

MEMO# 33240

March 17, 2021

SEC Final Rule to Update NMS Market Data Infrastructure

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March 17, 2021 TO: Equity Markets Advisory Committee
Security Valuation Operations Committee RE: SEC Final Rule to Update NMS Market Data Infrastructure

Last December, the SEC unanimously adopted a final rule to expand NMS market data content and replace the exclusive securities information processors (SIPs) with a decentralized model.[\[1\]](#) The SEC adopted the rule as proposed in most significant respects. We summarize major aspects of the Final Rule and highlight changes from the Proposed Rule, including other aspects of interest to members. They include the SEC's view on how the Final Rule affects broker-dealer best execution requirements. As we previously informed you, the major exchange groups have filed a petition for review in the DC Circuit Court of Appeals to vacate the rule.[\[2\]](#)

Expansion of NMS Core Data

Similar to the Proposed Rule, the Final Rule defines and expands the definition of "core data" to include (i) additional "round lot sizes," *i.e.*, orders in share amounts smaller than 100 shares; (ii) depth-of-book data; and (iii) auction information.

Changes in Price Tiers and Round Lot Sizes

With respect to additional round lot sizes, the SEC reduced the number of tiers and increased the notional value ranges as shown below. The SEC adopted these modifications based on comments that the original proposed five-tier approach was unnecessarily complex and that the tiers should be based on a higher notional value. Similar to the Proposed Rule, the Final Rule requires aggregation of odd-lots across multiple price levels that together are equal to or greater than a round lot, with dissemination at the least aggressive price.[\[3\]](#)

Proposed Rule	Final Rule	Stock Price Group	Round Lot Size	Stock Price Group
\$0.00 - \$50.00	100 shares	\$0.00 - \$250.00	100 shares	\$50.01 - \$100.00
20 shares	\$250.01 - \$1000.00	40 shares	\$100.01 - \$500.00	10 shares
\$1000.01 - \$10,000.00	10 shares	\$500.01 - \$1,000.00	2 shares	\$1,000.01 + 1 share
				\$10,000.01 + 1 share

Changes to Odd-Lot Quotations

The SEC further modified its proposal by expanding core data to additionally include all odd-lot quotes that are priced at or better than the national best bid and national best offer (“NBBO”), aggregated at each price level at each exchange.^[4] The SEC did not originally propose to include this data, but believes its inclusion would further reduce the information asymmetries between proprietary market data products and SIP data. The SEC also stated that these odd-lot quotes would not be subject to the Order Protection Rule, except to the extent that they are aggregated into round lots; it emphasizes, however, that such quotes are subject to best execution requirements, meaning that broker-dealers are required to seek the most favorable terms reasonably available under the circumstances for such orders.

Changes to Applicability of Order Protection Rule

The SEC ultimately did not limit the applicability of the Order Protection Rule (Rule 611) and the requirement to avoid locked or crossed markets (Rule 610(d)) to round lot orders of 100 shares or more. Therefore, these requirements will also apply to the additional smaller round lot sizes. The SEC acknowledged concerns from many different commenters about the proposed limitation, including concerns that unprotected round lot quotes could increase complexity and ambiguity to order handling and routing and, thus, best execution. The SEC further noted that its modifications to the additional round lot sizes would effectively limit the “expansion” of order protection.

Further, the SEC modified its approach to odd-lot aggregation for protected quotations. As originally proposed, order protection would have only applied to odd-lot quotes at a *single price* that, when aggregated, equal 100 shares or more. As adopted, however, such aggregation would be required across *multiple prices* for order protection purposes. The SEC noted that this approach would establish a more consistent odd-lot aggregation methodology across all core data, along with other benefits.

Changes to Depth of Book Data

The SEC modified its proposed inclusion of “depth of book data” in several respects. First, given the changes to the scope of order protection to round lot quote sizes, depth of book data will not include all quote sizes between the best quotes and protected quotes.^[5] Second, to reduce the amount of information to be disseminated, depth of book data will include the next five price levels from the NBBO, rather than five price levels from each exchange’s protected quotes. Third, depth of book data will specify that the aggregate size at each included price level shown will be attributed to each exchange on which the interest is available. Fourth, depth of book will include quotes of national securities associations to account for any future quotes reported to FINRA’s Alternative Display Facility.

Auction Information

The SEC modified the proposed definition of “auction information” to clarify that only auction information that is publicly disseminated on an exchange’s proprietary feeds is included. It would not include auction-related information made available to a limited group of market participants that is not publicly available, *e.g.*, auction information disseminated to floor brokers.

Competing Consolidators and Self-Aggregators

The SEC adopted the proposed decentralization model largely as proposed. Therefore, registered “competing consolidators” and “self-aggregators” will be able to collect from SROs all quote and transaction information necessary to generate consolidated market data. SROs will be required to provide this information in the same manner and using the same methods as they provide to any person. Competing consolidators will be able to consolidate this data and disseminate equity market data products. Self-aggregators, which may include a broker-dealer, exchange, national securities association, or SEC-registered investment adviser, can consolidate this information solely for their own internal use. The SEC reiterated its belief that this model would create a more competitive environment for consolidated market data, which would help deliver data to market participants in a more timely, efficient, and cost-effective manner. Although each competing consolidator and self-aggregator will generate their own NBBO, the SEC reiterated its view that market participants are already accustomed to an environment where multiple NBBOs exist based on the different sources of market data that they currently rely upon.

Implications for Best Execution

The SEC addressed the implications of the Final Rule on the best execution requirement for broker-dealers. In the Proposed Rule, the SEC stated that enhanced core data and greater competition in disseminating consolidated data should allow brokers and dealers to better provide “best execution” to their customers. In the Final Rule, the SEC noted that the amendments would not fundamentally change the requirement but acknowledged that the changes may be relevant to a broker-dealer’s best execution analysis.[\[6\]](#)

However, the SEC also stated that a best execution analysis varies depending upon the characteristics of customers and orders handled. Therefore, it reiterated that it is not setting forth minimum data elements needed to achieve best execution and does not expect that all market participants will need to purchase the most comprehensive or fastest consolidated market data product available. If a broker-dealer uses low-latency or content-rich consolidated market data for proprietary trading, however, then the SEC expects that those products would also be used when handling customer orders.

Effective Date and Transition Period

The Final Rule will be effective 60 days from publication in the Federal Register, but establishes a complex three-phase transition period thereafter:

- Phase One: The fees for data content underlying consolidated market data will be filed with the SEC, reviewed and approved by the SEC, and competing consolidator infrastructure will be developed and tested. Initial competing consolidators will also apply for registration with the SEC.
- Phase Two: The decentralized consolidation model will run in parallel to the exclusive SIP model for an initial operating period. During this time, however, the existing 100-share round lot would continue (until Phase 3). Based on the evaluation of the decentralized model’s operation, the exclusive SIP model will be terminated.
- Phase Three: Additional competing consolidators may register with the SEC. Further, the changes necessary to implement the new round lot sizes will be tested for 90 days. At the end of this test period, the new round lot sizes will be implemented.

endnotes

[1] Market Data Infrastructure, Release No. 90610 (Dec. 9, 2020), *available at* <https://www.sec.gov/rules/final/2020/34-90610.pdf>.

[2] See ICI Memorandum No. 33111 (Feb. 17, 2021), *available at* https://www.ici.org/my_ici/memorandum/memo33111.

[3] The SEC clarified that such aggregation is applicable to each market and does not require cross-market aggregation of odd lots.

[4] The SEC did so by adopting a new definition of “odd-lot data,” which will also include odd-lot transaction data.

[5] The SEC notes that the best quotes and the protected quotes will be the same in the majority of cases.

[6] The SEC noted, for example, that a broker-dealer’s selection of a competing consolidator may be relevant in its ability to achieve and analyze best execution.