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January 31, 2007

Via Electronic Submission and U.S. Mail
Ms. Nancy Morris
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Statement in Support of Action Made by Delegated Authority, File No. SR-NYSEArca-2006-21; Release No. 34-54597 (the "Approval by Delegated Authority");
In the Matter of NetCoalition; Release 34-55011

Dear Ms. Morris:

Philadelphia Stock Exchange, Inc. ("Phlx" or the "Exchange") is pleased to submit to the Securities and Exchange Commission (the "SEC" or the "Commission") this statement in support of the above-referenced Approval by Delegated Authority of a proposed rule change (the "NYSEArca Filing") submitted by NYSE Arca, Inc. to establish fees in respect of specified NYSEArca market data. This review proceeding under Commission Rule 431 was initiated by a petition dated November 14, 2006 (the "Petition") by NetCoalition, a group of companies engaged in Internet business, seeking the Commission's review of the Commission Staff's (the "Staff") approval, under delegated authority.

Phlx strongly believes that the Staff's approval of the NYSEArca Filing was deliberative and consistent with the standards established in the Securities Exchange Act of 1934 (the "Exchange Act"), Commission Rules and settled Commission practices, and was reflective of the Staff's application of sound public policy. Accordingly, the Phlx believes that the Commission should affirm the Approval by Delegated Authority.

Moreover, Phlx contends that the Petition was an attempt to use the Commission's procedures to its advantage to obtain the valuable content of NYSEArca's market data at a lower cost in order to boost the profits of NetCoalition participants. That is, NetCoalition's participants, like other Internet companies, pursue a business model under which they distribute information and other "content" for free (or, in some cases, based upon paid subscriptions for "premium services") to the public (or to defined subscribers). The cost of this data distribution, and the profits of the Internet companies, are subsidized by paid advertising. The more desirable and extensive the content that the

Internet companies can make available on their sites, the more Internet users will seek to visit the site and be exposed to the advertising on the site. The more "hits" there are on the site, the more advertisers will want to be represented there, and the more they will pay. Naturally, NetCoalition wants the Commission to apply standards that will lower the cost of content (such as market data information), because this will result in more valuable content being available to distribute at a lower cost.

To this end, the Petition misstates the law applicable to the approval by the Commission of market data fees, such as those at issue in the NYSEArca Filing. If the Commission were to adopt the standards advocated by NetCoalition (which are not supported by applicable law or precedent), it would severely undercut a number of important policies that are embedded in Section 11A of the Exchange Act, and in the Commission's own rulemaking (most notably its recent adoption of Regulation NMS). Moreover, even if the Commission were to adopt such standards, it would represent a sufficiently significant departure from Commission precedent that the Commission should only do so in the context of rulemaking.

I. The Standards Applied by the Staff in the Approval by Delegated Authority Were Appropriate

NYSEArca proposed to charge specified fees for access to information on limit orders resident on the NYSEArca limit order book and also transaction and limit order information on debt securities that are traded through NYSEArca's facilities. Formerly, this data was distributed by NYSEArca to market data vendors, broker-dealers, private network providers and others without charge.[1] NYSEArca proposed to charge fees of a type charged by other regulated entities, such as the National Association of Securities Dealers, Inc. (the "NASD") and the New York Stock Exchange LLC (the "NYSE"), for similar information, but at significantly lower rates.

In the Approval by Delegated Authority, the Staff reviewed the proposal under the standards established in the Exchange Act. Specifically, Section 19(b)(2) of the Exchange Act requires that proposed rule changes be approved if it finds it to be consistent with applicable provisions of the Exchange Act and rules. Under Section 6(b)(4) of the Exchange Act, national securities exchanges must "provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities." Therefore, all exchange fee filings, including those involving market data fees, must meet this standard.[2]

Moreover, the Commission applies the standards set forth in Section 603 of Regulation NMS to exchange market data filings. Quotation and transaction information

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[1] Approval by Delegated Authority at page 2.

[2] Although many exchange fee filings may be submitted on an "effective on filing" basis under Section 19(b)(3)(A) of the Exchange Act (and therefore need not be approved by the Commission, or by the Staff under delegated authority), market data fees are generally filed on a basis that requires Commission approval (or Staff approval under delegated authority, where available). *See* Concept Release Concerning Self-Regulation, Release No. 34-50700 (December 8, 2004) ("Self-Regulation Concept Release") at footnote 231.

in NMS stocks distributed by an "exclusive processor" to a securities information processor must be done on "terms that are fair and reasonable." In addition, such terms may not be "unfairly discriminatory."

The NYSEArca Filing (as supplemented by NYSEArca's responses to criticism and comments made during the public comment process) reviewed the reasons that these standards were satisfied. In particular, NYSEArca asserted that it had incurred significant costs in developing and enhancing its technology, including specific enhancements geared to the distribution, quality and integrity of the specific data that was the subject of the proposed fees. NYSEArca also offered a detailed comparison of the proposed fees with other comparable data products offered by other self-regulatory organizations. NYSEArca also presented its reasoning why the contractual terms of distribution met the applicable standards.

In the Approval by Delegated Authority, the Staff reviewed in detail the specific justifications advanced by NYSEArca. In particular, it considered the technological resources devoted by NYSEArca,[3] and also analyzed the fairness of the fees in light of other comparable products.[4] Thirteen pages of the Approval by Delegated Authority is devoted to reviewing the proposal in light of applicable standards and addressing the commenters' specific concerns. The Staff's discussion is comprehensive, and indeed much more extensive than in other recent Staff approvals of market data fee proposals.[5]

II. NetCoalition's Cost Justification Arguments are Flawed

The Petition's central argument (though it is styled in several different ways[6] is that the Staff should not have approved the NYSEArca Filing because it did not contain a detailed justification of the proposed fees based upon NYSEArca's cost of producing the data. As set forth below, this argument fails for two main reasons:

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[3] Approval by Delegated Authority at page 45. These enhanced resources will "expand capacity and improve processing efficiency as message traffic increas[es], thereby reducing the latency association with the distribution of ArcaBook data." *Id.* at page 8.

[4] Specifically, NYSE OpenBook, Nasdaq TotalView and OpenView, and data disseminated pursuant to the Nasdaq UTP plan, and the CTA plan. Approval by Delegated Authority at page 45.

[5] *See, e.g.*, Approval of Nasdaq TotalView fees (File No. SR-NASD-2002-33, Release No. 34-46843 (November 22, 2002)); Approval of NYSE OpenBook fees (File No. SR-NYSE-2001-42, Release No 34-45138 (December 7, 2001); Approval of NYSE Real-Time OpenBook fees (File No. SR-NYSE-2004-43, Release No. 34-53585 (March 31, 2006)).

[6] *See* Petition at pages 5 (Approval by Delegated Authority should be set aside because the Staff did not use cost-based standards), 6 (Approval by Delegated Authority arbitrary, capricious, or an abuse of discretion because NYSEArca provided no cost analysis, and Commission staff did not provide economic analysis, of NYSEArca Filing), 8 (view that proposed fees are "an equitable allocation of overall costs" and "fair and reasonable" not supported by cost data), 9 (without cost data, Commission staff "lack[s] a legally sufficient foundation to approve the proposed fee"), 10 (exchange market data fees should be subject to a rigorous cost-based analysis), and 15 (approval of fees is a transfer of money to for-profit exchanges with no showing of cost basis of fees).

- Neither the Exchange Act nor the Commission's rules limit NYSEArca's ability to charge fees for this product to fees that will enable it to recover its costs in producing the data; and
- Requiring a detailed cost justification for the distribution of non-core market data is inconsistent with several critical public policy objectives.

A. *Cost Recovery is Not the Legal Standard*

Neither the statutory language of Section 6(b)(4) of the Exchange Act, nor the terms of Rule 603 or Regulation NMS, compel a result that self-regulatory organizations ("SROs") are limited to recovering their costs in relation to the fees they charge, including market data fees.

Cost recovery is not the standard for SRO fees generally, and there is no statutory language that distinguishes market data fees from other types of fees. Indeed, with rare exceptions (such as fees with a specific stated cost recovery purpose, such as recovering index licensing charges for which the SRO is liable), one would be hard pressed to find examples of a strict cost recovery standard being applied.

Regarding market data fees specifically, NetCoalition cites extensively the Commission's 1999 Concept Release entitled "Regulation of Market Information Fees and Revenues" (the "Market Data Concept Release"), in which the SEC requested comment on various topics concerning the structure of market data distribution, including the standards applicable to market data fee proposals by SROs and NMS plans.[7] It is quite clear from the Market Data Concept Release's discussion of the law, and from subsequent sources cited below, that cost recovery is not the applicable legal standard, nor would it even be a workable standard.

In the Market Data Concept Release, the Commission considered the role of exchange fees, including market data revenues.[8] However, far from asserting that the law requires a strict cost recovery standard for market data revenues, the Market Data Concept Release carefully distinguishes other Exchange Act requirements (including the Exchange Act's provisions pertaining to SRO proposals concerning fixed commission rates) from the requirements applicable to market data revenues.[9] The Commission notes that:

> In Section 11A, however, Congress did not require the Commission to undertake a similar, strictly cost-of-service (or "ratemaking") approach to its review of market information fees in every case. Such an inflexible standard, although unavoidable in some contexts, can entail severe practical difficulties. Instead, Congress, consistent with its approach to the national market system in general, granted the Commission some flexibility in evaluating the fairness and reasonableness of market information fees.

[7] Release No. 34-42208 (December 9, 1999).
[8] *See* Market Data Concept Release at pages 9-10.
[9] *See id.* at pages 22-23 and 33.

> Specifically, Congress articulated general findings and objectives for the national market system in Section 11A and directed the Commission to act accordingly in overseeing its development. Congress thereby allowed the Commission to adopt a more flexible approach than ratemaking.[10]

In fact, in its discussion of Commission proceedings regarding market data revenues, the Market Data Concept Release cites only a single instance in which a strict cost recovery standard was applied, and it took care to distinguish the specific facts prevailing in that instance from most other situations where an SRO or national market system plan seeks to charge for the distribution of market data.[11]

Although the Commission proposed in the Market Data Concept Release a specific approach to the regulation of overall revenues for "core" market data (*i.e.*, consolidated quotation and last sale data for NMS stocks, the collection, consolidation and dissemination of which is mandated under Section 11A of the Exchange Act and Regulation NMS), which is not at issue here, even that approach was not adopted by the Commission.[12] The approach on which the Commission sought comment was harshly commented upon by many commentators, and specifically rejected by the Committee on Market Regulation in its September 2001 report (the "Market Data Advisory Committee Report").[13]

The Market Data Concept Release stands, in part, for the proposition that cost is a factor that may give "guidance" in the application of the "fairness," "reasonableness" and other statutory standards,[14] but it is not, itself, a standard. Rather, the Commission's view was succinctly stated in the following statement drawn from the Market Data Concept Release:

> In summary, Congress granted the Commission broad flexibility in the 1975 Amendments in determining whether the fees charged by an exclusive processor for market information are "fair and reasonable," "not unreasonably discriminatory," and an "equitable allocation" of reasonable fees among persons who use an SRO's facilities. The most important objectives for the Commission to consider in evaluating fees are to assure (1) the wide availability of market information, (2) the neutrality of fees among markets, vendors, broker-dealers, and users, (3) the quality of market information – its integrity, reliability, and accuracy, and (4) fair competition and equal regulation among markets and broker-dealers. [15]

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[10] *Id.* at page 23.
[11] *Id.* at pages 35-37.
[12] Indeed, the Commission again sought public comment on the role of SRO costs in determining appropriate market data fees in the Self-Regulation Concept Release – Questions 23-30.
[13] Letter to the Commission dated September 21, 2001 from Dean Joel Seligman, transmitting the Market Data Advisory Committee Report at page 2.
[14] *Id.* at page 22.
[15] *Id.* at page 33.

Phlx believes that these represent the proper considerations for Staff review of market data fees.

The Commission has not required detailed cost justifications to support proposed market data fees. For example, no such detailed cost justifications were called for in relation to the establishment of fees for Nasdaq's TotalView, DepthView and Powerview data products, the initial establishment of NYSE's OpenBook service, or the addition of real-time fees to NYSE Openbook.[16] In fact, as the Commission noted in its 2004 Concept Release Concerning Self-Regulation[17] (the "Self-Regulation Concept Release"):

> In reviewing a market data fee filing, the Commission has relied to a great extent on the ability of the Networks to negotiate fees that are acceptable to SRO members, information vendors, investors, and other interested parties. The negotiation process is buttressed by the public notice and comment procedures that accompany the Commission's consideration of proposed rule changes.

Therefore, the Staff applied the appropriate legal standards, consistent with established precedent.

B. *A Cost Recovery Standard Would Contravene Important Public Policies – Especially Respecting the Sale of Non-Core Data*

SROs incur significant costs in developing trading systems and communications networks and connectivity. They are, moreover, required to ensure the physical and operational integrity of market data and to conduct surveillance of their members and other users' activities to ensure that the data stream is not corrupted by fraud or manipulative conduct. It is virtually impossible to determine what costs are specifically associated with the production and dissemination of high quality market data versus other SRO functions. Indeed, many costs may be expended for multiple and overlapping functions. Therefore, even if strict cost recovery were the applicable legal standard, it could not readily be applied without extensive use of Commission and SRO resources, and the application of necessarily arbitrary principles of cost and revenue allocation.[18]

Although the Commission has rightfully considered deeply, and solicited public comment on, the extent to which market data revenues should cross-subsidize regulation and other SRO operations,[19] the Phlx believes that the Commission has implicitly accepted this principle over a course of decades. The current position is that SROs must

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[16] *See* supra note 6. *See also* Adopting Release for Regulation NMS, Release No. 34-51808; 70 FR No. 124, 37496 (June 29, 2005) ("Regulation NMS Adopting Release") at page 37561.

[17] *Supra* note 2.

[18] The Commission and commentators point out, rightly, that allocation of particular SRO costs to specific uses (such as isolating those costs that are attributable to the creation and dissemination of particular market data) is extremely subjective and complex. *See id.* at pages 38-39, text accompanying footnotes 95-103; Self-Regulation Concept Release at pages 52-53, text accompanying footnotes 239-249; Market Data Advisory Committee Report at page 39, text accompanying footnotes 180-184.

[19] Self-Regulation Concept Release at pages 57 and 58.

be adequately funded overall in order to carry out their regulatory mission, and that market data fees are an important component of that overall funding.[20]

Historically, market data revenues comprise a large percentage of total revenues for many SROs.[21] By permitting exchanges to demutualize and operate in for-profit form, it seems to Phlx that the sale of data products, and market data revenues, are a legitimate and appropriate source of exchange profitability (subject, of course, to the standards set forth in the Exchange Act and Commission rules).

One of the key recommendations in the Market Data Advisory Committee Report was that "data deeper than that provided by the Display Rule should be available to market participants."[22] The reasons for this are obvious. Market participants can use non-core information, including depth of book data of the type that NYSEArca proposes to charge for to make better-informed trading decisions.[23] Promoting the dissemination of this information advances the key objectives of the national market system. The Commission has endorsed this principle, and yet has not opted to compel the dissemination of such data. Rather, it has chosen to rely on free market forces to determine what non-core data will be disseminated by various markets and broker-dealers.

In its recent adoption of Regulation NMS, the Commission liberalized the freedom of markets to disseminate core and non-core data, which was widely supported by commentators.[24] The Commission followed a principle that SROs themselves should determine what information (beyond what is legally required) would be provided to the marketplace.[25] Traders and investors would decide what services would be useful to them, and what those services are worth. In so doing, the SEC wisely chose not to dictate specific terms, but rather to apply the standards of fairness and nondiscrimination set forth in Rule 603 of Regulation NMS to govern. Establishing a rigid cost-recovery standard for market data fees runs contrary to the Commission's objectives in Regulation NMS.

The Commission's premise in allowing the market to operate to induce SROs to make new data products available will surely not be valid if markets cannot operate profitably. Market data revenues are an important factor in that calculus.

Section 11A(c)(1) of the Exchange Act delegates to the Commission the authority to establish standards pertaining to the dissemination of specified market data. Among the goals of the Commission's rules and regulations promulgated under this authority are to "assure equal regulation of all markets for qualified securities, and all exchange

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[20] Regulation NMS Adopting Release at page 37561, text accompanying footnote 588.
[21] *See* Self-Regulation Concept Release at pages 47-48.
[22] Market Data Advisory Committee Report at page 47.
[23] *See* Regulation NMS Adopting Release at page 37566; *see also* Self-Regulation Concept Release, *supra* note 2, at page 49.
[24] Regulation NMS Adopting Release at page 37566, text accompanying footnote 636.
[25] *Id.* at 37567; *see also* Self-Regulation Concept Release at page 55.

members, brokers, and dealers effecting transactions in such securities."[26] Under Section 3(a)(36) of the Exchange Act, a class of persons or markets is subject to "equal regulation" if "no member of the class has a competitive advantage over any other member thereof resulting from a disparity in their regulation under [the Exchange Act] ... which the Commission determines is unfair and not necessary or appropriate in furtherance of the purposes of ... [the Exchange Act]." In the instant case, NYSEArca is proposing to sell for a fee information of a type that some SROs are selling already, and that a broker-dealer could distribute for free or at a cost which it determines. The dissemination by both NYSEArca, other SROs and such broker-dealers are subject to the standards set forth in Rule 603 of Regulation NMS cited above. NYSEArca should not be held to a standard that is more stringent than that which was applied to its SRO competitors. Moreover, the Commission has not historically, and would not likely, apply such standards to require a detailed cost justification by a broker-dealer seeking to charge a fee for its depth of book information. How could such a justification and standard be applied to NYSEArca without imposing a serious competitive burden on NYSEArca in violation of the equal regulation standard established by Section 11A(c)?

III. If the Commission is to Establish a New Standard, It Should do so Through Rulemaking and not in the Context of an Individual SRO Rule Proposal

Finally, should the Commission decide to establish a new standard for evaluation of market data fees, that standard should be established via the SEC rulemaking process, not through a proceeding under Commission Rule 431 to review a single SRO's proposed fee structure. Rulemaking provides all interested parties who would be affected by a new standard an opportunity to comment upon a specific proposal. Commission rulemaking also entails a rigorous process of cost-benefit analysis and a review of efficiency, burdens on competition and capital formation, among other things. [27]

Based on the foregoing, the Exchange believes that there is no need for Commission action in this instance, other than to affirm the Staff's action. If the Commission seeks a broader review of market data fees, then it should conduct it in the proper fora.

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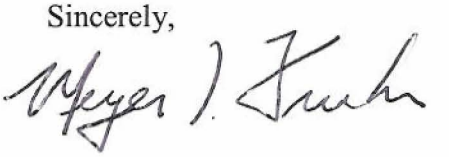
For the reasons stated above, Phlx urges the Commission to uphold the Approval by Delegated Authority.

Sincerely,



[26] Section 11A(c)(1)(F) of the Exchange Act.
[27] 15 U.S.C. 78(c)(f).