SIFMA
Securities Industry and Financial Markets Association

March 5, 2007

U.S. Securities and Exchange Commission
100 F Street N.E.
Washington DC 20549-0609
Attention: Nancy M. Morris, Secretary

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

Dear Chairman Cox and Commissioners:

The Securities Industry and Financial Markets Association ("SIFMA")[1] again would like to express its appreciation for the Securities and Exchange Commission's ("Commission" or "SEC") unanimous decision to grant the NetCoalition petition ("Petition")[2] to review the Staff's approval of NYSE Arca LLC's ("NYSE Arca") market data fees under delegated authority. We have thoroughly addressed the issues raised by the Staff's order of approval and the petition in our letter dated January 17, 2007, in response to the Commission's request for statements on the Staff's action.[3] We are submitting this additional letter, however, to respond to letters subsequently filed by NYSE Arca and the new "Exchange Market Data Coalition."[4]

I. REASON FOR ADDITIONAL COMMENT

The fact that NYSE Arca and the Exchange Market Data Coalition either have ignored or glossed over the points we and other commentators have raised underscores the wisdom of the SEC in granting this review, which we believe is essential to facilitating a thorough examination of the relevant issues, including:

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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, and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

[2] Petition by NetCoalition re: Securities Exchange Act of 1934 ("Exchange Act") Release No. 54597 (Nov. 14, 2006).

[3] Comment Letter from SIFMA re: In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21 (Jan. 17, 2007).

[4] Comment Letter from NYSE Arca Response to NetCoalition Petition for Commission Review of SR-NYSEArca-2006-21 (Feb. 6, 2007) ("NYSE Arca Response"); Comment Letter from Exchange Market Data Coalition re: NetCoalition Petition for Review; Release No. 34-55011 (Jan. 26, 2007) ("Exchange Market Data Coalition Response").

- The lack of both economic market forces and comprehensive oversight of the exchanges as the sole-source exclusive processors of market data, which has allowed the exchanges to simply "name their prices" and thereby stifle incentives for the exchanges to innovate in this area (and preclude others from doing so as well);

- The imposition of excessive fees on broker-dealers, vendors, and investors by exchanges through the sale of needed but non-innovative products, which consist of nothing more than packaged quotation and limit order facts that the broker-dealers are required by regulation to give to the exchanges;

- The aggregate number and size of market data costs exchanges now seek to impose on market participants, which are growing at an alarming rate without comprehensive oversight (see Appendix A);

- The failure to meet the statutory standard that fees be reasonable and therefore reasonably related to cost, much less to publicly disclose any cost data whatsoever to inform Commission decision-making or public comment;

- The conflicts generated by the emergence of for-profit exchanges and their exploitation of their regulatory status to charge inflated prices for increasingly essential yet basic factual information about current stock quotations reported to their market;

- The anti-competitive potential of increasingly consolidated markets;

- The importance of depth-of-book quotation data to all investors after decimalization and Regulation NMS;

- The impact on investors and the professionals who serve them of effectively denying them access to faster depth-of-book quotation data, which results in reliance on slower top-of-book or last sale data to their trading and execution disadvantage; and

- The failure of NYSE Arca (and the other exchanges who support NYSE Arca's position) to respond to the issues raised in the petition or in SIFMA's January 17th letter concerning the Commission's statutory obligation to articulate clear standards and then determine whether the challenged fees are "fair and reasonable" and "not unreasonably discriminatory," and represent a "fair allocation" of NYSE Arca's fees under those standards.

While we will not repeat the extensive comments in SIFMA's January 17th letter, NYSE Arca and the Exchange Market Data Coalition subsequently made a series of arguments that require rebuttal in that they are irrelevant, misleading, or not supported by the facts and sound economic analysis. We first will address below three frivolous procedural issues raised by the exchanges, and then will address certain substantive issues.

II. THE PETITION IS NOT MOOT, STANDING IS NOT AN ISSUE, AND THE COMMISSION HAS THE RIGHT TO REVIEW STAFF ACTIONS DE NOVO

The petition is not moot. NYSE Arca argues that the petition is moot because NYSE Arca has now offered an NYSE Internet proposal that provides internet service providers with unlimited real-time last sale prices for a fixed price. This argument is irrelevant because it is premised on a completely different type of data. The NYSE Arca fees that are contested in this proceeding involve real-time depth-of-book quotations. Any attempt to placate the petitioner with a very different market data product that has a very different purpose for professionals and investors is not an answer to the underlying policy issues that the petitioner and SIFMA – as well as the Financial Services Roundtable, American Bar Association, and others – have raised with respect to sole-source depth-of-book data.[5] Likewise, NYSE Arca's discussion of nonprofessional subscriber fees that were set over six years ago for top-of-book *consolidated* data is completely irrelevant.

Standing is not an issue. NYSE Arca argues that NetCoalition does not have standing to petition the Commission. We disagree. NetCoalition's members have tens of millions of customers who invest in our markets who are impacted by the issues raised in the petition. The exchanges' argument that NetCoalition lacks standing is also irrelevant in light of the Commission having already granted the petition for review. In response to the SEC's request for statements in support or opposition of their order by delegated authority, SIFMA – which undeniably has standing to participate[6] – has joined in opposing the Staff's action by delegated authority in approving the NYSE Arca depth-of-book fees ("Arca Book Fees").

The Commission has the right to review Staff actions approving Exchange filings. Equally without merit is NYSE Arca's attempt to parse the precise scope of statutory delegation of authority to the Staff. The fact is that the Staff "approved" NYSE Arca's rule change to implement the new Arca Book Fees that was the pre-condition to NYSE Arca's authority to charge those fees. NYSE Arca tries to distinguish "approval" from "findings," which it says were made by the Commission itself. In addition to the fact that no cost data or economic analysis were made part of the public record, it is clearly unnecessary to continue to argue over the definition of "approve" or how that relates to "findings" that underlie the approval. The Commission found that it was appropriate to exercise its inherent authority to review the basis for the Staff's action under delegated authority.

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[5] As NetCoalition itself informed the Commission regarding the last sale proposal: "The proposed rule, however, does not lessen the need to address the critical, underlying issues regarding the cost and availability of monopoly market data that are the subjects of the NetCoalition petition. While the discussions that led to this proposal are a positive development, it does not lessen the need to address the critical underlying issues regarding the cost and availability of monopoly market data." Comment Letter from NetCoalition re: In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21 (Jan. 17, 2007).

[6] See Comment Letter from SIFMA re: In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21 (Jan. 17, 2007) at 12 and note 22. NYSE Arca itself recognized that "[T]he market for Arca Book quotations, and therefore the individuals and organizations that the Arca Book Fees will directly impact, are the broker-dealer members of NYSE Arca and other market professionals and institutional investors." NYSE Arca Response at 8.

III. THE ABSENCE OF BOTH COMPREHENSIVE REGULATORY OVERSIGHT AND ECONOMIC MARKET FORCES IN SETTING THE PRICE OF SOLE-SOURCE MARKET DATA FROM THE EXCLUSIVE PROCESSOR INFLATES MARKET DATA PRICES AND DISCOURAGES INNOVATION

Allowing the exchanges to "innovate" in the market data area is a theme that emerges in many of the exchange letters as a way to justify inflated market data fees unrelated to costs of aggregating and distributing the data. This argument is misguided. For decades, the exchange function has been described as "price discovery," not "price creation," and there is a good reason for this description. Exchanges do not create data; rather, (i) market data is merely a necessary input for the exchange's primary business – which is trading, and (ii) this input is created by investors in conjunction with their broker-dealers and only then is it provided to the exchanges – for free, as required by law. There is little innovation in the NYSE Arca market data product or any other depth-of-book data products. The value of depth-of-book data comes not from an exchange's innovation in terms of creating a new "product," but rather from the exchange's regulatory *uniqueness* arising from its exchange status as an *exclusive* processor of data registered with and regulated by the SEC. To an investor who needs NYSE Arca data to access current quote pricing information and to understand what is happening in the market for a given security (*i.e.*, transparency), the availability of another exchange's depth-of-book product may be irrelevant. One exchange's depth-of-book data does not substitute for another's; that is why it is "exclusive."

Nonetheless, NYSE Arca argues that market forces alone should be trusted to establish and regulate the price of market data, claiming that "[i]n the realm of proprietary market data products, the laws of supply and demand provide an appropriate basis for determining whether fees are fair and reasonable."[7] The Exchange Market Data Coalition Letter is also premised on the theory that repeating the phrase "market forces," while telling the government to move out of the way, constitutes a formula to make Adam Smith proud. Exhortations to "let the markets work," homage to "market-based solutions," and warnings that these market forces work only when "unencumbered by industry regulation" pervade the NYSE Arca submission.

The National Stock Exchange, in stark contrast, has had the integrity and foresight to place the public interest above its own short-term economic interest to refute the arguments made in the Exchange Market Data Coalition and NYSE Arca submissions:

> The Exchange Market Data Coalition has stated in its comment letter that "each Exchange certainly considers market data to be a significant product of their core business . . . and that "revenue fosters innovation." NSX disagrees with these statements. In our view, it is competition, or the opportunity for competition, that fosters innovation – not revenue.[8]

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[7] NYSE Arca Response at 5.

[8] Comment Letter from National Stock Exchange re: In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21(Feb. 27, 2007) ("NSX Response") at 2 (attached as Appendix B).

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> NSX believes . . . that fair and free access to basic market information [such as depth of book data] certainly benefits investors. By allowing more potential participants to deliver innovation to the industry, fair and free access to basic market information will provide the entire U.S. securities market a competitive advantage globally.[9]

SIFMA applauds the NSX for its comments in the public interest and its willingness to relinquish the exchanges' "excessive markup" for market data. The comments of the NSX reflect the "white elephant in the room" that there is no source for obtaining the NYSE Arca Book other than from NYSE Arca. Every vendor, Internet portal, or broker-dealer must obtain that data from NYSE Arca; however, NYSE Arca claims that the appropriate market under review is the competition for order flow between other market centers and NYSE Arca.[10] Although that may be how NYSE Arca views its use of market data – as a lever to use in a market where it does face competition – the proper economic analysis should focus on how the market for the product (for which the supplier is charging) operates from the consumer's perspective. When it comes to single exchange market data like NYSE Arca's Book Data, there are no market forces at work in the transaction between the exchange and the consumer, whether that consumer be a vendor, an investor, an Internet portal, or a broker-dealer. It is a sole-source product.

The exchanges' attempt to leverage their regulatory position to charge inflated prices for non-innovative products would not surprise Congress, which understood the dangers of exclusive processors and charged the Commission with guarding against abuse:

> [S]erious antitrust questions would be posed if access to this facility and its services were not available on reasonable and non-discriminatory terms to all in the trade, or if its charges were not reasonable. Therefore, in order to foster efficient market development and operation and to provide a first line of defense against anti-competitive practices, Sections 11A(b) and (c)(1) would grant the SEC broad powers over any exclusive processor and impose on that agency a responsibility to assure the processors' neutrality and the reasonableness of its charges in practice as well as concept.[11]

Likewise, the absence of market forces and need for oversight have not surprised the Commission. The Commission is wisely exercising its oversight powers granted to it by Congress to address the exchanges' abusive practices in charging excessive fees for market data, which are simply an aggregation of quotation facts and not an innovative "product." In the

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[9] NSX Response at 4.

[10] NYSE Arca Response at 16.

[11] *Securities Acts Amendments of 1975*, Report of the Senate Comm. On Banking, Housing and Urban Affairs to Accompany S. 249, S.Rep. No. 94-75, 94th Cong. 1st Sess. 11-12, 1975 U.S.C.C.A.N. 179 (1975).

release adopting Regulation NMS, 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 of an SRO on an exclusive basis.[12]

That is, a national securities exchange that is the exclusive source of the data it distributes with respect to Regulation NMS stocks is subject, under Regulation NMS, to Exchange Act standards because of the very absence of market forces. While Regulation NMS may envision market forces driving innovation, the Commission clearly intended for sole-source market data products to be regulated as described above. This is because the presence of competition in the listing market or in the order execution market does not mean that there is competition or innovation in the market data market dominated by exclusive processors.[13]

NYSE Arca as an exchange is clearly acting as an exclusive processor as defined in Section 3(a)(22)(B) of the Exchange Act.[14] As NYSE Arca itself admits in its response to the

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

[13] While we have focused our discussion on the absence of "market forces" in the context of sole-source depth-of-book products, obviously there is a lack of "market forces" as well in the context of sole-source information that is tied into other products. In this regard, the NetCoalition petition, NetCoalition's submissions before and after the Petition, and SIFMA's submissions before and after the Petition also raise objections to the Nasdaq Analytics Package and the Trading and Compliance Data Package. Despite the enormous controversy surrounding these products – and despite the fact that the SEC had expressly rejected the Nasdaq Trading and Compliance Package only six months prior – the NASD designated the Nasdaq Trading and Compliance Package and the Nasdaq Analytics Package filings as "non-controversial" under Section 19(b)(3)(A) thus providing that these contentious proposals would be immediately effective upon filing. This process, of course, precludes meaningful public comment. These products contain regulatory data and other data that the exchanges receive in their regulatory role and are now marketing by tying them into commercial products. As no other entity has access to the underlying data, there can be *no* competitive product. There are no "market forces" when a regulator simply leverages its control of data downstream into a new market under conditions that make competition impossible. This is a structure designed to thwart innovation.

[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: "[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).

petition,[15] it is therefore subject to both the “fair and reasonable” standard of Rule 603(a)(1) and the “not unreasonably discriminatory” standard of Rule 603(a)(2). The Commission has repeatedly stated that the "fair and reasonable," "not unreasonably discriminatory," and "equitable allocation” of costs standards are the relevant tests for evaluating exchange market data rule filings.[16] Although NYSE Arca agrees that these standards apply, it nonetheless argues that because it faces competition in a different market – the market for order flow – it should be relieved from having to demonstrate how it meets these standards when it comes to fees it charges for quote data. This is a specious argument because the economic premise is wrong.

Normal market forces cannot be relied upon here because of the unique structure of the market for data that the exchanges compile from their captive broker-dealer customers and then sell back to them. As NSX observed in its comment letter, “until the market data fee structure is reformed, broker-dealers will still be forced to purchase market data at a fixed and, we believe, arbitrary price.”[17]

That is certainly what happened in this case. Before Archipelago and NYSE merged, Archipelago was praised for its decision to give away its limit order book data – by none other than the NYSE itself. This occurred back in 2000 during a meeting of the Advisory Committee on Market Information (“Advisory Committee”), after Gerald Putnam, then Chief Executive Officer of Archipelago (NYSE Arca’s predecessor) and now Vice-Chairman of the New York Stock Exchange, charged that “the New York Stock Exchange is the first one at the table complaining when a handful of ECNs decide to give away their quotes to Yahoo Finance.”[18] Robert G. Britz, Group Executive Vice President of NYSE, responded that, to the contrary, “[w]e applaud Archipelago giving out its limit order book to Yahoo and any other distribution means it cares to.”[19] For-profit incentives have changed the exchanges’ attitudes and policies regarding how they treat the market data for which they are the sole-source

In 2001, the Commission also praised Archipelago’s practice of making its book data available to the public without charge (the practice NYSE Arca now proposes to eliminate) as a freely available facility of the Pacific Exchange: “The Commission also believes that the real-time dissemination of the Arca Book to the public via the internet will provide valuable information to all market participants and is reasonably designed to promote price discovery.”[20]

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[15] *See* NYSE Arca Response to NetCoalition Petition (Nov. 6, 2006) at 4, as cited in the SIFMA letter dated Jan. 17, 2007 at fn 13.

[16] *See e.g.*, Market Data Concept Release, Exchange Act Release No.42208 (Dec. 9, 1999) at fn 47.

[17] NSX Response at 2.

[18] SEC Advisory Committee On Market Information, transcript of meeting (Oct. 10, 2000) at 26, prepared by Diversified Reporting Services, Inc. (“Advisory Committee Transcript”) available at http://www.fisd.net/mdregulation/111000_sectrans.pdf.

[19] *Id.*

[20] Exchange Act Release No. 44983, 66 Fed. Reg. 55225, at 55236 (Oct. 25, 2001).

When NYSE acquired Arca and combined Arca's liquidity pool with its own, it ended the depth-of-book dissemination policy that had garnered so much praise from both the NYSE and the Commission. It now seeks to introduce a fee for the same data without any cost information, economic analysis, or analysis on the impact on investors to support the fee's alleged fairness or reasonableness. (We emphasize that, as explained in our January 17th letter, we do not oppose an exchange charging for access to its data; however, we believe that any such fee must be supported by cost information and analysis as provided by statute.) Inexplicably, NYSE Arca actually argues in the NYSE Arca Response that *"the establishment of Arca Book Fees represents the epitome of competition*. It reflects the interplay of market forces at work."[21] Under this Orwellian logic, increased market concentration that allows the dominant U.S. exchange group to impose any charges it wants for data, which its captive broker-dealer customers must provide and which its erstwhile competitor had given away for free, is somehow pro-competitive.

What the Commission is faced with today are all the elements of a perfect storm – creating a classic economic market failure – that requires comprehensive regulatory intervention to ensure "fair and reasonable" prices. The merger has enhanced the networking effect of the NYSE Group's *combined* pool of liquidity, resulting in greater market power over its pricing for market data. Investors and other market participants need the depth-of-book information to trade effectively in today's decimalized world, while at the same time there is information asymmetry between NYSE Arca's detailed knowledge of the liquidity on its book at any given time and investors' inability to accurately place a value on that information "product" without seeing it, which they cannot do unless they are willing to buy it in the dark. Coupled with the regulatory requirements of best execution, discussed below, we are not witnessing the typical interplay of market forces at work.

Finally, NYSE Arca's assertion that its Arca Fees compare favorably with the level of fees charged by other major U.S. exchanges for similar market data products does not satisfy the "fair and reasonable" test because the same market failure applies to such exchanges as well.

IV. NYSE ARCA'S RELIANCE ON THE SELIGMAN COMMISSION REPORT TO ARGUE THAT THE COMMISSION ITSELF HAS REJECTED COST AS A FACTOR IN DETERMINING "FAIR AND REASONABLE" FEES IS WRONG AS A MATTER OF FACT AND LAW – AND NYSE ARCA'S PROPOSALS REQUIRE COST DATA

NYSE Arca argues that the Commission has not mandated cost-based pricing. It dismisses the Commission's support for cost-based pricing in its 1999 Concept Release on Market Data Fees and Revenues[22] as one isolated instance of Commission support for the concept, saying that "neither Congress nor the Commission has ever adopted such a standard"

[21] NYSE Arca Response at 19.

[22] SEC Concept Release: Regulation of Market Information Fees and Revenues, Exchange Act Release No. 42208 (Dec. 9, 1999).

and that the Advisory Committee subsequently "rejected the concept of cost-based pricing."[23] This is not a fair representation of the Advisory Committee's Report, or of its significance.

The Advisory Committee's Report, issued on September 14, 2001, was never adopted by the SEC and the Advisory Committee's members were far from unanimous in their recommendations. The Report provided insufficient clarity and no real consensus positions, and cannot be relied on to guide our current deliberations. Moreover, the Advisory Committee's work pre-dated the NYSE's conversion into a publicly-held for-profit company that competes with vendors of market information as well as with its members in the provision of downstream trading venues. Nevertheless, looking ahead, the Advisory Committee noted that "[s]ome Advisory Committee members expressed concerns that the rise of publicly-held for-profit exchanges, and their obligation to maximize shareholder value, will put upward pressure on market data fees." The Committee went on to advise the Commission that it "may want to be more vigilant in assuring that a for-profit SRO's market data fees meet the statutory 'fair and reasonable' standard."[24]

Indeed, one need only look to the Commission's proposed Regulation SRO (the Commission's most recent effort to address the issue of market data fees) to see that the matters addressed by the Advisory Committee Report are very much in play and that the Commission has taken very seriously the Committee's advice to remain vigilant. In the Concept Release proposing Regulation SRO, the Commission observed, (i) "many" commentators to Regulation NMS stated that market data fees should be tied to costs, and (ii) "to provide greater transparency of SRO revenue and expenses, the Commission is proposing in the SRO Governance and Transparency Proposal to require SROs to file with the Commission public reports . . . [which] could empower users to respond to market data fee changes on a more informed basis."

Similarly and in response to "the concerns raised in response to proposed Regulation NMS regarding market data fees," among others, the SEC sought comment on Regulation SRO as to such questions as whether market data fees limit investor access, "why certain market data fees are more problematic than others, such as those associated with SRO data products that are not part of the consolidated quote stream," "[o]n a conceptual basis, what should be included in the cost of generating market data?" and "[s]hould the Commission require that all SRO fees and charges be closely related to the cost of the SRO providing the service in question?"[25] Clearly, potentially excessive market data fees and recognition of the fact that there often is a lack of innovation associated with market data products remain issues that are still foremost on the SEC's mind, as they acknowledged in Regulation SRO and in taking the extraordinary step of granting this petition.

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[23] NYSE Arca Response at 14.

[24] Report of the Advisory Committee on Market Information: A Blueprint for Responsible Change (Sept. 14, 2001).

[25] Concept Release Concerning Self-Regulation, Exchange Act Release No. 50700, 69 Fed. Reg. 69256, at 71274-75 (Dec. 8, 2004).

Moreover, there is already a significant precedent, which is very relevant to this proceeding, in which the Commission emphatically embraced the cost-based approach to setting market data fees in circumstances impacting competition between a market center that is the exclusive processor of the data it collects and distributes, and its customers seeking access to that data to offer a competitive service. In the 1980 *Instinet* case,[26] the Commission evaluated a market information fee in a denial of access proceeding involving a dispute between the NASD and Instinet over the sale of a market data product where NASD and Instinet were competing against each other. NASD had proposed to charge Instinet a fee based on the fee it charged its own individual subscribers, thereby charging a retail price to a competitor in the wholesale market. The Commission rejected NASD's use of value-of-service pricing, insisting on strict cost-based justification for its market data fees. The Court of Appeals for the D.C. Circuit affirmed the Commission's decision, stating that avoidance of cross-subsidization of services is a legitimate reason for requiring difficult cost allocations and that the difficulty of allocating costs does not provide an excuse for refusing to do so.[27]

The Commission and the Court's reasoning apply fully to the NYSE Arca Fee. Without credible cost data, there is no way for the Commission to be sure that NYSE Arca is not using its market data revenues to cross-subsidize its other services that are competitive. Moreover, broker-dealers and others, who have no place to go other than NYSE Arca for the depth-of-book quotation data compiled by that exchange, are both the exchange's captive customers and their competitors in the execution of transactions. NYSE Arca emphasizes the highly competitive nature of the downstream transaction market. This is precisely the reason why the Commission must be especially vigilant in requiring cost justification for NYSE Arca's depth-of-book fees. There is no other way the Commission – and the investors whom it protects – can be sure that NYSE Arca is not using its market power in the upstream data market as the exclusive processor for this data in order to price squeeze its competitors in the downstream transaction market and to cross-subsidize its reduction in transaction fees.

The Exchange Coalition's submission in this proceeding inadvertently underscored the need for full transparency of the exchanges' costs when it observed that "Exchanges build and maintain costly trading floors…the effort, care and expense necessary to operate an exchange . . . is largely hidden from the general public."[28] The Exchange Act does not envision that these "largely hidden" costs should be paid for by a captive rate-base, in an act of faith in these now for-profit entities. Nor do the Exchange Act's "fair and reasonable" and "equitable allocation" standards guarantee that revenue from market data sales fill the breach when events curtail other sources of revenue, or guarantee that an exchange's percentage of revenue from market data sales be fixed, as argued by NYSE Arca.[29]

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[26] Exchange Act Release No. 20874 (April 17, 1984), 49 FR 17640 (April 24, 1984), affirmed in NASD, Inc. v. SEC, 801 F. 2d 1415 (D.C. Cir. 1986).

[27] *Id.*

[28] Exchange Market Data Coalition Response at 3.

[29] NYSE Arca Response at 12 and fn 29.

Finally, NYSE Arca's own attempt to justify its proposed fee as meeting the statutory standards requires the provision of cost data, which is absent from the public record. NYSE Arca claims that it must use the fees to "enable [it] to recover the resources that NYSE Arca devoted to the technology necessary to produce Arca Book data", and that it considered "the contribution that revenues accruing from Arca Book Fees would make toward meeting the overall costs of NYSE Arca's operations."[30] NYSE Arca fails to provide any data to substantiate these claims. In fact, one would have thought that the marginal cost to NYSE Arca of implementing a depth-of-book product using its existing infrastructure already funded amply by consolidated book and other market data revenue would be *de minimis*. This is especially true where NYSE Arca or its predecessor already had distributed the product free of charge for a long period of time. In the absence of cost data relating to the necessary technology, and in the absence of cost data relating to how market data relates to the overall costs of NYSE Arca's operations, there is insufficient basis to approve NYSE Arca's proposed fees.

V. NYSE ARCA'S OPINION THAT BROKER-DEALERS DO NOT NEED DEPTH-OF-BOOK QUOTE INFORMATION TO SERVE INVESTORS IN OBTAINING BEST EXECUTION FAILS TO JUSTIFY ITS PROPOSED FEE

NYSE Arca opines that only top-of-book consolidated quotation data is required for best execution purposes, not depth-of-book quotes. We find it to be curious how NYSE Arca changed its characterization of its depth-of-book products after the SEC granted the petition for review:

> April 6, 2006:
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> "In response to customer demand for depth-of-market data, we've created NYSE OpenBook Real-Time, a new standard in real-time market information with transparency for stocks trading on the NYSE market," said Ron Jordan, Senior Vice President, Market Data. "Innovative products like OpenBook Real-Time, are what investors want and need in today's marketplace."[31]
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> January 19, 2007:
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> "We believe our depth-of-book information is very valuable," said Ron Jordan, senior vice president of market data at NYSE Group. "It is expensive to maintain, it is expensive to distribute." He added that "depth-of-book information is needed by only a small percentage of professional traders, and we think almost no individual investors. It's not something everybody needs."[32]

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[30] *Id.* at 12-13.

[31] http://www.nyse.com/Frameset.html?nyseref=http%3A//search.yahoo.com/sear

[32] http://foxnews.smartmoney.com/news/on/index.cfm?story=ON-20070119-000956

The first statement starkly illustrates how the exchanges are using their regulatory status to merchandise depth-of-book data as the “standard” for “transparency” which is “what investors . . . need.” The subsequent contradictory statement seems expedient at best, especially in light of the comment letters filed in this proceeding, as well as the 144 comment letters filed in the recent Nasdaq depth-of-book integration proceeding involving the former Instinet book data.[33]

To the extent this data is vital to broker-dealers and investors – as NYSE Arca argued prior to this proceeding – broker-dealers and their customers will suffer the consequences in not being able to access it on fair and reasonable terms. Obtaining order execution at the best reasonably available quote is not just a regulatory liability issue. It is a matter of how broker-dealers attempt to best serve their customers in fairly competing against other market participants in the buying and selling of securities.

NYSE Arca’s more recent casual dismissal of the importance of depth-of-book data is also at odds with the statements of the NSX cited above, earlier statements by Mr. Putnam before the merger, and the NYSE Group in its prospectus. In the Advisory Committee meeting referred to earlier, Mr. Putnam had this to say:

> “We think that transparency is key. A consolidated quote is great, but in the decimalized world that we're moving into, NBBO alone is not going to be good enough anymore. We're going to have to see a lot more prices in-between what's current, a sixteenth world in order to see the same aggregated liquidity in a decimalized world. So NBBO plus limit order book is going to be critical.”[34]

And, the NYSE itself linked its single-market depth-of-book market data and best execution when it stated that “NYSE Arca’s market data products are designed *to improve trade execution*.”[35]

VI. THE EXCHANGES’ ATTEMPT TO COMPARE THEMSELVES TO “UNENCUMBERED” DATA INTERMEDIARIES IS BASELESS

The Exchange Market Data Coalition asserts that "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 … [and] success will be determined by the marketplace."[36] NYSE Arca laments that "Congress and the Commission regulate the market data fees, but allow the intermediaries to

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[33] File Nos. SR-NASDAQ-2006-053, and SR-NASDAQ-2006-013; see Comment Letter from SIFMA re: File Nos. SR-NASDAQ-2006-053, and SR-NASDAQ-2006-013 (Feb. 12, 2007).

[34] Advisory Committee Transcript at 26.

[35] NYSE Group, Inc. Form S-1 at 122 (March 13, 2006) (emphasis added).

[36] Exchange Market Data Coalition Response at 4.

charge whatever the market will bear."[37] We are told that markets do best "when unencumbered by industry regulation."[38]

Of course, the business model of the exchanges is unlike any other business model, which in large part is why Congress adopted the Exchange Act. And, the exchanges' desire to be unencumbered by regulation is very selective. They, like the government when it mandates that broker-dealers, and ultimately the public, must bring them the raw materials of the market – quotes, bids, offers, and limit orders – immediately and without compensation. They like the government when it empowers them to use their regulatory status to promote their commercial ends. They like having antitrust immunity, albeit of undefined scope. Their comparison to private sector intermediaries – who compete without benefit of government mandates, government regulatory power, antitrust immunity, or a captive rate-base – is simply inapposite.

Self-regulatory organizations have statutory obligations such as those under Exchange Act Sections 6(b)(5), 6(b)(8) and 11A to protect investors and serve the public interest, to avoid imposing unjustifiable burdens on competition, and to promote the goals of a national market system. To remove those obligations that ostensibly justify and counterbalance the powers granted SROs would require Congress to propose legislation and an ensuing healthy debate.

VII. NYSE ARCA MISREPRESENTS THE INTERESTS OF RETAIL INVESTORS AND THE PROFESSIONALS WHO SERVE THEM IN TERMS OF FAIR ACCESS TO DEPTH-OF-BOOK QUOTATION DATA

NYSE Arca states that retail investors should have no issues with NYSE Arca imposing a new fee on Arca Book Data and should now be satisfied with the top-of-book consolidated quotation alone. They cite four primary reasons: (i) broker-dealers provide the consolidated quote at "no charge"; (ii) retail investors will benefit from "new and innovative products for investors" now that Regulation NMS Rule 603 allows exchanges to sell last sale price information; (iii) Arca Book "is primarily a product for market professionals" so it does not matter that retail investors cannot afford it; and (iv) retail investors should not be concerned because the speed difference between the Arca Book feed and the consolidated quote is a "time difference that only the most sophisticated" trading programs "would notice."[39] Each of these points is inaccurate and fails to address the investor protection, equal access, market fairness, and transparency requirements of the Exchange Act.

The principal goal of the National Market System when it comes to market data should be assuring that all investors – whether professional or non-professional, or whether accessing information for institutional trading systems, through a broker-dealer, through an Internet portal, or directly from an exchange – have equal access to the same quality information, at a reasonable price, and at the same time. Any investor or professional should be able to type in a stock

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[37] NYSE Arca Response at 2.

[38] *Id.*

[39] NYSE Arca Response at 3, 4, 13, and 21.

symbol and a quantity up to 1,000 or 2,000 shares (a typical retail order), and obtain the current quotation from the markets. These quotations at "depth" are simply basic pricing facts – bids, offers, quotes, and orders – that are important to any investor on Wall Street or Main Street for making a sound investment decision. As NSX observes, market participants "who do not purchase the exchanges' depth of book data will suffer the types of informational disadvantages that Regulation NMS seeks to eradicate."[40]

But despite tremendous technological advances in the last 20 years, unless a non-professional investor signs multiple agreements and agrees to pay $97 per month (more than $1,100 per year), it is not possible for such an investor to obtain that 1,000 or 2,000 share quote. Moreover, neither is it possible for their professional adviser to obtain that quote without paying over $4,500 per year, and without the adviser's firm paying over $186,000 in additional fees. All of these costs ultimately will be borne by investors in some way. For an investor who may make only a dozen trades per year, that cost is not reasonable. Nor is it reasonable for the broker-dealer who serves that investor and thousands of others, as the exchanges charge per individual investor and professional. The inflated, non-cost-based fees also threaten to act as a drag on the competitiveness of American securities markets and to remove all incentive for the exchanges to increase their revenues through innovation as opposed to the exploitation of regulatory status.

As discussed above, the Commission's adoption of Regulation NMS has enhanced the need for depth-of-book data for all investors. The promise of Regulation NMS is transparency to enable price discovery. Market data illuminates the fragmented pool of liquidity to enable buyers and sellers to find each other on fair and equal terms. An unequal result in terms of access to market data, however, threatens to undermine this promise by benefiting some market participants at the expense of others by granting those who can access the data a distinct information advantage. A series of innovations in the last decade, including the advent of online trading, decimalization, and electronic trading networks, have brought millions of individual investors into the marketplace. Today's investors are demanding better quality information, such as real-time "depth-of-book" information. What once was necessary only for professional investors should now be considered basic information for retail investors too, whether they access that data directly or through the professionals who serve them. As NSX stated, "[t]his basic quotation information, we believe, is no longer limited to top of book quotes. In today's markets, it is vital that both consolidated depth of book quotation data, in addition to last sale information, be disseminated promptly into the marketplace."[41]

There should be no doubt that these issues matter to retail investors. Some 140 individual investors recently took the time to submit comment letters to the Commission in the parallel Nasdaq depth-of-book data rule filing, in which Nasdaq has eliminated the separate and free Instinet book and is now seeking approval for imposing its TotalView fee on those investors.[42] The same questions of eliminating investor access to data that investors have relied on and

[40] NSX Response at 2.

[41] NSX Response at 3.

[42] File Nos. SR-NASDAQ-2006-053, and SR-NASDAQ-2006-013; see Comment Letter from SIFMA re: File Nos. SR-NASDAQ-2006-053, and SR-NASDAQ-2006-013 (Feb. 12, 2007).

imposing unfair and unreasonable fees are at issue in that matter and, therefore, the Commission should consider those comments in this proceeding as well.

To debunk another myth: there are no innovations in the exchanges' provision of market data today that are benefiting retail investors. Recent exchange moves are only to change the fee structure to benefit the exchanges' bottom line, as pointed out by NSX in its letter. The recently proposed Nasdaq and NYSE last sale (post-trade) data may or may not be of use to individual investors; it all depends on whether it ultimately will be cheaper to buy last sale data from each individual exchange or to buy it from the old consolidated tape. But this is not innovation in terms of a new "product." It's the same basic factual data. It also has nothing to do with the data that is most important in terms of investing decisions which is at issue in this matter: single exchange, sole-source depth (and top) of book quotation data, which is distributed faster than the old consolidated quote.

From an investor perspective, we think the NSX's proposal that "all exchanges be required to consolidate and distribute their real time top *and* depth of book data, with the associated costs imposed only on those who act on the information," is an important proposal that the Commission must thoughtfully consider.[43] That, after all, is the system under which NYSE Arca formerly distributed the Arca Book Data.

VIII. CONCLUSION

SIFMA respectfully urges the Commission: (i) to reverse the Staff's order by delegated authority approving NYSE Arca's fee proposal pursuant to the Commission's Rule of Practice 431 on the grounds that the order failed to establish that the fees are fair and reasonable; (ii) to conduct a prioritized review of the Commission's approach to market data generally and the process and standards by which the Commission should evaluate market data proposals; (iii) to impose a moratorium on reconsideration of the NYSE Arca proposal, a moratorium on approval of any other market data rule proposals; and (iv) due to the significant public policy issues and controversy that extends beyond exchange members, to request that the staff either abrogate or not process any market data proposals filed by the exchanges for immediate effectiveness until the Commission conducts its review and adopts appropriate standards.

[43] NSX Response at 2.

SIFMA appreciates the interest of the Chairman, the Commissioners, and the Staff in this important topic. We stand ready to provide further input concerning this topic to the Commission and the Staff.[44] If you have any questions or would like to discuss any of these issues further, please contact me, or SIFMA's Vice President and Associate Counsel Ann Vlcek, or SIFMA's Assistant Vice President and Assistant General Counsel Melissa MacGregor, all 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. Chester Spatt, Chief Economist
Brian G. Cartwright, Esq., General Counsel

[44] *See* SIFMA letter of January 17, 2007 for proposals to address questions of cost and access to market data.

Appendix A

Fees for Major "Depth-of-Book" and NBBO Market Data Products

	Non-Professional	**Professional**	**Firm (Variable Fees for Access/ Distributor)**
NYSEArca ArcaBook[1]	$10/month/device, $120/year/device	$30/month/device, $360/year/device	$750/month, $9,000/year
NYSE OpenBook (excludes Level 1 charges)	$60/month/device, $720/year/device	$60/month/device, $720/year/device	$5,000/month, $60,000/year
Nasdaq TotalView and OpenView (includes Level 2 but excludes level 1 UTP)	$14/month/device, $168/year/device	$70/month/device, $840/year/device	$5,000/month, $60,000/year[2]
Amex Depth-of-Book[3]	$10/month/device, $120/year/device	$20/month/device, $240/year/device	$2,000/month, $24,000/year
CTA Tape A[4]	$1/month/subscriber, $12/year/subscriber	$127.25/month/subscriber, $1527/year/subscriber	$1,450/month, $17,400/year
CTA Tape B	$1/month/subscriber, $12/year/subscriber	$30.20/month/subscriber, $362.40/year/subscriber	(covered by CTA Tape A fee)
Nasdaq Level 1	$1/month/subscriber, $12/year/subscriber	$20/month/subscriber, $240/year/subscriber	$3,750/year
OPRA[5]	$1/month/subscriber, $12/year/subscriber	$20/month/subscriber, $240/year/subscriber	$1,000/month, $12,000/year
Annual Total for Investor to Access All Relevant Data	**$1,176**	**$4,529.40**	**$186,150**

1 The ArcaBook fee is split - half for access to data on CTA securities and ETFs; and half for Nasdaq-UTP securities. The data in the table assumes a customer wants access to both feeds.

2 The Nasdaq firm fee is split, half for access, and half to serve as a distributor.

3 The Amex firm charge is based on direct access; slower indirect access costs 25% less.

4 CTA Tape A professional and non-professional fees both decline with volume; firm fee is based on direct access; slower indirect access costs 50% less.

5 The OPRA firm charge is based on direct access; slower indirect access costs 40% less. The table does not include single-exchange "depth-of-book" market data products for the options markets (such as CBOE's $5/month/user non-professional fee).

Appendix B

National Stock Exchange Comment Letter dated February 27, 2007

PDF attached

NSX National Stock Exchange[SM]

Joseph Rizzello
Chief Executive Officer

February 27, 2007

Submitted Via Electronic Mail

Ms. Nancy M. Morris, Secretary
U.S. Securities and Exchange Commission
100 F St. N.E.
Washington, DC 20549-0609
Email: rule-comments@sec.gov

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

Dear Ms. Morris,

The National Stock Exchange ("NSX") appreciates this opportunity to comment on the Commission's review of the approval by the Division of Market Regulation of a rule change that would establish fees to be charged by NYSEArca, Inc. ("NYSEArca") for its Arca Book market data product ("NYSE Arca Data").[1] This comment letter is filed in connection with the Commission's order[2] granting the petition by NetCoalition for review of the Division's approval of the NYSE Arca Data fee proposal. NSX's view is that this fee approval should not be implemented until the Commission has first conducted a thorough, broad-based review of the securities market data structure and, based on such a review, reconsiders the NYSE Arca Data fee proposal.

NSX requests that the Commission examine closely the fundamental issues concerning both "depth of book" and consolidated real time market data. Recent, dramatic changes in technology and the competitive landscape affecting securities exchanges have transformed the manner that information is currently being produced and accessed by market participants. The Commission should carefully consider the alternatives now available to modernize and optimize the dissemination of securities markets data.

Under the National Market System ("NMS"), consolidated data is essentially a rate-fixed product which is redistributed back to the broker-dealers who are required to supply it. Not only is the markup for the data excessive[3], but also the data has already become insufficient by itself

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[1] See Securities Exchange Act Release No. 34-54597 (October 12, 2006), (October 12, 2006)

[2] See Securities Exchange Act Release No. 34-55011 (December 27, 2006), (December 27, 2006)

[3] In 2003, consolidated market data revenue totaled $386 million, with network expenses of only $38 million. See Exchange Act Release No. 49,325 (February 26, 2004), 69 Fed. Reg. 11126, 11179 (March 6, 2004)

as a tool for investors to make trading decisions. One reason for this is that unfettered access to consolidated quotation data at multiple price points is necessary as liquidity naturally aggregates around multiple penny increments.

The Commission has outlined several key objectives for Regulation NMS, including transparency, fairness, and access. These key policy objectives ultimately call for the automation of all markets wherever possible. We believe NMS will foster a more competitive and efficient secondary market, one which mitigates unfair informational advantages because markets will be both better informed and more competitive. Decimalization and technology advances in order management systems, however, have served to reduce the displayed liquidity at the top of book. As these trends continue, the tangible value to the marketplace of consolidated top of book data will continue to decrease. In the meantime, until the market data fee structure is reformed, broker-dealers will still be forced to purchase market data at a fixed and, we believe, arbitrary price. Market participants who do not purchase the exchanges' depth of book data will suffer the types of informational disadvantages that Regulation NMS seeks to eradicate.

The Exchange Market Data Coalition has stated in its comment letter that "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 that "revenue fosters innovation"[4]. NSX disagrees with these statements. In our view, it is competition, or the opportunity for competition, that fosters innovation – not revenue. More importantly, to the extent that market data revenue is used to fund regulatory activities, we submit that it would be more logical and transparent to charge an explicit regulatory fee for these services.

Market forces today clearly indicate that the $400 million consolidated data revenue pool is too large. NSX estimates that in 2006, roughly $50 million of the $400 million market data revenue pool was actually rebated back to broker-dealers/subscribers. This amount would be higher still if not for the limits on rebate amounts imposed under Commission regulation. Furthermore, the securities industry levies market data fees on a per user basis, but rebates back market data fees on a per trade basis, in amounts that are limited, we believe artificially, by SEC rule. This results, at best, in a misappropriation of fees and, at worst, an incentive for adverse gaming behavior.

We believe the Commission should explore all possible approaches to reforming market data consolidation and dissemination with a minimum of market disruption, including the means through which exchanges fund their vitally important regulatory functions. We recommend that all exchanges be required to consolidate and distribute their real time top *and* depth of book data, with the associated costs imposed only on those investors who act on the information. Such a

[4] Comments of Exchange Market Data Coalition, January 26, 2007

surcharge would be uniformly applied in the same manner as are Section 31 fees that fund SEC regulatory activities. Unlike Section 31 fees, however, the surcharge would be collected by an appropriate securities industry entity. As a result, the costs borne by each self regulatory organization for market data collection, consolidation, dissemination, and regulation thereof would be explicitly paid for by investors who transact in the markets, and not by passive investors who merely wish to access basic quotation information. This basic quotation information, we believe, is no longer limited to top of book quotes. In today's markets, it is vital that both consolidated depth of book quotation data, in addition to last sale information, be disseminated promptly into the marketplace.

Potential distributors of this consolidated data would not be limited solely to those who can afford a variety of access fees. Instead, the consolidated data would be available to any entity with a commercial interest in distributing data, or who has the creativity to repackage it into a product more valuable or useful to the investing public. Exchanges could continue to offer market data services. Similarly, other businesses, such as technology companies, could be invited to compete and innovate. This competition would be premised on non-discriminatory access to data.

NSX believes that the adoption of these recommendations would provide immediate and substantial benefits for the entire U.S. capital markets system. These reforms would eliminate several hundred million dollars in unnecessary and misallocated fees imposed on the investing public, while simultaneously spurring the free market to create an environment where market data can be creatively and profitably redistributed worldwide.

Based on the foregoing, NSX urges the Commission to consider and adopt the following proposals:

1. Break the monopoly on real time consolidated top and depth of book data and deliver it to the innovators. Allow a market to develop for the repackaging of this data and new products that will follow.

2. Charge the securities industry an explicit fee for the costs of data consolidation, which should be embedded in the transaction cost. We believe this fee in the aggregate would be significantly less than the current cost of consolidated data.

3. Exchanges should be free to charge explicitly for their costs associated with regulation, to the extent they choose to do so. If a regulatory fee is transaction based, it should be shared equally by both parties to the transaction.

NSX today is the beneficiary of the revenue it receives from market data fees for transactions occurring there. Our arguments for dismantling the existing consolidated market data fee and revenue allocation formulas would cost NSX and other exchanges substantial revenue. NSX believes, however, that fair and free access to basic market information certainly benefits investors. By allowing more potential participants to deliver innovation to the industry, fair and free access to basic market information will provide the entire U.S. securities market a competitive advantage globally.

NSX believes that the goals of Regulation NMS ultimately will be frustrated unless the market data issue is fully and fairly addressed. The Commission should seize this opportunity to articulate new standards to govern decision-making in these areas. Given the strong positions articulated on all sides of this complex issue, we believe the Commission should consider issuing a concept release in order to prompt thorough industry wide discussion. Until these important issues are comprehensively reviewed and vetted, we urge the Commission to continue the stay on the NYSE Arca Data fee proposal and to delay approval of any proposed exchange rule to establish fees for depth of book information.

Thank you for the opportunity to express these views. We hope that the Commission will not hesitate to call upon us if we may provide you additional information or assistance concerning these issues.

Respectfully submitted,

/s/

Joseph Rizzello
Chief Executive Officer
National Stock Exchange, Inc.

cc: Chairman Christopher Cox
Commissioner Paul S. Atkins
Commissioner Roel C. Campos
Commissioner Kathleen L. Casey
Commissioner Annette L. Nazareth
Erik R. Sirri, Director, Division of Market Regulation