

STEP 5: METHOD OF SALE

The three main methods of a bond sale are [Competitive](#), [Negotiated](#), and [Private Placement](#).

The lack of agreement among Issuers¹, Municipal Advisor and Underwriters about the relative merits of Competitive vs. Negotiated sales has resulted in considerable debate and discussion over the issue. A large majority of the research studies on the issue suggest an advantage to Competitive sales, yet about 75-80% of bonds nationally are sold through negotiation. Each of the three methods offer different benefits that may result in one method being more suitable than another. For more information, read <http://www.munibondadvisor.com/SaleStudies.htm>

GFOA Best Practices recommended that the Issuer and its Municipal Advisor carefully consider the characteristics of the proposed bond sale and select the method of sale that is best suited to those characteristics. Investment bankers and Underwriters seeking to be hired as Underwriter for a Negotiated sale should not be consulted on the method of sale decision due to their inherent conflict of interest. As such, the Municipal Advisor should be hired before any decision is made as to whether the bonds will be sold through Competitive bidding or negotiation.

It is optimal for the Issuer to have debt policies in place which ensure that:

- The most appropriate method of sale is selected in light of financial, market, transaction-specific, and Issuer-related conditions. Many Issuer's debt policies state that Competitive sales will be used unless there is a clear benefit to using a Negotiated sale. The method of sale is evaluated for each bond issue, including an assessment of the different benefits and risks associated with each method.
- The governmental entity should be able to explain to its governing body and citizens the rationale for its decision.

Competitive Sales

Competitively bid sales are a frequent method of choice for well-rated Issuers selling reasonably sized bonds because competition drives the cost of the issue to the lowest possible level. Consequently, Underwriters bid for these bonds with the comfort of knowing that investors understand and buy them without an extensive educational process. Conditions that generally favor a Competitive sale include:

¹ The term "Issuer" is a general reference to issuing districts, municipalities, and local governments.

- The rating of the bonds is “A” or better.
- The security of the bonds includes the Issuer’s full-faith-and-credit or a strong, historically performing revenue source, such as water or sewer revenues.
- The bond structure does not include complex features that require excessive explanation to the market.

A general outline to a Competitive bond sale is as follows:

1. The Issuer hires outside professionals (usually a Bond Counsel and Municipal Advisor) to review the nature of the project and help them determine the financing requirements.
2. The Issuer, with the assistance of the financing team, prepares a Preliminary Official Statement (POS) that describes the Issuer, the credit structure, the finances, local economy and other items that may be important to potential bond investors.
3. The Bond Counsel and Municipal Advisor prepare legal documents related to the sale including a Notice of Sale (NOS) describing the process for bidders (usually investment banking firms) to submit bids for the bonds.
4. The Issuer’s governing body passes/approve the required authorizing documents to sell the bonds.
5. The Issuer and Municipal Advisor prepare a rating presentation of the credit highlights and schedule a conference call or meeting with the rating agency.
6. The Bond Counsel and Municipal Advisor arrange for the dissemination of the POS and NOS.
7. On the date and time specified in the NOS, the Issuer receives bids for the bonds. The bidders provide bids based on their review of the bond credit worthiness and their perception of investor interest in the bonds. Bids can be received via online bidding programs. The Issuer awards the bonds to the lowest cost bidder. Once the bids are awarded, the winning bidder owns the bonds and can then resell the bonds to investors. The winning bidder receives compensation based on a percentage of the par amount but also takes on the risk they can find investors to purchase the bonds. The ultimate amount of profit the winning bidder receives is based on the price at which they resell the bonds to investors.

Official Bid Form

For Competitively issued bonds, Issuers should include a NOS in the POS. Most commonly, Competitive issues use an electronic platform to accept bids. Two nationally recognized platforms are Ipreo/Parity and MuniAuction/[Grant Street Group](#). Issuers submit the NOS to the electronic bidding service and the details of the sale are posted on a website. Bidders sign up and submit bids using a standardized format which does not allow submittal of bids that do not meet the requirements of the NOS. The Issuer

may view the sale results, confirm the bid calculations, and award the bid electronically after the sale has closed.

Awarding the Bid on Competitive Sales

Acceptable bids must adhere to the terms and conditions of the NOS. The Issuer, Bond Counsel, and Municipal Advisor should be in close contact during the sale to ensure the bids conform to the NOS. One bid should be identified as the apparent winner, subject to later verification. The winning bid is generally awarded based on the lowest True Interest Cost (TIC) but other metrics may be used if identified in the NOS. The Municipal Advisor will verify the computation provided by the electronic bidding platform for the winning and cover bids and Bond Counsel will verify the bid meets all of the parameters identified in the NOS.

Issuers commonly require a good faith deposit from the winning bidder shortly after the award of the bonds. Typically, this good faith deposit is provided by wire transfer to the Issuer by a certain time on the day of the award and is generally set at approximately one percent of the par amount. Most Underwriters will wire the good faith deposit to the Issuer on the same day as the bid. The good faith amount is deducted from the purchase price wired at closing and the Issuer gets to keep interest earnings on the deposit.

Negotiated Sale

In a Negotiated Bond Sale, an Underwriter or team of Underwriters is selected through a Request for Proposals process to help prepare the bonds for sale. The Municipal Advisor can assist the Issuer in writing the RFP and in evaluating the proposals. Negotiated Bond issues allow the Underwriter to know several weeks in advance that it will have a specific product to sell. The Underwriter's sales and marketing force can then begin pre-marketing efforts and discussions with potential investors to determine how receptive the market is to the bond issue. The Issuer also has flexibility to adjust the maturities and coupons at the time of pricing so the structure best suits the Issuer's needs. At the time of the bond sale, pricing is agreed upon between the Issuer, the Municipal Advisor, and the Underwriter.

Conditions that favor a Negotiated Bond Sale include:

- The rating of the bonds is below "A" and credit enhancement is not available.
- The revenue stream backing the debt is weak, uncertain, or has little history.
- The Issuer has specific levy rate targets for a General Obligation Bond.
- The issue is a refunding which is close to savings thresholds.

- The structure of the bonds includes complex features requiring focused explanation to investors.
- Active litigation which could have a material adverse impact on the Issuer's finances.
- Policy considerations, such as Disadvantaged Business Enterprise (DBE) participation and regional firm participation that relate to syndicate membership and bond allocations, or targeting specific investors.

If a Negotiated Sale is to be used, Issuers should make sure that the process is equitable and defensible and keep thorough records throughout the selection process. Critics of Negotiated sales may argue they promote an open and fair process that is inherent to the Competitive bid method of sale. It is imperative that Issuers guard against any appearance of impropriety or abuse of the public trust and select Underwriters and other municipal finance players based on the merit of their qualifications and cost to the taxpayer.

If an Issuer decides to go through the negotiated sale process, there are additional steps to hiring an Underwriter and ensuring a transparent, equitable process:

- The Issuer may undergo an Underwriter selection process through a Request for Proposals (RFP), a Request for Qualifications (RFQ), or another form of solicitation, however, this process is not required under State procurement rules.
- Remain actively involved in each step of the negotiation and sale processes to uphold the public trust.
- Ensure that either an employee of the Issuer or an outside professional (other than the Underwriter), is familiar with, and abreast of, the conditions of the municipal market and is available to assist in structuring the issue, and pricing/monitoring of sales activity.
- The Underwriter and Municipal Advisor of a Negotiated sale are separate roles that are restricted from being performed by the same firm. Hire an Underwriter who offers an electronic online order monitoring platform for reviewing orders as they are entered during the order period, ensuring transparency.
- Request that financial professionals disclose the name or names of any person or firm (e.g. attorneys, lobbyists, and public relations professionals), compensated to promote the selection of the particular financial entities.
- Request all financial professionals submitting joint proposals or intending to enter into joint accounts or any fee-splitting arrangements in connection with a bond issue to fully disclose to the Issuer. This disclosure would include any plan or arrangements to share tasks, responsibilities, and fees earned as well as disclosing the financing professionals with whom the sharing is proposed, the method used to calculate the fees to be earned, and any changes thereto.

- If multiple underwriting firms are hired, review the Agreement Among Underwriters (AAU), and ensure that it governs all transactions during the underwriting period.

A Negotiated Bond Sale has many similar steps to a Competitive sale:

1. The Issuer hires outside professionals (usually a Bond Counsel, and Municipal Advisor and/or Underwriter) to review the nature of the project and help them determine the financing requirements.
2. The Issuer's governing body passes the needed authorizations to sell the bonds.
3. If the Issuer decides to hire an Underwriter through an RFP, the Municipal Advisor and Issuer will prepare a solicitation for Underwriters and distribute the solicitation to qualified firms. A selection should be made based on a preferred method of review of received proposals, and those proposals should include both the firm's experience and the fees they would charge.
4. The Issuer, with the assistance of the financing team, prepares a preliminary official statement (POS) which describes the Issuer, the credit structure, the finances, local economy and other items that may be important to potential bond investors.
5. The Underwriter, Bond Counsel, and Municipal Advisor work with the Issuer to prepare legal documents related to the transaction.
6. The Issuer, Municipal Advisor and/or Underwriter prepare a rating presentation of the credit highlights and schedule a conference call or meeting with the rating agency.
7. The Underwriter arranges for the dissemination of the POS to potential investors.
8. In the weeks leading up to the sale, the Underwriter discusses the bonds with investors and determines, in consultation with investors, the rates and structure that will result in sufficient investor interest to sell all of the bonds. Issuers and their Municipal Advisor should ensure that the preliminary official statement is distributed to a wide array of potential investors, not just to the Underwriter's internal sales force. At the time of pricing, the Underwriter takes orders for the bonds and adjusts the interest rates based on actual orders, to optimize the sale.

Private Placements

A [Private Placement](#) is a special type of Negotiated Sale in which the Issuer sells bonds directly to the investor. The investor is often a bank but may be another type of sophisticated investor. The Issuer either directly contacts a bank or prepares a term sheet, which is circulated to a limited group of banks. A Placement Agent (usually the same firm serving as Underwriter) may perform these duties on behalf of the Issuer, but a Municipal Advisor may **not** provide a list of potential banks or negotiate on behalf of the Issuer in a Private Placement. The Issuer generally specifies the preferred terms of the loan and the

bank responds with conditions and terms that it can offer. The transaction does not generally include disclosure documents (such as the Official Statement) and is generally limited to a loan document prepared by either the bank's counsel or Bond Counsel. The Private Placement can be a cost effective means of financing because issuance costs are lower than the costs of issuing publicly-offered bonds. Therefore, short transactions or small transactions can bear a slightly higher interest rate and still have an overall lower effective borrowing cost. A Private Placement may also offer the benefits of a shorter time to closing, less staff time required and the bank may extend more flexible call provisions or other financing terms compared to a public offering. Riskier securities, such as urban renewal, may not have access to the public market so a Private Placement may be the only option.

A Private Placement generally follows the following steps:

1. The Issuer determines financing needs.
2. The Issuer discusses financing options with a Municipal Advisor or Underwriter/Placement Agent to determine that a Private Placement is the best fit for the financing.
3. The Issuer, Municipal Advisor and/or Placement Agent prepare a proposed term sheet to describe the transaction and circulate to banks.
4. The Issuer contacts their bank or compiles a list of banks, or the Placement Agent solicits proposals from banks.
5. The Issuer, Municipal Advisor and/or Placement Agent review proposals and selects the bank.
6. The Bond Counsel and Municipal Advisor prepare authorizing documents for the financing, which the Issuer's governing body approves.
7. Bond Counsel (usually) or the bank's counsel prepares the loan documents.
8. Issuers should voluntarily disclose the details of Private Placements or bank loans on EMMA, especially if the security is on parity with outstanding publicly sold debt of the Issuer.

Governmental Agency Direct Loans

There are a number of direct lending programs at State agencies and through the USDA. These include programs for clean water, wastewater, highways, and general governmental infrastructure. The availability of funds and the timing of funds vary greatly from program to program and from year to year. Issuers may contact [Oregon Department of Environmental Quality \(DEQ\)](#), [Business Oregon](#), or [Oregon Department of Transportation \(ODOT\)](#) and/or [United States Department of Agriculture \(USDA\)](#) to inquire about these programs. These programs often make funds available at lower costs (often for longer

terms than market-based transactions), may offer longer maturities and more flexible call provisions.

When amendments to SEC Rule 15c2-12 take effect February 27, 2019, issuers of new municipal bonds may be required to agree to disclose to investors significant information about the incurrence of bank loans and similar borrowings, as well as events reflecting financial difficulties related to its existing financial obligations. The new disclosure requirements will apply if a municipality issues a bond on or after February 27, 2019, for which it enters into a new continuing disclosure agreement.