SIFMA
Securities Industry and
Financial Markets Association

August 1, 2007

Via E-mail
Ms. Nancy Morris
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20002

Re: In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21

Dear Ms. Morris:

The Securities Industry and Financial Markets Association ("SIFMA")[1] would like to offer comments on the letter filed by Nasdaq (the "Nasdaq Letter")[2] in connection with NetCoalition's petition (the "Petition") challenging the Division of Market Regulation staff's approval of SR-NYSEArca 2006-021. SIFMA believes the arguments offered by Nasdaq for its position cannot be supported and thus should not be given weight in any Securities and Exchange Commission ("SEC" or "Commission") decision on the Petition.

At the outset, SIFMA reiterates its support for the unanimous decision of the Commission to grant the Petition, and continues to believe that the Commission must overturn the decision of its staff in this matter. As we have explained in our prior letters on this matter and once again below, we see no legally sufficient basis under the Securities Exchange Act of 1934 ("Exchange Act"), including Sections 6(b), 11A, and 19(b), and the Administrative Procedure Act, for the Commission to uphold the staff's order approving this new NYSEArca market data fee. This fee, as do other recent exchange fee proposals, represents an unfortunate trend whereby for-profit exchanges are misusing their regulatory power in a non-competitive market to set a fee to benefit itself as a commercial enterprise. We believe the public input from

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[1] The Securities Industry and Financial Markets Association brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C. and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

[2] Comment Letter from Jeffrey Davis, Vice President and Deputy General Counsel, Nasdaq re: File No. SR-NYSEArca-2006-21 (May 18, 2007) available at http://www.sec.gov/comments/34-55011/3455011-19.pdf.

SIFMA,[3] as well as from other business, professional, and financial industry associations, individual firms, and over 140 individual investors in support of the Petition or in raising objections to Nasdaq's own similar pending single exchange market data depth-of-book rule proposal, underscores the need for the Commission to undertake a broad public review of the approval process for exchange market data products and fees to ensure that – in today's market – there is compliance with the Exchange Act and all investors have fair access to market data.[4]

The following discussion responds to what we deem to be incorrect assumptions and arguments in the Nasdaq Letter, namely that single exchange market data is "proprietary," that it is subject to market "choice" and ease of entry, and, therefore, that any fee proposals need only be reviewed under a more relaxed standard of "fair and reasonable" under the Exchange Act.

A. Prices Charged by For-Profit Exchanges Are Not Entitled to Deference

Nasdaq asserts in its letter that its prices for market data it calls "proprietary," including depth-of-book data, are reasonable because the market for such data is "currently competitive and inherently contestable." Nasdaq also asserts that the Commission should defer to the exchanges and let "market forces" take over as regulator. Unfortunately, Nasdaq does not provide any back-up economic data or analysis of the relevant market, and does not address the fact that competitive forces do not apply here because each exchange is the sole source for its market data.

The exchanges previously claimed that they should be given deference by the Commission in such fee decisions. The U.S. Senate, however, rejected such arguments in its Securities Industry Study preceding enactment of the 1975 Amendments. There, the U.S. Senate emphasized that the exchanges are not "partners" with the Commission, but are subject to the

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[3] Comment Letter from SIFMA re: In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21 (Mar. 5, 2007); Comment Letter from SIFMA re: In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21 (Jan. 17, 2007); *see also* Comment Letter from SIFMA re: File Nos. SR-NYSEArca-2006-21 and SR-NYSEArca 2006-23 (Aug. 18, 2006); Comment Letter from SIFMA re: File Nos. SR-NYSEArca-2006-21 and SR-NYSEArca 2006-23 (June 30, 2006).

[4] *E.g.*, Comment Letters from David T. Hirschman, Senior Vice President, U.S. Chamber of Commerce (May 3, 2007); Keith F. Higgins, Chair, Committee on Federal Regulation of Securities, Business Law Section, of the American Bar Association (Feb. 12, 2007); Richard M. Whiting, Executive Director and General Counsel, The Financial Services Roundtable (Jan. 17, 2007); Joseph Rizzello, Chief Executive Officer, National Stock Exchange (Feb. 27, 2007); James A. Forese, Managing Director, Head of Global Equities, Citigroup (Feb. 5, 2007); Jeffrey T. Brown, Senior Vice President, Charles Schwab & Co.; Sanjiv Gupta, Bloomberg L.P. (Jan. 17, 2007). Nasdaq and the Commission must also consider and respond to the 143 comment letters in the original Nasdaq TotalView – INET market data rule proposal, SR-NASDAQ-2006-013, which raises the same statutory and policy issues and covers the identical proposed changes to INET and TotalView as the subsequently filed SR-NASDAQ-2006-053 as well as the NetCoalition Petition.

Commission's authority and are, therefore, not entitled to deference**.** The relevant passage states:

> In an effort to emphasize the fact that both the industry *and* the government have regulatory responsibilities under the Exchange Act, many people have referred to the "partnership" between the self-regulatory organizations and the SEC, or to the "cooperative" character of the regulatory system. Indeed, the recent Securities Industry Study Report of the House Subcommittee on Commerce and Finance went so far as to conclude " . . .that the phrase 'self regulation' must be consigned to the past. 'Cooperative regulation' best describes the common task of protecting investors and the public interest." The Subcommittee concurs in the need to reaffirm the mutual regulatory responsibilities of the industry and the SEC. If the term "self regulation" is misleading, then by all means it should be discarded. However, care should be exercised, lest the use of phrases such as "partnership" and "cooperative regulation" lead to the impression that the industry and the government fulfill the same function in the regulatory framework or that they enjoy the same order of authority or deserve the same degree of deference, whether by firms, courts, or the Congress.[5]

B. Distribution of Market Data Must Be on Fair, Reasonable, and Non-Discriminatory Terms

We are aware that the Commission has determined that exchanges are not obliged to publish depth-of-market quotation data (data concerning quotations above and below the NBBO). If an exchange chooses to publish such data, however, we maintain that the Commission did not also rule that the fees for such data products are free of Commission oversight and review or that those charges are not subject to the same statutory standards as apply to "top-of-file" data the exchanges are required to publish. The same statutory standards apply to both "consolidated" and "depth-of-book" data.

1. Exchanges Must Provide Reasonable Access to All of Their Facilities

Exchange Act Section 6(b)(4) sets forth a standard that exchange rules must meet for the use of their facilities:

> …the rules of the exchange [must] provide for the equitable allocation of reasonable dues, fees, and other charges among the members and issuers and other persons using its facilities.

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[5] *Securities Industry Study*, Report of the Subcomm. on Securities, Senate Comm. on Banking, Housing and Urban Affairs, S. Doc. No. 93-13, 93d Cong., 1st Sess. 147 (1973) [emphasis in original; footnotes omitted].

Exchange Act Section 3(a)(2) defines "facility" of a national securities exchange in a way that unambiguously encompasses all market quotation data:

> …the term 'facility' when used with respect to an exchange includes its premises, tangible or intangible property whether on the premises or not, any right to the use of such premises or property or any service thereof for the purpose of effecting or reporting a transaction on an exchange (including, among other things, any system of communication to or from the exchange, by ticker or otherwise, maintained by or with the consent of the exchange), and any right of the exchange to the use of any property or service.

Thus, if exchanges are going to make depth-of-book data available, Section 6 does not permit a different standard to be used for accessing the consolidated book as opposed to depth-of-book data.

2. Congress Intended That the Exchanges' Rates be Subject to Review

Congress, in amending the Exchange Act in 1975, made it clear that exchanges were no longer free to have rules that fell outside the statutory standards and that were exempt from Commission review. Congress repealed former Exchange Act Section 6(c) and, for the first time, subjected exchanges to the more exacting standards that had previously applied only to the NASD as a registered national securities association. The Senate described the reasons for that change as follows:

> [T]here is nothing in the [pre-1975] Exchange Act which explicitly limits or defines an exchange's rule-making authority: Indeed, present [*i.e.*, pre-1975] Section 6(c) states:
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> > Nothing in this title shall be construed to prevent any exchange from adopting and enforcing any rule not inconsistent with this title and the rules and regulations thereunder and the applicable laws of the State in which it is located.
>
> The authority of national securities associations is dealt with substantially differently. . . . The Committee believes that the statutory pattern governing the scope of the NASD's authority is basically sound. The bill would extend the pattern now applicable to registered securities associations to exchanges. Thus, the bill would eliminate . . . the seemingly open-ended authority in present Section 6(c).
>
> Under the bill the scope of the rule-making authority and responsibility of all self-regulatory organizations would be defined in terms of purposes and standards . . . The purposes to be served by self-regulatory rules

> would be expressed affirmatively and negatively (what the rules must, and what they may not be, designed to accomplish).[6]

We note that Nasdaq itself believes that the requirement that the Commission consider whether a market data fee proposal promotes efficiency, competition, and capital formation should not be a "pro forma requirement."[7] We concur with this statement but have a more robust interpretation of it, in that we believe the statute requires that the Commission's findings should be grounded in cost information and analysis to support any new market data fees and not just on a summary "reasoned explanation for the fee." If the exchange does not provide more than this summary information, it is not possible for interested parties to respond to the fee proposals and their possible impact on investors during the comment period as Nasdaq suggests.[8]

3. The Exchange Act Requires the Distribution of All Raw Market Data on Fair, Reasonable, and Non-Discriminatory Terms

Exchange Act Sections 11A(c)(1)(C) and (D) charge the Commission with the authority to regulate exchanges to ensure that market information processors may obtain on terms that are fair, reasonable, and not unreasonably discriminatory "information with respect to quotations for and transactions in securities as is published or distributed by any self-regulatory organization or securities information processor." The intent and legal effect of those provisions is unambiguous. Congress did not distinguish between "top-of-file" quotation information and depth-of-market information. Once an exchange publishes or distributes any such information, regardless of its legal obligations to do so, the statutory standards attach to the fees and other conditions to access the information.

The Commission has recognized that exchange market data fees are subject to Section 11A. In its 1999 Concept Release on the Regulation of Market Data Information Fees and Revenues, the Commission stated:

> Congress was particularly concerned about entities that would be exclusive processors of market information for the SROs. It noted that any such processor would be 'in effect, a public utility, and thus it must function in a manner which is absolutely neutral with respect to all market centers, all market makers, and all private firms.' Section 11A was intended to 'grant the SEC broad powers over any exclusive processor and

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[6] Senate Comm. on Banking, Housing, and Urban Affairs, Securities Acts Amendments of 1975, S. Rep. No. 94-75, at 26-7 (1975), *reprinted in* 1975 U.S.C.C.A.N. 179, 205-6.

[7] Nasdaq Letter at 10.

[8] Nasdaq Letter at 15.

> impose on that agency a responsibility to assure the processor's neutrality and the reasonableness of its charges in practice as well as in concept.'[9]

In keeping with Congress's approach, the Commission did not suggest that any distinction be drawn under the Exchange Act between exchange fees for top-of-file quotations and exchange fees for depth-of-book quotations. Both are equally subject to the Exchange Act standards. This is the standard the Commission has consistently applied, and there is no legal or policy basis to depart from it now.

Indeed, the courts have repeatedly held that an unjustifiable departure from prior Commission interpretation is reversible as a matter of law. In a recent case, *Goldstein v. Securities and Exchange Commission*, the D.C. Circuit Court of Appeals stated: "By painting with such a broad brush, the Commission has failed adequately to justify departing from its own prior interpretation of [Advisers Act] § 203(b)(3). . ."[10] The court further stated:

> As discussed above, the Commission does not justify this exception by reference to any change in the nature of investment adviser-client relationships since the safe harbor was adopted. Absent such a justification, its choice appears completely arbitrary. See Northpoint Technology, Ltd. v. FCC, 412 F.3d 145, 156 (D.C. Cir. 2005) (**"**A statutory interpretation . . . that results from an unexplained departure from prior [agency] policy and practice is not a reasonable one.**"**).[11]

In short, Nasdaq's effort to draw a distinction between "consolidated data" and "proprietary data" is insupportable under the statute. This separation of raw price data into two categories for disparate regulatory treatment appears nowhere in Section 6(b)(4), quoted above, or in Exchange Act Section 11A. The latter section prohibits an improper limitation on access to the SRO's services and imposes the "fair and reasonable" pricing standard on an SRO or other entity that distributes the market information of an SRO on an exclusive basis.

C. Sole-Source Market Data is Not Competitive

In its letter, Nasdaq analogizes market data to pricing new cars, and argues that neither has a monopoly.[12] This analogy, however, does not work for several reasons. First, purchasers

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[9] Exchange Act Release No. 42208 (December 9, 1999) in text at nn. 77 & 78 [footnotes omitted].

[10] *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006)(overturned the SEC's rule that required most hedge fund managers to register as investment advisers with the SEC, holding that the SEC had failed adequately to justify departing from its own prior interpretation of the relevant statutory provision and that there was a "disconnect" between the factors the SEC cited and the rule it promulgated).

[11] *Id.*

[12] Nasdaq Letter at 7.

can easily substitute one car for another. Although a Ford and a Honda can take you to the same place, you must purchase both NYSE and Nasdaq dated to show you the best price, and therefore they are not substitutable for each other. In addition, Ford and Honda are not legally entitled to receive all of the glass, rubber, and steel required to assemble the cars from their customers without compensation. Likewise, Ford and Honda are not authorized to issue regulations binding on their customers, nor to bring enforcement actions against their customers.

The "market" provides no assurance that the prices the exchanges set for their sole source market data are fair, reasonable, or not unreasonably discriminatory as required by the Exchange Act. Each exchange receives quote and order information from broker-dealers at no cost. The exchange then has exclusive control over aggregating that data, and is the only supplier of that data. An investor who wants to understand fully what is happening in the largest liquidity centers for a given security (commonly known as transparency) and to make the best investment decision needs speedy access to current quote pricing information at each of these dominant exchanges. As a result, the investor needs to have the data from each of the exchanges where the security is traded, not just one. The data from one is not a substitute for data from the other.

Nasdaq's assertion that "the market for proprietary data is currently competitive and inherently contestable" is untrue. Although the exchanges today compete for order flow in securities traded on more than one exchange, there is no competition among exchanges for the resulting market data on any particular exchange. Competition in the listing market does not mean that there is competition or innovation in market data which is dominated by exclusive processors such as Nasdaq.

Indeed, the Commission provided the following explanation of the policy goals of Rule 603:

> The "fair and reasonable" and "not unreasonably discriminatory" requirements in adopted Rule 603(a) are derived from the language of Section 11A(c) of the Securities Exchange Act. Under Section 11A(c)(1)(C), the more stringent "fair and reasonable" requirement is applicable to an "exclusive processor," which is defined in Section 3(a)(22)(B) of the Exchange Act as an SRO or other entity that distributes the market information on an exclusive basis.[13]

As the Commission's order of last year underscored, NYSEArca as an exchange is clearly acting as an exclusive securities information processor as defined in Section 3(a)(22)(B) of the Exchange Act.[14] In fact, Congress has charged the Commission with regulating market data fees

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[13] Exchange Act Release No. 51808, 70 Fed. Reg. 37496, at 37567 (June 29, 2005).

[14] The Commission's order of May 24, 2006 granting an exemption to NYSE Market, Inc. and NYSE Arca from requirements to register as a securities information processor underscores sole-source depth of book as an exclusive securities information processor. In its order granting the exemption, the Commission noted that in connection with the NYSE/Arca merger, the Commission approved a proposed rule change filed by the NYSE pursuant to Section 19(b) of the Exchange Act and Rule 19b-4 thereunder in which the Commission stated:

charged by exclusive processors because there are no "market forces" at work. Further evidence of the monopoly comes from the United Kingdom, where its competition authorities, the Office of Fair Trading and the Competition Commission, have concluded that:

> An exchange is a monopolist of its proprietary market information. Of necessity the available market data sets will vary as between exchanges. As such, information from other exchanges is complementary and cannot substitute for exchange-specific information.[15]

D. Comparison to Previous Anticompetitive Proposals

1. Value – *Instinet* Case

Nasdaq is asking the Commission to depart from the Commission's prior interpretation of Section 11A. In the 1980s, the Commission rejected, and the D.C. Circuit later affirmed, as excessive a fee proposed by NASD to be charged to its competitor's customers for access to depth-of-book market data.[16] Instinet, a former competitor of NASD (and Nasdaq), argued that NASD's proposed fee for Instinet subscribers to access certain depth-of-book data, without access to other services available to NASD subscribers at the same price, was unreasonably high and constituted an improper limitation on access to the data.[17]

The Commission agreed with Instinet, explaining that NASD's value-of-service method of computing the Instinet subscriber fee effectively would require Instinet's subscribers to pay for services that they did not receive. The Commission ruled that "NASD, in effect, should recover only those costs it would incur if it operated a pure "pass-through" system--a system that only collected information and passed it on to vendors. The NASD should not recover any costs related to its own competing vendor service."[18] The Court, in affirming the case, observed that

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"[B]ecause NYSE Market would be engaging, on an exclusive basis on behalf of NYSE LLC, in collecting, processing, or preparing for distribution or publication of information with respect to transactions or quotations on, or effected or made by means of, a facility of NYSE LLC, it would be an exclusive processor … NYSE Arca LLC is acting as an exclusive processor for NYSE Arca and is therefore also subject to the registration requirement in Section 11A(b) of the Exchange Act." Exchange Act Release 53856, at 2 (May 26, 2006).

[15] *Anticipated acquisition by Deutsche Börse AG of the London Stock Exchange plc,* Office of Fair Trading decision (Mar. 29, 2005), at 26, available at http://www.oft.gov.uk/shared_oft/mergers_ea02/2005/deutsche.pdf.

[16] Exchange Act Release No. 20874, 49 FR 17640 (Apr. 24, 1984), *aff'd NASD, Inc. v. SEC*, 801 F. 2d 1415 (D.C. Cir. 1986).

[17] *Instinet* shows that if exclusive data is not priced according to statutory standards, the amount charged can become prohibitory and an impermissible limitation on access to an exchange facility. This concern about exclusive data processors, such as NYSEArca (and Nasdaq), underlies Sections 11A(b)(5)(A) and 6(b)(7) of the Exchange Act, and is reflected in the Commission's consideration of NYSE Arca's request for exemption from registration as a securities information processor. *See* Exchange Act Release No. 53856 (May 24, 2006).

[18] 49 Fed. Reg. 17,640, 17,649 (1984).

"[t]he Commission agreed with Instinet that NASD's charges must be cost-based," and characterized the NASD argument that fees be based on "value" as "obviously untenable."[19]

Today, Nasdaq and other exchanges are imposing a similar fee structure to that struck down in the *Instinet* case. Nasdaq charges broker-dealers and other distributors a license fee for the right to distribute its depth-of-book TotalView product to professional and non-professional users. In addition, Nasdaq imposes usage charges on the broker-dealers' customers — professional and non-professional — that are the same as what Nasdaq charges the same classes of users who receive the data via a direct feed from Nasdaq.

In today's for-profit exchange environment, the Commission should not embrace the use of the "value" standard previously rejected by the Court and the Commission. The Commission should instead base its decisions on cost data and economic analysis of the fees.[20]

2. **"Fair and Reasonable" – The Consolidated Tape Association**

The interested parties in this matter continue to debate what Congress meant by "fair and reasonable" as used in Exchange Act Section 11A(c)(1)(C) as a standard for the Commission to approve market data fees. Nasdaq and some other exchanges have suggested that the "fair and reasonable" standard leaves unbounded the relationship of market data fees to the costs of collecting and disseminating the data. Yet, Nasdaq has argued, and the Commission agreed, that the entrance fee it is required to pay as a new CTA participant is not "fair and reasonable" because CTA did not submit cost data supporting that fee. We respectfully assert that "fair and reasonable" cannot have one meaning when applied to exchange market data fees and yet another, diametrically opposed meaning when applied in other contexts.

Commissioner Nazareth, when she was Director of the Division of Market Regulation, advised the Consolidated Tape Association as follows with respect to the fees to be charged to new entrants pursuant to its Plan:

> The Division believes that the process for determining a proper entrance fee should be transparent to ensure fairness to potential new participants and to address potential anti-competitive concerns. New entrant fees should not pose an unnecessary competitive burden or barrier to entry on new entrants. We therefore believe that the Plan should be amended to include solely objective standards for determining new entrant fees. In particular, the Plan should delineate the method for determining (1) the specific costs current Plan participants have incurred in the development,

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19 *Id.*

20 SIFMA welcomes Chairman Cox's naming of James Overdahl as SEC Chief Economist and head of the Commission's Office of Economic Analysis and the accompanying commitment to "…ensure that rigorous economic analysis is fully integrated into the Commission's rulemaking and policymaking process." SEC Press Release 2007-150 (July 26, 2007).

> expansion, and maintenance of CTA-related facilities and/or systems, (2) the portion of those costs participants can legitimately recoup from a new entrant, and (3) the costs incurred or to be incurred for modifying systems to accommodate the new participant (which are not otherwise required to be paid or reimbursed by the new participant). The Plan should not otherwise include any subjective criteria, or objective factors designed to compensate for the costs of operating the systems prior to the time the new participant joins the Plan, or for 'goodwill' or any future benefits to the new entrant.[21]

The Commission, in a subsequent action brought by Nasdaq challenging CTA's fees as not having sufficient cost justification, concluded that the entry fees should be "fair and reasonable" and that a rigorous cost-based analysis was therefore required. The Commission said the CTA should employ a "fair and reasonable method" for determining a new participant's entrance fee. The Commission explained that each new participant would pay a "fair share of the costs previously paid by CTA for the development, expansion and maintenance of CTA's facilities."[22] The Commission also stated that the fee should not include "any subjective or intangible costs such as 'good will.'"[23]

The Commission further noted that the CTA had not presented work papers to support its cost calculations and, without such data, the Commission could not properly assess whether CTA's fees were "fair and reasonable" and thus referred the matter to an administrative law judge to preside over the proceeding.[24] This advice was well-grounded in Commission precedent. When the Chicago Board of Options Exchange joined the Plans, an outside consultant was retained to help design an entry fee that would objectively ensure that the new entrant reimburse other Participants only for an appropriate portion of the development costs expended by the facilities.[25]

We believe that the same "fair and reasonable" analysis applied to CTA fees should be applied to the exchanges' market data fees. Without underlying cost data and calculations, the Commission cannot determine, and the public cannot assess, whether such fees are "fair and reasonable."

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21 Letter from Annette Nazareth to Thomas E. Haley, Chairman, CTA (Aug. 3, 2004).

22 *In re Nasdaq Stock Market, LLC for Review of Action Taken by the Consolidated Tape Association*, Exchange Act Release No. 55909 (June 14, 2007) in text at nn. 17-20 [emphasis in original deleted; footnotes omitted] available at http://www.sec.gov/litigation/admin/2007/34-55909.pdf.

23 *Id.*

24 *Id.*

25 Exchange Act Release No. 34-33319 (Dec. 10, 1993).

E. Need for Transparency and Consistency

Transparency has always been a hallmark of the Commission's purpose and motivation, and should also be applied to market data fees. The need for transparency in market data fees is further amplified by the exchanges' for-profit motivation. In connection with efforts to improve transparency in mutual fund fees, Commissioner Nazareth recently stated:

> Transparency and disclosure are imbedded in our statutory mandate and we truly believe in their benefits. Transparency is embodied in virtually all of our regulatory initiatives and this area is no exception. And with good reason. Effective transparency leads to more informed investor behavior and better markets.[26]

To date, market data fees have not undergone the same critical review for transparency as mutual fund fees. By not requiring exchanges to submit underlying cost data, investors cannot assess whether NYSEArca's costs are related to the costs for distributing the data and justify the fees charged to investors for that data in accordance with the Exchange Act.

Although transparency seems critical to its mandate, the Commission has not advanced transparency in the exchanges' market data fees with the same vigor as it has in other contexts. As we have seen recently, the courts take notice when there is a "disconnect" between the Commission's actions and statutory requirements. For example, the Court of Appeals in *Goldstein* rejected the Commission's regulatory regime for hedge funds because:

> [W]ithout any evidence that the role of fund advisers with respect to investors had undergone a transformation, there is a disconnect between the factors the Commission cited and the rule it promulgated. . . . The Commission may not accomplish its objective by a manipulation of meaning.[27]

In contrast, the Commission has at times been convinced of the importance of transparency and mindful of the market power of SROs:

> [C]omprehensive trade and quotation information, even beyond the NBBO, is vital to investors. The Commission remains concerned that an SRO with a significant share of trading in NMS stocks could exercise market power in setting fees for its data. Few investors could afford to do

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[26] Remarks before the Mutual Fund Directors Forum Seventh Annual Policy Conference by Commissioner Annette L. Nazareth (Apr. 12, 2007), available at http://www.sec.gov/news/speech/2007/spch041207aln.htm.

[27] 451 F.3d at 882.

> without the best quotations and trades of such an SRO that is dominant in a significant number of stocks.[28]

Furthermore, we do not believe the Exchange Act envisions for-profit enterprises having carte blanch to exercise market power in ways that diminish the transparency of vital information.

F. SEC Regulation NMS

In adopting Regulation NMS, the Commission determined not to require exchanges to publish their depth-of-book data, reasoning that market forces could be allowed to control that decision. The Commission stated:

> The consolidated information on quotations and trades must be provided in an equivalent manner to any other information on quotations and trades provided by a securities information processor or broker-dealer. Beyond disclosure of this basic information, market forces, rather than regulatory requirements, will be allowed to determine what, if any, additional data from other market centers is displayed. In particular, investors and other information users ultimately will be able to decide whether they need additional information in their displays.[29]

The Commission announced that the exchanges could determine what data below the consolidated information would be made available based on market forces. The SEC did not state that exchanges, having made the decision to publish such data, were thus exempt from complying with the Exchange Act requirements for access to the exchange's facilities, reflected in Sections 6(b)(4) and 11A(c), among other sections. Nor could the Commission have made such a determination lawfully. Exchanges act as "exclusive processors" within the meaning of Exchange Act Section 3(22)(B) when they engage on their own behalf in processing or preparing for distribution or publication *any* information with respect to: "transactions or quotations on or effected or made by means of any facility of such exchange." This is the case regardless of whether they do so voluntarily or under regulatory compulsion, and they have to meet the same statutory standards under Section 11A, without variation. While we are not legally obligated to drive to work, once we get behind the wheel we are subject to traffic laws. The exchange asserts that, being free to determine what data to make public, they are also free of all laws governing that data. This argument is neither logical nor supported by the statute.

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[28] Exchange Act Release No. 51808 (June 9, 2005), in text following n.575.

[29] *Id.* in text following n.650.

G. Market Data Ownership

Any purported rights of ownership in the market data do not alleviate or eliminate the Exchange Act requirements governing market data fees. SIFMA does not agree with Nasdaq's purported "ownership" of non-creative factual data which broker-dealers and investors are required to provide. As NetCoalition noted in its petition, the Supreme Court has rejected copyright claims to non-creative factual data, and Congress has rejected exchange requests to legislate on the issue.[30] Regardless of any ownership claim, sole-source data should be provided on terms that are "fair and reasonable" and not unreasonably discriminatory.

H. Comparisons to Competitive Industries

Nasdaq argues that "fair and reasonable" should be determined by the market-based standard employed by other federal agencies in other industries, including telecommunications, airlines, and railroads. The federal utility agencies Nasdaq cites as examples of using competitively determined market rates as a presumptive test of reasonableness are inapposite to the fees exchanges charge. Unlike those other commodities, exchange market data is unique to each exchange and not interchangeable with other exchanges' market data, as explained earlier.

Nasdaq's analogies to other regulated industries have no bearing for four reasons:

- Nasdaq exchange data is not substitutable for data that pertains to bids and offers on other exchanges, unlike commodities.
- Nasdaq has significant market power with respect to its exchange data unlike the examples cited.
- Nasdaq exchange data is sold to a different set of customers from the customers that pay Nasdaq for listing or transaction fees.
- Regulation creates a barrier to entering the market data industry by compelling market data customers to provide the input materials (bids, offers, order prices) to Nasdaq for free, unlike other industries where raw materials must be purchased.

In all of the examples that Nasdaq cites, the regulatory authorities only allowed market-based rates where, and because, the regulated entity lacked market power. Further, in the deregulation of the telecommunications industry, the FCC treated dominant and non-dominant firms differently in price-setting. Only non-dominant carriers were exempt from providing detailed back-up for their proposed charges, because they could not operate beyond the limits of price, terms, and conditions that the still-regulated dominant firms, such as AT&T, could.[31] In

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[30] NetCoalition petition at 17, citing *Feist v. Rural Telephone Service Company, Inc.*, 499 U.S. 340 (1991).

[31] *MCI Telecom. Corp. v. American Tel & Tel Co.*, 512 US 218, 220-223 (1994).

fact, the FCC did not deregulate AT&T, the dominant interexchange carrier, until it was convinced that the market was workably competitive.[32] The incumbent local exchange carriers remain subject to regulation to protect against their ability to abuse their monopoly power over the 'local loop' to the detriment of competition in the inter-exchange market.[33]

The same holds true for the other examples cited by Nasdaq of federally sanctioned market-based rates in other industries. Each example involved firms that did not have market power operating in a marketplace where the alternatives were reasonably interchangeable and/or there were no barriers to entry. For example, Nasdaq cites the Federal Communication Commission ("FCC") strategy for determining "just and reasonable" rates for telecommunications services. Nasdaq quotes the FCC decision as stating "traditional tariff regulation . . . is not only unnecessary to ensure just and reasonable rates, but is actually counterproductive…"[34] Nasdaq, however, left off a key portion of this quote which states: "traditional tariff regulation *of nondominant carriers* is not only unnecessary…" (emphasis added).[35] This strategy would not apply to Nasdaq's market data, because Nasdaq is the dominant, and the only, provider of its exchange data.[36]

In addition, the energy, telecommunications, and transportation products and services cited by Nasdaq are all sold to a single set of demand-side customers. The exchanges, however, are subject to more than one set of demand-side customers:

Customer Set 1: Transaction *and listing fees* are paid by market participants to Nasdaq.

Customer Set 2: Market data fees are paid by consumers of market data to Nasdaq.

Market data is sold to a different set of customers from those that pay Nasdaq for listing or transaction fees. Competition between exchanges, to the extent that it exists, encourages the exchanges to reduce transaction and listing fees to attract more market participants and generate more orders. Indeed, as transaction fees and listing fees are driven down by intermarket competition, the exchanges will be under pressure to cross-subsidize their operations by increasing market data fees. Thus, intermarket competition does not constrain the exchanges'

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[32] *Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, 11 FCC Rcd 3271 (1995); *WorldCom, Inc. v. FCC*, 238 F.3d 449 (DC Cir. 2001).

[33] *See* 47 CFR Part 61 (2006).

[34] Nasdaq Letter at 12.

[35] *In re Tariff Filing Requirements for Nondominant Common Carrier*s, 8 FCC Rcd 6752, 6752 (1993); vacated on other grounds, Sw. Bell Corp. v. FCC, 43 F.3d 1515 (D.C. Cir. 1995).

[36] Nasdaq's additional examples are equally unpersuasive. The Federal Energy Regulatory Commission decision cited by Nasdaq is based on customers having "genuine alternatives" to the product, which is not the case for market data. Nasdaq Letter at 12. Nasdaq also cites a decision by the Surface Transportation Board which similarly required "effective competition alternatives" which are not available for market data. Nasdaq Letter at 13.

pricing of market data, but it actually creates an incentive for the exchanges to increase their prices for data.[37]

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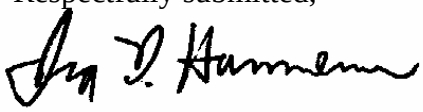
The NetCoalition petition raises legal and policy issues that warrant a comprehensive review of the Commission's rules and procedures for approving market data fees to ensure that – in today's market – there is compliance with the Exchange Act and all investors have fair access to market data. We welcome the opportunity to provide assistance to the Commission and the staff in this matter.

If you have any questions, please contact Ann Vlcek, Managing Director and Associate General Counsel, and Melissa MacGregor, Vice President and Assistant General Counsel, or me at 202-434-8400.

Respectfully submitted,



Ira D. Hammerman
Senior Managing Director and General Counsel

cc: The Hon. Christopher Cox, Chairman
The Hon. Paul S. Atkins, Commissioner
The Hon. Roel C. Campos, Commissioner
The Hon. Kathleen L. Casey, Commissioner
The Hon. Annette L. Nazareth, Commissioner
Dr. Erik R. Sirri, Director Division of Market Regulation
Robert L.D. Colby, Deputy Director Division of Market Regulation
Dr. James Overdahl, Chief Economist
Brian G. Cartwright, Esq., General Counsel

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[37] Nasdaq is correct that the Commission in adopting Regulation NMS had hoped that the rule would lead to lower costs to investors, but the actions of the exchanges have undermined that goal. NYSEArca book data used to be free. Under the rule proposal, there will be a significant new fee that investors and the professionals who serve them will have to pay to access the same data in order to assure they are not placed at an information disadvantage. Nasdaq also argues that Regulation NMS was intended to encourage market data vendors and broker-dealers "to produce proprietary products cooperatively in a manner never before possible." Nasdaq Letter at 9. That has not happened to date, as evidenced by the Petition and the numerous comment letters in support of the Petition.