

# NMS Plans Require Good Governance to Strengthen Market Structure

February 23, 2016

An important, but little understood feature of US market structure is the operation of National Market System (NMS) Plans. NMS Plans came about through the 1975 Amendments to the Securities and Exchange Act, and essentially provide a mechanism for Self Regulatory Organizations (SROs) to analyze, discuss and make decisions regarding important market structure initiatives intended to enhance the operation of the National Market System. Amongst other plans, there currently exists 1) an [NMS Plan to implement a Tick Size Pilot Program](#), 2) an [NMS Plan to Address Extraordinary Market Volatility](#) and 3) the [Consolidated Tape Association Plan / Consolidated Quotation Plan](#) (CTA/CQ Plans).

What's the plan?

NMS Plans are likely to be getting some more scrutiny in the future, because of a bill currently being worked on in the House of Representatives that seeks to change how the NMS Plans are managed and how decisions are made. Currently this privilege rests solely with the SROs (i.e. Exchanges) involved in that area of market structure, but this draft bill would require that NMS Plans also have representation from the broker dealer community. As [reported by Bloomberg](#) recently, a number of exchange operators recently wrote a letter to members of the House Financial Services Committee objecting to any changes in the governance of NMS Plans.

Profound Effects on Market Structure Rule Making

Changing the governance of an arcane construct of US financial markets regulation may not seem important, but it strikes a blow at the anachronistic way for-profit exchanges get to set the rules by which they play and could have a profound effect on how our markets work.

In 1975 when NMS Plans came into law, all exchanges were member owned organizations - meaning they existed to serve the benefits of their broker dealer owners and the market overall. When they demutualized at the turn of this century they became public companies responsible to deliver profits to their shareholders, but got to keep their SRO status and other benefits. Many in the industry, including SIFMA (which represents broker-dealers, banks, and asset managers) have been critical of NMS Plan governance and believe that better outcomes could be achieved with wider industry participation.

Take for example the CTA/CQ Plan - this encompasses the Security Information Processor (SIP) which is one of

the most controversial pieces of market infrastructure. The SIP was involved in a Nasdaq outage in August 2013, and one related to the NYSE in October 2014. It is also now renowned for being slower than direct feeds (sold by exchanges) often disadvantaging investors who depend on the SIP. This leaves many wondering what incentive do exchanges have to fix and reform the SIP when they are selling a competing product - a product that makes up a significant part of their revenue (approx. 20%).

Or consider the NMS Plan to Address Extraordinary Market Volatility (a.k.a. LULD Plan for Limit Up/Limit Down). This was initiated following the May 2010 Flash Crash and was implemented in phases during 2013. However, as we learned in August last year these new LULD rules did little to address extraordinary market volatility. As selling pressure and volatility built up overnight, structural flaws in market structure were exposed that led to repeated halting in hundreds of securities. Many stocks opened down 20% or more and there was a severe dislocation in the pricing of exchange traded products. Of course, it is impossible to say whether a different governance structure for the NMS Plan would have resulted in better outcomes on August 24<sup>th</sup> 2015, but broader participation from the trading community would undoubtedly add fresh perspective and resources to the problem.

#### A Good Plan

The draft bill currently being drawn up in the House is just a couple of pages long, and calls for a simple change to rule making governance. However the benefits it could bring about are significant - not just for the Plans currently being worked on, but ultimately by redefining the role of SROs in a demutualized world.

---

[www.greenwich.com](http://www.greenwich.com) | [ContactUs@greenwich.com](mailto:ContactUs@greenwich.com)

Coalition Greenwich, a division of CRISIL, an S&P Global Company, is a leading global provider of strategic benchmarking, analytics and insights to the financial services industry.

We specialize in providing unique, high-value and actionable information to help our clients improve their business performance.

Our suite of analytics and insights encompass all key performance metrics and drivers: market share, revenue performance, client relationship share and quality, operational excellence, return on equity, behavioral drivers, and industry evolution.

#### About CRISIL

CRISIL is a leading, agile and innovative global analytics company driven by its mission of making markets function better. It is majority owned by S&P Global Inc., a leading provider of transparent and independent ratings, benchmarks, analytics, and data to the capital and commodity markets worldwide.

CRISIL is India's foremost provider of ratings, data, research, analytics, and solutions with a strong record of growth, culture of innovation, and global footprint.

It has delivered independent opinions, actionable insights and efficient solutions to over 100,000 customers through businesses that operate from India, the U.S., the U.K., Argentina, Poland, China, Hong Kong, and Singapore.

For more information, visit [www.crisil.com](http://www.crisil.com)

## Disclaimer and Copyright

This Document is prepared by Coalition Greenwich, which is a part of CRISIL Ltd, an S&P Global company. All rights reserved. This Document may contain analysis of commercial data relating to revenues, productivity and headcount of financial services organisations (together with any other commercial information set out in the Document). The Document may also include statements, estimates and projections with respect to the anticipated future performance of certain companies and as to the market for those companies' products and services.

The Document does not constitute (or purport to constitute) an accurate or complete representation of past or future activities of the businesses or companies considered in it but rather is designed to only highlight the trends. This Document is not (and does not purport to be) a comprehensive Document on the financial state of any business or company. The Document represents the views of Coalition Greenwich as on the date of the Document and Coalition Greenwich has no obligation to update or change it in the light of new or additional information or changed circumstances after submission of the Document.

This Document is not (and does not purport to be) a credit assessment or investment advice and should not form basis of any lending, investment or credit decision. This Document does not constitute nor form part of an offer or invitation to subscribe for, underwrite or purchase securities in any company. Nor should this Document, or any part of it, form the basis to be relied upon in any way in connection with any contract relating to any securities. The Document is not an investment analysis or research and is not subject to regulatory or legal obligations on the production of, or content of, investment analysis or research.

The data in this Document may reflect the views reported to Coalition Greenwich by the research participants. Interviewees may be asked about their use of and demand for financial products and services and about investment practices in relevant financial markets. Coalition Greenwich compiles the data received, conducts statistical analysis and reviews for presentation purposes to produce the final results.

THE DOCUMENT IS COMPILED FROM SOURCES COALITION GREENWICH BELIEVES TO BE RELIABLE. COALITION GREENWICH DISCLAIMS ALL REPRESENTATIONS OR WARRANTIES, EXPRESSED OR IMPLIED, WITH RESPECT TO THIS DOCUMENT, INCLUDING AS TO THE VALIDITY, ACCURACY, REASONABLENESS OR COMPLETENESS OF THE INFORMATION, STATEMENTS, ASSESSMENTS, ESTIMATES AND PROJECTIONS, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE ARISING OUT OF THE USE OF ALL OR ANY OF THIS DOCUMENT. COALITION GREENWICH ACCEPTS NO LIABILITY WHATSOEVER FOR ANY DIRECT, INDIRECT OR CONSEQUENTIAL LOSS OR DAMAGE OF ANY KIND ARISING OUT OF THE USE OF ALL OR ANY OF THIS DOCUMENT.

Coalition Greenwich is a part of CRISIL Ltd, an S&P Global company. ©2024 CRISIL Ltd. All rights reserved.