EXCHANGE MARKET DATA COALITION

AMERICAN STOCK EXCHANGE
◆
BOSTON STOCK EXCHANGE
◆
CHICAGO BOARD OPTIONS EXCHANGE
◆
CHICAGO STOCK EXCHANGE
◆
INTERNATIONAL SECURITIES EXCHANGE
◆
THE NASDAQ STOCK MARKET
◆
NEW YORK STOCK EXCHANGE
◆
NYSE/ARCA EXCHANGE
◆
PHILADELPHIA STOCK EXCHANGE

January 26, 2007

Via Electronic Submission and U.S. Mail

Nancy M. Morris
Secretary
US Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: NetCoalition Petition for Review; Release No. 34-55011

The American Stock Exchange, the Boston Stock Exchange, the Chicago Board Options Exchange, Chicago Stock Exchange, the International Securities Exchange, the NASDAQ Stock Market, the New York Stock Exchange, the NYSE/Arca Exchange, and the Philadelphia Stock Exchange (collectively, the "Exchanges") jointly urge the Commission to affirm the order of the Division of Market Regulation approving SR-NYSEArca-2006-021. The economic and regulatory implications of the Petition for Review filed by NetCoalition ("Petition") are so profound that nine of the nation's registered securities exchanges – ordinarily fierce competitors – have organized this Exchange Market Data Coalition to speak with a single voice against it.

The Petition reflects a basic misunderstanding of the role of exchanges in the economy and the national market system, and how exchanges compete, invest and innovate to produce market data. Competition between exchanges was a cornerstone in Congress's creation of the national market system and has remained a guiding principle in its development during the last three decades. Exchange competition benefits investors by increasing transparency, lowering trading costs, and providing equal access to the best prices in the deepest pools of liquidity of any securities markets in the world. The Petition, in failing to understand the role of exchanges and the competition between them, puts those benefits at risk.

The Petition also overlooks seven years of almost-continuous debate on market data policy which culminated in the adoption of Regulation NMS. The Petition selectively quotes from 1999 and 2004 concept releases for the proposition that the Division of Market Regulation erred by failing to apply the "cost based" standard of review for fee proposals governed by the Securities Exchange Act of 1934. [1] In fact, "cost based" is not the current standard of review, nor has it ever been the standard of review. The Petition ignores the 2001 blue-ribbon panel that considered and flatly rejected the "cost based" standard[2], and the three proposing and adopting releases regarding Regulation NMS[3] in which the Commission specifically considered and refrained from imposing the "cost based" standard NetCoalition now proposes. The Petition would replace Regulation NMS – prior to implementation – with a complex and intrusive rate-making approach that is inconsistent with the goals of the Securities Exchange Act of 1934 and would be more costly than beneficial.

Exchanges Play a Pivotal Role in the US Economy and National Market System

Exchanges perform a unique and vital function at the heart of the United States economy: they provide an efficient, transparent, and well-regulated venue for capital formation. For over 200 years, Exchanges have fed the nation's economic engine by offering businesses an opportunity to showcase their potential and to entice investors to provide them with capital by purchasing their securities. New businesses rely on the Exchanges for initial public offerings that attract public investors for the first time, increase their visibility in the economy, and reward their innovative founders and early supporters. Mature businesses rely on the Exchanges' deep pools of liquidity for secondary offerings that fund continued expansion and strategic initiatives such as mergers and acquisitions.

Millions of public investors rely on the Exchanges to safeguard their economic futures. Each day on the Exchanges, billions of shares representing trillions of dollars of capital are exchanged on behalf of public investors by broker-dealers with individual investors' accounts, by mutual funds that hold pools of investors' funds, and by the companies in which individuals invest. Whether they are aware of it or not, public investors rely on the Exchanges, secure in the knowledge that the companies whose shares they purchase are sound, that the prices paid for those shares are fair, and that shares purchased from unknown sellers will arrive without fail.

---

1 Securities Exchange Act Release No. 42208 (Dec. 14, 1999) ("Market Data Concept Release"); Securities Exchange Act Release No. 50699 (Nov. 18, 2004) ("SRO Concept Release").

2 *Report of the Advisory Commission on Market Information*, Sept. 14, 2001 ("Seligman Report") at text accompanying fn. 276 ("There was widespread agreement among Advisory Committee members that a cost-based approach is both unnecessary and impractical").

3 Securities Exchange Act Release No. 51808 (June 9, 2005) ("Reg NMS Adopting Release").

Exchanges build and maintain costly trading floors, electronic systems, and surveillance systems to ensure that all investors have access to fast, fair, efficient, low-cost trading in a well-regulated trading environment. Thanks to the Exchanges' record of reliability, the effort, care and expense necessary to operate an Exchange and the value that Exchanges add to securities trading is largely hidden from the general public on whose behalf the trading occurs. Every aspect of the Exchanges' operations –- from the issuers they list, to the members granted quoting and trading privileges, to the trading facilities and systems themselves – is the product of years of development, investment, and experience devoted by the Exchanges to benefit investors.

The end product of these efforts – the listings, the members, the trading facilities, the regulation – is market data. Market data is the totality of the information assets that each Exchange creates by attracting order flow. It includes everything from basic quotation and transaction information familiar to most investors, to sophisticated data products tailored mainly to professional and algorithmic traders – and everything in between. Market data is the public face of the Exchanges, appearing in millions of newspapers, television sets, and computer screens every second of every minute of every trading day, day in and day out without fail.

Exchanges Compete and Innovate To Produce Market Data

Market data is critical to competition between the Exchanges, for while Exchanges are in the business of helping business, they are also businesses themselves. Like all businesses, the Exchanges exist to produce products and services and to provide them to willing consumers to further their business objectives. Like all businesses, Exchanges fight for survival and primacy by offering more desirable products and attracting more buyers than their competitors.

Exchanges have operated as businesses and competitors of one form or another for over 200 years. For much of their 200-year history, Exchanges operated as not-for-profit membership organizations, meaning they were owned and operated by their members solely for the benefit of their members. Beginning in the late 1990's, exchanges in the US and abroad began "demutualizing" or separating themselves, in terms of ownership, from their members to operate independently and for profit. Most demutualized exchanges have taken the additional step of taking on investors, either privately or through initial public offerings.

As Exchanges have evolved in form and ownership, competition has intensified. Competition among the exchanges is waged along three lines: listings, transactions, and market data. Listings are the *sine qua non* of the national market system. Listings create the opportunity for trading by competing markets on an unlisted trading privileges ("UTP") basis, which, together, generate quotes and trades, and, in turn, market data. Exchanges compete for listings by offering a mix of services, including a high quality brand image, attractive pricing, and attentive customer service.

Increasingly, Exchanges compete for listings with foreign exchanges. The U.S. securities markets have historically been the envy of the world, attracting issuers and investors from around the globe on a scale unmatched by international exchanges. That equation is rapidly changing, and the nature of exchange competition is changing along with it.

In addition to competing for listings, exchanges must also compete to execute trades in the securities of listed companies. Congress and the Commission have determined that an effective way to promote competition among the Exchanges, and thereby benefit investors, is to permit each exchange to trade any security listed on any other exchange via "unlisted" trading privileges. Thus, Exchanges compete not only with one another, but also with broker dealers that match customer orders within their own systems and also with a proliferation of alternative trading systems ("ATSs") and electronic communications networks ("ECNs") that the Commission has also nurtured and authorized to execute trades in any listed issue. As a result, market share of trading fluctuates among execution facilities based upon their ability to service the end customer. The execution business is highly competitive and exhibits none of the characteristics of a monopoly as suggested in the NetCoalition Petition.

The undersigned Exchanges are funded in varying ways and thus rely to varying degrees on market data revenue as a funding source. Because the law does not mandate a particular funding stream for exchanges, how exchanges are funded is a matter of business strategy for each exchange to determine and a basis on which the exchanges can and should compete. This includes, therefore, determining how to best promote and utilize market data within the applicable legal and regulatory framework. It is in each Exchange's best interest to provide proprietary information to investors to further their business objectives, and each Exchange chooses how best to do that. Market data is pervasive and affordable. Exchanges continue to innovate to meet the changing data needs of their customers. Success will be determined by the marketplace.

As the Commission has expressly acknowledged, competition among market centers is an essential cornerstone of the national market system, to the direct benefit of the investing public:

> Vigorous competition among markets promotes more efficient and innovative trading services, while integrated competition among orders promotes more efficient pricing of individual stocks for all types of orders, large and small. Together, they produce markets that offer the greatest benefits for investors and listed companies.[4]

[4] *See* SEC Release No. 34-51808, 70 F.R. 124 (June 29, 2005), promulgating the final Regulation NMS rules.

Indeed, Regulation NMS was designed to foster competition among markets. As the Commission noted, "[t]he NMS is premised on promoting fair competition among individual markets."[5] Particularly with respect to market data, the rule has already yielded positive results in the form of new market data products that have been made available to consumers. Ironically, the Petition has resulted in preventing these types of new market data products from reaching consumers.

Although the Exchanges vary in terms of their respective revenue sources and the allocation thereof, each Exchange certainly considers market data to be a significant product of their core business and an appropriate means to fund operations, including key regulatory activities, and to pursue important strategic initiatives. In short, revenue fosters innovation, which in turn is essential to healthy competition.

It is also relevant that the Petition was submitted by a coalition whose members stand to gain financially if they are successful in using the government to reduce or eliminate their access costs to market data from Exchanges. Each NetCoalition member wishes to use Exchange market data to further its own business models. Some wish to lower or eliminate their content acquisition costs while others wish to free-ride on Exchange prices to internalize order flow, effectively competing with the very same Exchanges whose data they use to price their customer orders. If the Commission were to grant the Petition, and entertain considerations advanced by the NetCoalition regarding market data fees, the resulting impact on the Exchanges would be significant, with the certain result of reducing innovation and competition among markets, to the detriment of the investing public. The resulting impact to the NetCoalition members would also be significant by improving their financial results.

The Commission Rule-making Process Is Critical

The current rules regarding market data dissemination are the culmination of seven years of nearly continuous Commission-sponsored debate on market data policy. The Petition largely ignores that debate. It selectively quotes from the 1999 Concept Release on Market Information and mentions the 2004 concept release on self-regulation of exchanges but it fails to note that those releases provoked strenuous objections and that the Commission never adopted the "cost based" standard NetCoalition supports. The Petition states that the Division of Market Regulation erred by failing to apply a "cost based" standard of review to the NYSE/Arca proposal but it ignores the 2001 blue-ribbon panel that considered and flatly rejected the "cost based" standard.

It also largely ignores Regulation NMS, which followed a proposal and re-proposal process that sparked a comprehensive dialogue on market data policy. That process produced a balancing of interests concerning the appropriate modifications to the national market system, and recognized, for the first time, that promoting the wide availability of market data by specifically authorizing markets to distribute their own data

5 *Id.*

independently would benefit all investors. It recognized that market-based solutions, not regulatory mandates, would best serve investors.

In fact, it is no surprise that in light of the nearly unanimous support of the Exchanges, the Commission specifically proclaimed its agreement that the self-regulatory organizations and their members should be allowed to distribute their trade data independently. In light of the interests of retail investors, the Commission defined the consolidated display requirements as basic, top-of-book quotations or "core data" (*i.e.* prices, sizes, and market center identifications of the national best bid and offer ("NBBO")) and emphasized that it "believes that markets should have considerable leeway in determining whether, and on what terms, they provide additional non-core data to a Network processor."[6] The Commission expressly understood that market forces, as opposed to regulatory requirements, would best determine what – and under what conditions – additional data outside the NBBO should be displayed to investors.[7] The Commission should adhere to the principles of Regulation NMS and the rule authorizing markets to distribute their market data independently.

The Exchange Market Data Coalition respectfully urges the Commission to affirm the order of the Division of Market Regulation approving SR-NYSEArca-2006-021.

Respectfully submitted,

The American Stock Exchange

The Boston Stock Exchange

The Chicago Board Options Exchange

The Chicago Stock Exchange

The NASDAQ Stock Market

The New York Stock Exchange

The NYSE/Arca Exchange

The Philadelphia Stock Exchange

The International Securities Exchange

---

6 *See* note 2, *supra*, at p. 279.

7 *Id.* at 272-3.