managers) are not *per se* inconsistent with issuer interest (contrary to what the consultation seems to suggest), since they mostly operate on an arms' length basis (such allocations are subject to the same allocation considerations as for similar unconnected investors).

(d) It is puzzling that some might see allocations to investors that contribute to price discovery, or (in some market conditions) that could generate a *"favourable"* secondary market, as presenting a potential conflict of interest – since that is exactly the kind of contribution issuers need.

(e) It is unsurprising that IOSCO member responses varied on the extent of issuers' involvement in final allocations determination, since this depends on individual issuer preference – though underwriters try to encourage issuer engagement (clients in any service relationship may choose to be more or less active/granular in instructing their contracted service providers).

(f) Pure pro-rata or time-priority approaches to managing oversubscription are perceived as crude / not accounting for issuer interests and used only on the margins, whilst any 'case-by-case selective reduction' at underwriter *"discretion"* would be, in fact, based on the applicable allocation priorities.

(g) Laddering, spinning and quid pro quo arrangements were considered unacceptable prior to MiFID II being introduced in the EU. See paragraph 6.1 in the 2004 *Guidance on Policies and Procedures for Managing Conflicts of Interest in the Context of Allocation and Pricing of Securities Offerings* (by several organisations including IPMA, one of ICMA's predecessor organisations). In 2003, the FSA (as UK's then financial regulator) stated[5] *"we made clear that practices such as spinning (and quid pro quo arrangements) and laddering are contrary to the [FSA] Principles and COB rules (as they apply to the management of conflicts of interest in relation to issues of securities) and other existing UK law."*

(h) It is unclear why some might see a connection between a perceived absence of conflict/conduct risks and the use of electronic booking platforms (the logistical aspects of order handling do not influence how an order is allocated) or advertised pre-set allocation criteria (which would seem to reduce issuer flexibility to manage its own risk exposure).

10. Pricing

(a) Orderbook demand is the main factor in fixing the credit spread when pricing a new bond (issuers and their underwriters merely suggest price guidance to the market that may or may not result in sufficient investor orders). In this respect, any credit ratings only influence investors' general bond category bucketing / preliminary filtering (by way of minimum floor or maximum ceiling) and so can impact pricing indirectly rather than directly (they should not be the primary basis for an investment decision).

(b) Pricing is ultimately an issuer decision, informed by actual orderbook bids from investors – it is difficult to see how pricing could be subject to underwriter manipulation risk in this respect (and the competitive landscape between underwriters to win business from issuers is a natural incentive to seek to price consistently with issuer objectives).

(c) Any rebates to private banks, regarding further placing work they undertake, may if anything disincentivise (rather than incentivise) issuer allocation, since such allocations are intrinsically more expensive for issuers.

[5] Financial Services Authority *Conflicts of interest: Investment research and issues of securities* (October 2003).

11. Other

(d) *"Cornerstone"* investors, *"early-look"* and *"pilot fishing"* are concepts specific to equity capital raising rather than debt capital raising. [6]

(e) Any marketing roadshows for infrequent/debut issuers precede, rather overlap, transaction execution (which often occurs intra-day as for frequent issuers).

(f) The frequency of inflated orders is variable.[7]

(g) Overnight market risk driving intra-day execution is not so much related to a potential move in the issuer's idiosyncratic credit 'spread' over a reference rate, but rather to a potential move in reference rates themselves and deterioration in broader general credit market sentiment (going 'risk-off').[8]

(h) Issuers may undertake pre-hedging transactions ahead of announcing their new issues.

(i) Underwriters undertake RMT activity following firm hedging quotes to issuers or investors (infrequent/debut issuer execution can also be intra-day and so it is unclear that a frequent issuer context might involve more acute conflict risk).

(j) Grey market trading is ubiquitous, though underwriters will do not participate until the bonds are declared 'free to trade' (FTT) following formal pricing.[9]

(k) The notion of capping fees would seem very strange (if referring to underwriter fees), given the intensely competitive (even all-time low) underwriter fee environment.

(l) The Consultation Report does not explain why further conflict/conduct risks are perceived around client services related to issuance, such as credit facilities, pre-hedging and cross-currency swaps.

Potential risks/harms and regulatory framework

12. The *potential* for conflicts / poor practices may exist in any environment and cannot be 'eliminated' as such (even if only to the point that employees may not always exert themselves as much as they should) – rather one should minimise such *potential* to the extent practical and avoid *actual* conflicts (through the effective management of residual *potential* conflicts).

13. Though conflicts can impact investors, one should not forget the interests of issuers who initiate debt capital raising transactions in order to fund their real economy businesses (and not as a service to investors). Underwriters' syndicate functions act for one client only: the issuer. Any simultaneous investor relationships arise from the separate sales function (and, depending on circumstances, may or may not amount to a 'client' relationship[10]).

14. Various jurisdictions have specific financial regulation relating to conflicts of interests (in addition to more general laws that may have some similar effect). The regime in the European Economic Area (EEA) has been recently re-edited as MiFID II, with notably more granular requirements arising under Articles 38-43 of Regulation EU/2017/565. ICMA understands this consultation is not intended to suggest a re-opening of current EU or US rules.

[6] There can, for example, be proactive 'reverse' interest from investors (enquiring about possible issuance) that can then lead to a new issue being executed. Such 'leadership' might then be recognised in the subsequent allocation process. However, this does not involve a post-issuance 'lock-up' arrangement that is common in the equity 'cornerstone' concept.

[7] However, underwriters may well apply a discount factor to, or even entirely exclude on allocation, orders they view as being potentially inflated.

[8] See also #13 in Annex 2.

[9] See also #15 in Annex 2.

[10] In the UK for example, an investor may formally be, depending on circumstances, a 'corporate finance contact' rather than a client.

<u>Proposed IOSCO Guidance</u> *(Question – "If there are such conflicts, is the Guidance set out in Chapter 5 of this Consultation Report appropriate to address the potential conflicts of interest and associated conduct risks arising in the debt capital raising process?")*

15. Measure 4 (concerning the preparation of research on a new bond offering) is of no practical impact given the absence of such research in the context of international syndication transactions. The remaining measures proposed in the Consultation Report seem to be consistent with current regulatory regimes (notably in the EU). (The generally worded Measure 7 seems to duplicate the more granular Measures 5 and 6.)

<u>Distributed ledger technology</u>

16. The transparency offered by distributed ledger technology (DLT) can be offered under legacy processes and technologies. However, neither issuers nor investors want allocations to be made public. Disintermediation of underwriters is already possible from a technology perspective and its occurrence or not depends on commercial competitive market dynamics, rather than new technologies (such as DLT) that are neutral in this respect.

Annex 2 – International syndication

Issuer objectives

1. Issuers seek not only to minimise their cost of capital, but also the ability to fund themselves flexibly in line with their underlying business needs. In this respect issuers seek to maximise their ability to access the bond markets at any time in the future. This involves building and maintaining investment relationships with a sufficient range of investors that are:

   (a) able meaningfully to contribute to satisfying the issuer's ongoing funding needs; and

   (b) willing to act as committed ('buy and hold') stakeholders in the issuer's business in respect of the above and engage meaningfully in any reasonable restructuring discussions if this unexpectedly comes to pass in the future (rather than immediately on-selling to a 'vulture' fund).

2. Building and maintaining such investment relationships involves, in turn, ensuring good secondary market performance in current transactions so as not to disincentivise such investors from participating in future. If prices decrease or spreads increase (or 'widen') in immediate aftermarket secondary market trading, this will cause buy and hold investors to regret having acquired their bonds in the primary market issue rather than in secondary market trading (all the more so if marking-to-market). Ensuring good secondary market performance also involves:

   (a) receiving constructive feedback from potential investors as to desired issue parameters;

   (b) careful selection of the investors that will receive bonds on issuance, so that there are sufficient sellers to provide the liquidity necessary for the transaction to complete its bedding down but not so many that the bond price or spread is adversely impacted.

3. Issuers are financial market 'end-users' with a strong interest in deciding which investors will receive bonds on issuance.

Typical deal-flow/process

4. Set out below is a description of how international/cross-border ('Euromarket') investment grade book-built syndicated issuance transactions are ***typically*** executed today (bearing in mind issuance methods evolve continuously). There may be much variance in actual practice in individual cases, in response to specific needs and circumstances.

5. Origination desks constantly seek to inform existing and potential issuer clients with market 'colour': the underwriter's assessment (based on investor dialogue and recent primary market activity) as to how the new issuance markets are performing generally and its expectations of what kind of issuance terms (size/maturity/yield combinations) the specific issuer might be able to obtain should it choose to launch a transaction. If an issuer is seriously considering a transaction, it requests proposals from individual underwriters, which notably include information on (i) issuance pricing and terms expectations, (ii) related investor base dynamics/options, (iii) underwriter expertise and (iv) fee/cost arrangements/estimates.

6. In this respect, pre-sounding notably enables an issuer (usually via its underwriters) to privately check with a few meaningful investors whether the likely terms for a bond issuance transaction fit the issuer's corporate objectives, where this is not otherwise clear from existing information (e.g. secondary trading curves). This is particularly so for issuers that are new or infrequent, either

generally or in a particular currency/maturity segment (all the more so if there is sparse activity from other issuers). If a borrower only discovered this after publicly launching the transaction and therefore had to cancel it, it would suffer a significant loss of goodwill from investors who would have wasted valuable resources preparing themselves for the new issue (due diligence, credit lines and liquidity arrangement, etc). This, in turn could prejudice investors' willingness to participate in future transactions, and in turn that issuer's future access to bond market funding. Anecdotal reports indicate that the incidence of pre-sounding substantially reduced following the introduction of the EU's Market Abuse Regulation regime in 2016, with investors reportedly increasingly refusing to be sounded (a combination of extreme bull market conditions might have also contributed).

7. Following subsequent discussions, the issuer then **mandates** as lead-managers those underwriters it wishes to retain as a syndicate to actively run the transaction, fixes the fees and instructs them as to which junior co-managers to invite into the syndicate. The lead-managers' syndicate desks then proceed with the transaction, referring back *throughout* to the issuer whenever necessary (the degree dependent on their detailed understanding of the issuer that in turn depends on the granularity of their prior discussions on this or in any previous transactions[11]), and otherwise involving the issuer to the extent it desires and is willing to make the relevant staff available – *decisions are ultimately the issuer's*.

8. Based on their general market knowledge and any available specific information, the mandated lead-managers **announce** the transaction (issuer name, maturity and any size indication).

9. Issuers will have a public disclosure document, in either 'programme' form (these are updated at least annually and so available potentially months in advance of a transaction) (c.f. #14 below) or in 'standalone' form (often initially as a draft 'red herring' in the context of a two-week roadshow, depending on the level of market familiarity with the issuer concerned).

10. The lead-managers will then open the order book on publication of initial price guidance. This guidance is a spread range over an appropriate reference rate, e.g. +15-25bp or +20bp 'area' (basis points or hundredths of a percent) over mid-market swap rates of the same maturity. Lead-managers' syndicate desks contact their public-side sales desks who then contact investors to flag the transaction. Interested investors will place conditional orders[12] (e.g. €20 million at +15-20bp and €30 million at +21-25bp) with the sales desks, which pass them on to their syndicate desks for inclusion in the book. Depending on the volume of accumulating orders, the lead-managers' syndicate desks revise price guidance as they seek to secure the best (lowest) yield for the issuer commensurate with sufficient 'solid' distribution/demand (in relation to the issuer's funding maturity/size objectives): 'stakeholder' investors that are 'committed' to the issue and so will (i) not immediately on-sell and so depress the price / increase the yield (causing other investors to regret acquiring their bonds in the primary issue rather than in secondary trading and in turn prejudice the issuer's attractiveness for subsequent returns to the market) and (ii) be likely to stand by the issuer and engage in any reasonable restructuring discussions if this unexpectedly came to pass the in future (rather than immediately on-selling to a 'vulture' fund).

11. Once the book has reached the right size and character (with investors hopefully adjusting their conditional orders as price guidance is revised), the lead-managers' syndicate desks close it and formally **launch** the deal by announcing its definitive size and spread (e.g. €1 billion at 17bps). Very frequently in the initially volatile and then low interest rate environment of recent (post-crisis)

[11] So there will be less need for both initial and ongoing discussion with frequent issuers.

[12] Including orders "at reoffer" that are effectively conditional on the current price guidance (and so would need to be reconfirmed or amended following any revision of price guidance).

years, demand has so exceeded supply, that, even at the lowest plausible yield, order-books have been many times oversubscribed. Also, the number of investor 'accounts' in order-books has increased from about an average of 50 pre-crisis to up to 500 now. (Lead-managers cannot simply reduce the yield to exactly match demand, as there is an inflection point at which demand suddenly drops significantly from oversubscription to near-zero.)

12. Following launch, lead-managers as a syndicate determine the book size at the final spread (crystallising the conditional orders and scrubbing any duplicate entries). Then, as a syndicate and based on their general allocation policies (that generally focus on 'solid' distribution as noted in #10 above) and any issuer specific priorities (such as diversifying its investor base into a particular geography), they first establish general allocation percentages for broad groups of investors and then individually review/adjust each order's allocation in light of individual considerations (e.g. early, proactive and useful investor feedback on what the transaction size/yield could be, likely holding horizon, available explanation of any order size's apparent inconsistency with assets under management or prior investment history, etc.). Once the **allocations** have been approved by the issuer, the lead managers **price** the bond, effectively a formality: the issue price is (if needed) adjusted down from 'par' (100% of nominal/face value) to materialise the definitive spread at a coupon that meets the historic convention of being expressed in 1/8ths of a percent (0.125%, 0.25%, etc). This involves computation of future cashflow net present values until the bond's maturity. Therefore, a five-year USD bond pricing 'flat' (at a nil spread) to a mid-swap rate of 1.769% would use a coupon of 1.75% and therefore a reoffer price of 99.91% of par.

13. During the new issue execution process, both issuer and investors are subject to the 'market risk' that an intervening event unrelated to the issuer specifically (such as a central bank announcement on interest rate changes or another issuer's insolvency) will significantly impact the attractiveness of issuer funding / investor investment alternatives. Modern technology enables lead-managers to execute new issues swiftly and issuers and investors expect them to do so: the *time lapse between 'announcement' and 'pricing' above is a matter of hours* (at least for established issuers), often 8am to 4-5pm (with some time zone nuances where a targeting successively e.g. Asian, European and then US investors). Lead-managers consequently have to operate a very streamlined process, with very limited room for non-essential actions.

14. After pricing, the lead-managers finish preparation of contractual/other documentation and any stock exchange listing application (they may have had insufficient time prior to announcement if seizing a favourable market 'window'). Documentation is often available on a shelf-basis in the form of debt issuance programmes (c.f. #9 above). **Signing** of the subscription (and underwriting) agreement between issuer and lead-managers occurs three working days[13] after pricing and **closing/settlement** of the issue (when the bonds are actually issued and delivered to investors) follows a further couple of days later, so there is working week between pricing and the actual issuance. The lead-managers' contractual underwriting obligations run from signing to closing, though their reputational risk can extend wider than this.

15. **Trading** in new bonds can begin at any time – even prior to closing/settlement (the trades are on a conditional "if and when issued" basis). For example, two persons could agree to trade €20 million nominal of a bond (valid contracts usually just require enough certainty around the identity of the potential bond) at a price of 100.315% of nominal. Such 'grey market' trades are settled simultaneously with settlement of the primary issue. Lead-managers however do not participate until the bonds are 'free to trade' (FTT) following pricing. Between pricing and closing/settlement, lead-managers watch the bonds in case they stray much from their issue price (and so the final spread investors opted into) because of, for example, other transactions, misjudging of 'solid'

[13] At least where the bonds are not also being placed into the United States pursuant to Rule 144A.

demand, unrelated supervening events, etc. They do so for the reasons noted in #10. To the extent necessary and possible, they may buy back bonds in the (grey) market on their own account, in order to try to support the price and so keep the spread constant over the reference rate. Such '**<u>stabilisation</u>**' is regulated, e.g. under the Market Abuse Regulation in the EU.

16. An issuer planning to issue may wish to **<u>hedge</u>** its exposure to underlying interest rates and currency movements. It may approach a few financial firms to provide firm quotes in competition in this respect. Such firms may in turn seek to pre-hedge some of their resulting exposure in the event they are appointed. The same thing may apply where investors similarly wish to limit their underlying exposures.

Annex 3 – ICMA Primary Market Handbook, Appendix A12
Pre-sounding, bookbuilding and allocations

Introduction

1. The purpose of this note is to provide some practical information on investor meeting, pre-sounding, bookbuilding and allocation processes (and related disclosure), as often used in the prevalent 'pot' context of the European cross-border syndicated institutional primary debt markets today. Market practice in this area is continually evolving and individual transactions are structured according to their specific circumstances, so this memorandum is not intended to prescribe or endorse particular structures or practices. Rather it is intended to be both a document designed to enhance transparency for, and serve as a helpful point of reference to bookrunners when explaining their working practices to, colleagues, issuers and investors. Some markets (notably in the US) may operate in ways different to those outlined here.

2. Bookrunners of new bond issues seek to ensure transactions are executed as smoothly and as efficiently as possible, whilst meeting the issuer's size, pricing and distribution objectives (if any) and taking into account possible secondary market performance and an investor base willing to participate in this and subsequent transactions. Each bookrunner has internal procedures relating to the pre-sounding, bookbuilding and allocation process. These are applied to individual transactions, but may be tailored where appropriate to accommodate any issuer requirements, other bookrunner procedures and any specificities of the market segment concerned. In this respect, discussions with the issuer and between the individual bookrunners begin at an early stage and continue throughout the transaction.

Investor meetings

3. Many issuers, particularly in volatile times, focus on ensuring investor familiarity with their businesses in order to maximise their ability to take advantage of short and unpredictable issuance windows. This may include holding a series of meetings with investors that, unlike transaction-specific or 'deal' roadshows, are not intended to market a specific immediate transaction (though one might follow if particularly encouraged by investor feedback). Whilst issuers should not communicate material non-public or inside information concerning their businesses in such meetings (focusing rather on outlining published financials, issuance programme prospectus, etc), notice of such meetings is generally publicly disseminated at the time participants are invited (including pursuant to ICMA Recommendation R3.6). This helps address any participant concerns that knowledge of the mere scheduling alone of such meetings might subsequently be characterised as constituting material non-public or inside information of forthcoming issuance under the EU's Market Abuse Directive or similar regulatory regimes.

Pre-sounding

4. In certain market conditions (for example where there is high volatility and uncertainty and the issuer and the bookrunners are looking for confirmation of pricing rationale), seeking initial feedback from a small number of investors, representative of the issuer's targeted investor base, may help the bookrunners in assessing the depth of demand and formulating appropriate initial price guidance, and so help guide the terms of the transaction ahead of a public announcement. In some cases, sufficient feedback may be obtained through disclosing general information not amounting to material non-public or inside information. In other cases, this may be insufficient and more specific information, potentially amounting to material non-public or inside information, might need to be disclosed. In

such cases, the bookrunners carrying out the sounding will initially seek the consent of the investors they wish to approach by indicating that they wish to sound them for a potential transaction on the basis of information that may amount to material non-public or inside information and that the investors could, as a result, be subject to restrictions under laws and regulations applicable to the possession of such information (including restrictions on trading in related securities) – i.e. indicating that the investor is to be 'wallcrossed'. This may be understandably problematic for some of the investors concerned. Incidentally, records are generally required by law to be kept (e.g. of the persons who have been pre-sounded, of the time of the pre-sounding and of the information disclosed), and insider lists are to be updated. Such requirements are generally also incorporated into applicable compliance policies.

5. The interpretation of what constitutes inside information may differ. ICMA issued ICMA Recommendation R3.7 so that bookrunners may confer, and hopefully agree, a uniform approach in the context of individual transactions (both as to whether information may be inside and as to the specific wallcrossing format). The views of the bookrunners however do not constitute legal advice and so cannot and should not be relied upon by the investors, who would need to consult their own compliance functions as to the potential status of the information and the potential scope of the restrictions (including their duration).

6. The practice of wallcrossing is naturally limited by investors' ability and willingness (if they consider the related advantages worthwhile)[1] to be approached in this way and to provide meaningful feedback. Some financial institutions may sound 'hypothetical' transactions for which no issuer mandate has been contemplated (and where by definition no inside information can arise) so as to build up a continuous stream of information for use if needed. Investors may also make 'reverse enquiries' – proactively contacting financial institutions to indicate interest in certain similarly hypothetical transactions.

[Note // 1. Any comfort as to an issuer making, if needed, a public 'cleansing' statement to at least limit the duration of any potential investor restrictions could be a relevant consideration in this respect.]

Intermediate price discovery – "initial price talk"

7. Even following public announcements of transactions, issuers and bookrunners may at times have insufficient certainty as to likely pricing to be able to formally issue price guidance and open orderbooks (bearing in mind that investors expect price guidance, in very limited number of iterations, to be only tightened towards final pricing). If required by market conditions and absent sufficient prior investor feedback, bookrunners may implement an intermediate price discovery step following public announcement of the transaction. This involves public dissemination (recognised by ICMA Recommendation R5.1) of more tentative price indications, on which bookrunners then actively seek feedback. Such indications need to be clearly distinguished from formal price guidance (see further below) – this is because, unlike formal price guidance, they may involve several successive iterations that may widen as well as tighten. The designation generally used (and also recognised by ICMA Recommendation R5.1) is "initial price talk", though designations like "price discovery", "initial price thoughts" and "price level under discussion" are also sometimes used.

Bookbuilding – duration

8. Generally, transactions for frequent issuers (with an established credit curve and documentation) move on an abbreviated timeline (and are less likely to involve roadshows or preliminary offer documents) compared to transactions for inaugural and infrequent issuers

9. In certain market conditions, with substantially more investor demand than supply, submission of investor orders can potentially exceed the proposed new issue size many times over in a very short timeframe, with orders for billions of euros or dollars submitted in just a few minutes in some extreme cases. Aside the general show of market confidence, the additional orders may not bring issuers any material advantage (with even a small amount of oversubscription being sufficient for any desired increase of the initial anticipated size). Aside from further reducing individual allocations, this level of oversubscription can delay the allocation process (extending the parties' uncertainty and potential exposure to market risk). A swift closing of the orderbook helps address this, but may leave some investors aggrieved at not having had sufficient time to place orders reflecting their full demand. Issuers may even face a situation where interest expressed during roadshows alone exceeds the proposed new issue size. These challenges have tended to occur in the context of non-financial corporate issuance rather than in the context of issues by sovereigns, supranational institutions, international agencies or financial institutions.

10. Timing may present a challenge for some investors in that they may, for example, need to review their knowledge of the relevant transaction documentation, obtain credit approvals or to consult colleagues internally to consolidate interest stemming from several sub-funds (potentially across several time zones). There will also be different reaction speeds amongst a broad range of investors. In terms of documentation, frequent issuers (the majority of the market) usually issue off programmes, whilst inaugural or infrequent issuers usually come to market with preliminary offer documents – in both cases published in advance of opening of the orderbooks. For investor convenience however (and pursuant to ICMA Recommendation R5.12), bookrunners generally attach, or include links to, the relevant documentation to or in transaction announcements (or make it available through their orderbook management system). Regular participation in an issuer's roadshows and other investor-facing communication efforts should also assist in investors being kept up to date, in advance of the new transactions, on developments regarding that issuer and so in being ready to participate. In this respect, the few investors participating in any transaction pre-sounding may not be better placed to submit orders on a timely basis.

11. In order to address the above, and with investors currently seeming to favour the ability to place orders over the potential for delayed and reduced allocations, many bookrunners are generally keeping orderbooks open, unless otherwise agreed by the issuer, for a minimum period of 60 minutes from the formal announcement of the transaction. This is reflected in ICMA Recommendation R5.10.

Bookbuilding – price guidance

12. Some form of pricing information is required for investors to be able to decide what, if any, orders to place. Generally, bookrunners will open orderbooks after issuing initial price guidance. Even with prior feedback from a pre-sounding process, the guidance may need to be amended to reflect market conditions and response, with one or more iterations needed to identify the optimum pricing point. Essential to keeping this process efficient and to minimising the number of iterations (pursuant to investor expectations as noted above), is that investors give clear commentary as to the extent, and limits, of their demand by reducing or cancelling their orders at specific pricing levels and/or deal sizes they consider will be unacceptable. Distinctly, issuers faced with 'inflated' orderbooks (see further below) risk being misled into seeking pricing tighter than the market is able to absorb, which may lead to transactions performing poorly in the post launch market. It is for this reason that bookrunners seek to 'scrub' books ahead of allocation, as described below.

Allocation

13. Orders on a new issue may exceed the issuer's initially planned size. In some cases, the issuer may decide to increase the issue size, but, notwithstanding this, orders may even exceed any such increase. Issuers generally have very clear objectives for the amount they wish to borrow in advance of any deal announcement. These views are unlikely to be materially changed by the size of an orderbook. The challenge for bookrunners is firstly to reconcile (e.g. identify duplication) and consolidate the various orders (as books are generally built through several participating banks), secondly to establish true demand (as opposed to apparent demand) and thirdly to allocate the transaction in as efficient and fair a way as possible.

14. On the first aspect, efficiencies are being sought through increased automation with bookrunners increasingly connecting their orderbook management systems in a manner enabling unique investor identification.

15. The second aspect is complex. An investor might place an order larger than its true internal demand (order 'inflation') if, for example, it (i) anticipates that its order will be reduced on allocation because of oversubscription, (ii) overestimates demand that it was unable to confirm internally prior to placing its order, or even (iii) anticipates particularly strong demand by other investors and so expects to liquidate part of its allocation in initial secondary trading to crystallise the initial issuance premium ('flipping'). In this respect, it seems that some investors are unable or do not wish to inflate their orders, others appear to do so frequently, and yet others may do so just occasionally according to market conditions. Leaving aside how order inflation might be treated under applicable market abuse regulations, bookrunners may well apply a discount factor to, or even entirely exclude on allocation, orders they view as being potentially inflated (bookrunner views in this respect will inter alia account for previous experience with specific investors). Investor transparency to bookrunners is an important factor in avoiding mischaracterisation in this respect. In particular, investors may find it helpful to explain orders that (i) appear to be out of proportion compared to orders on previous transactions or to apparent assets under management, or (ii) are placed or increased at a relatively late stage during the launch process (and so appear to be based on perceived levels of demand rather than on transaction fundamentals). This later aspect is further complicated in that delayed demand may be due, as mentioned above, to investors legitimately needing to confer internally with colleagues managing sub-funds.

16. The third aspect is less complex, though 'scrubbed' final orderbooks are, despite the bookrunners efforts, not certain to be entirely inflation free. Aside any preference being given to specifically targeted investor groups (for example where an issuer is seeking to diversify its investor base), some preference may be given to long-term investors that (i) have shown interest in the transaction, for example through actively participating in roadshows, investor update calls, by submitting clear indications of interest / orders, etc., and/or (ii) have a history of investing in the issuer or its sector, and (iii) do not have a history of flipping. Helpful participation in the pre-sounding process may be rewarded by some prioritisation during allocations, though this is limited and seems to be insufficient for many investors to agree to being pre-sounded. A commercial relationship with other parts of bookrunners' firms is not a relevant consideration, being in any case restricted by regulation. Bookrunners frequently discuss their general allocations procedures with individual investors.

17. Bookrunners undertake the above in the interest of their issuer clients. Bookrunners make an allocation proposal to the issuer based on (i) their internal allocation policies developed in relation to their understanding of generic issuer interests (notably such as those outlined above) and (ii) any specific issuer interests/priorities explicitly communicated by the issuer (including pursuant to ICMA Recommendation R5.9) or otherwise arising from the bookrunners' understanding of the issuer's

activities. Issuers may choose simply to rely on the bookrunners' suggestion or to make specific amendments. Such amendments will be given effect – to the extent they are not subject to regulatory restrictions and the bookrunners are otherwise satisfied that the issuer is aware of any related implications. As transactions are executed pursuant to mutual (and ultimately contractual) agreement between issuers and their individual bookrunners, their completion of the transaction necessarily requires them to have reached a consensus on any amendments. A few very sophisticated and frequent issuers may choose to allocate entirely themselves, with bookrunners then providing just a limited book management service. Issuers may participate in allocation calls, bearing in mind that such calls cannot be delayed without potential transaction detriment and that any proactive issuer participation should involve appropriately knowledgeable and empowered issuer staff to avoid such delays.

18 Following an erroneous allocation, the bonds concerned are, prior to being free to trade, either (as appropriate) re-allocated as part of primary execution (subject to any issuer preference) or applied to the syndicate position. After being free to trade, any buying or selling generally takes place at market prices.

Orderbook and distribution disclosure

19. Investors should, and generally do, make their investment decisions on the basis of transaction 'fundamentals' (i.e. the issuer's business and the proposed terms of the issue) rather than 'technicals' (e.g. demand from other investors). Some investors may have understandable reasons for wanting to know levels of demand, and so seek disclosure of orderbook status. However, some investors also seek such information in order to magnify their orders where there is substantial oversubscription and so to improve the likelihood of securing individual allocations that, albeit reduced because of the oversubscription, match their true underlying demand (see further above on inflation of orders and principles of allocation).

20. Though individual bookrunners try to manage investor expectations whilst orderbooks are open, ultimately they will collectively agree, in the circumstances of individual transactions, what degree of disclosure is appropriate to be made before publicly disseminating it. This is reflected in ICMA Recommendation R5.13. Any such disclosure is required by law to be clear, fair and not misleading and issuers and bookrunners focus on ensuring any disclosure is representative of investor demand. This may result in a conclusion in individual cases that no information relating to the orderbook should be disclosed before the book closes. Distinctly, bookrunners may also seek (as one mitigant to order inflation) to limit disclosure of book size to just whether transactions are subscribed or not, without stating the scale of any oversubscription.

21. Investors' understanding of transactions ex-post may help moderate disappointments as to lower than expected allocations and, in this respect, many bookrunners are seeking to distribute, where possible, deal statistics to investors via sales desks within 48 hours of pricing. Any such disclosure of distribution, if made, will also be collectively agreed in advance by the bookrunners pursuant to ICMA Recommendation R6.3.