NSX National Stock® Exchange

September 9, 2013

Via Electronic Mail (rule-comments@sec.gov)

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: SR-FINRA-2013-031

Dear Ms. Murphy:

The National Stock Exchange, Inc. ("NSX" or "Exchange")[1] is writing to provide comments to the Securities and Exchange Commission (the "Commission") on the Financial Industry Regulatory Authority, Inc.'s ("FINRA") proposed amendments to Rules 6271 and 6272 ("ADF Proposal")[2] regarding members seeking registration as FINRA Alternative Display Facility ("ADF") Market Participants ("ADF Participants"). NSX urges the Commission not to approve the ADF Proposal because FINRA (1) fails to meet its burden of adequately articulating and justifying the reasonableness of the ADF Participant fees, (2) subsidizes the cost of developing and operating the ADF platform with member dues and fees which violates FINRA's obligation to ensure that its fees, dues and fines are fair, reasonable and equitably allocated among members, and (3) requires members to commit 75% of their quotes and trade reports to FINRA which is an unprecedented requirement for a self-regulatory organization and a burden on competition that is not necessary or appropriate.

I. Equitable Allocation of Reasonable Dues, Fees and Other Charges

Under the ADF Proposal, FINRA proposes to recoup a portion of the specific costs of building the new ADF platform from ECNs that fail to use the ADF platform after becoming an ADF Participant. FINRA's ADF Proposal requires new ADF Participants to (i) provide FINRA with monthly volume projections, (ii) deposit either $250,000 or $500,000 in an escrow account in five

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1 The NSX provides order delivery functionality to electronic communication networks ("ECNs"). The order delivery function provides a standard access point through which market participants can access the quotations of an ECN participant. An ECN that participates in the order delivery program provides NSX with its best bids and offers for display in the consolidated quotation system. NSX receives orders from market participants seeking to access these quotes, and it delivers an order delivery notification to the ECN. The ECN responds to the order delivery notification confirming the number of shares to be executed. The resulting execution occurs on the NSX. The NSX reports all executions to the consolidated tape for public display. NSX also disseminates a consolidated depth of book product through which an ECN can provide attributed quotations. Two ECNs participate in NSX's order delivery program, with one order delivery participant accounting for over 90% of overall ECN volume. Three additional ECNs are in various stages of certification to participate in NSX's order delivery program.

2 See Securities Exchange Act Release No. 70048 (July 26, 2013), 78 FR 46652 (August 1, 2013) ("ADF Proposal").

equal installments ("Proposed Participant Fee"), and (iii) agree to forfeit some or all of the Proposed Participant Fee if (1) the ADF Participant fails to quote or report trade reports for a two year period to the ADF, or (2) the ADF Participant fails to submit 75% of its quotes and trades to FINRA ("Quote and Trade Commitment").

The Proposed Participant Fee's two tiered rate is determined by the date that the ADF Participant begins quoting and reporting trades to FINRA. ADF Participants that request access to the ADF platform by the scheduled completion date of mid 2014 must deposit $250,000 in an escrow account. However, an ADF Participant can accelerate the completion date of the ADF platform to late 2013 if the ADF Participant deposits $500,000 rather than $250,000 in an escrow account. FINRA indicates that the higher amount reflects the increased costs associated with the accelerated development schedule. ADF Participants that begin quoting or reporting transactions to FINRA within 90 days of the ADF Participant requesting the accelerated completion must also pay the $500,000 escrow amount.

An ADF Participant can recover the Proposed Participant Fee through market data rebates which are equal to 50% of FINRA's market data revenue during any quarter. ADF Participants can recover up to 80% of the Proposed Participation Fee in the first quarter of participation while collecting the remaining 20% at the end of a two-year term, or 100% of the Proposed Participant Fee over the two-year term. ADF Participants must also agree to provide FINRA with 75% of both quotes and trades during the same two-year period (Quote and Trade Commitment) otherwise all or some of the Proposed Participant Fee will be forfeited to FINRA.

FINRA has not filed the proposed transaction costs which it intends to charge ADF Participants for shares executed and transactions reported to FINRA as a part of the Quote and Trade Commitment.

A. REASONABLE DUES FEES AND OTHER CHARGES – SECTION 15A(b)(5)

(i) FINRA Failed to Establish Reasonableness of Fees

FINRA has failed to articulate a reason or basis for the reasonableness of the Proposed Participant Fee and corresponding market data rebates as required by Section 15A(b)(5) of the Exchange Act.[3] FINRA has the burden of establishing that the ADF Proposal is consistent with the Exchange Act, and it cannot satisfy this requirement by a mere assertion.[4]

Furthermore, FINRA has failed to clearly explain why it chose $250,000 and $500,000 as the amounts of the Proposed Participant Fee. FINRA indicated that the Proposed Participant Fee represented a "portion" of the specific development cost. FINRA should be required to, at a minimum, disclose the specific percentage of total development costs that the Proposed Participant Fee represents so that FINRA members can comment upon how FINRA is covering the costs associated with the ADF platform.

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[3] Id. at text following Footnote 21.

[4] See Securities Exchange Act Release No. 65362 (September 20, 2011), 78 FR 46652 (August 1, 2013) at text preceding Footnote 51.

(ii) FINRA Failed to Provide Information on the Total Cost of Developing and Operating the ADF

The Commission must require FINRA to disclose how it is funding the development and operation of the ADF platform.[5] The ADF has no revenue, and FINRA proposes to rebate 50% of market data revenue to the ECN participants. The Commission and market participants can only determine whether the fees are reasonable for all FINRA members after analyzing (i) the total cost of development and operation of the ADF; (ii) the projected volume from potential ADF Participants; (iii) the source of funds used to pay for the ADF; and (iv) future fees to be charged to ADF Participants. Under the ADF Proposal, the largest ADF Participants may pay little or nothing for the development and operation of the ADF platform. FINRA has failed to establish how this is fair and reasonable for all FINRA members including those that do not use the ADF facility such as limited purpose broker-dealers.

(iii) FINRA failed to Disclose the Transaction Costs for Quote and Trade Commitment

The reasonableness of the fees charged under the ADF Proposal cannot be evaluated until FINRA discloses additional fees that it intends to charge for the quotes and transaction reports submitted under the Quote and Trade Commitment. Both fee structures are necessary for market participants to comment upon whether FINRA members that do not use the facility are being treated fairly and that the fees are reasonable.

B. EQUITABLE ALLOCATION– SECTION 15A(b)(5)

FINRA has failed to adequately articulate how the Proposed Participant Fee is equitably allocated between ADF Participants and all other FINRA member firms. In the ADF Proposal, FINRA states that fees are equitably allocated among member firms because the proposal "establishes an equitable and transparent method for registering" ADF Participants, and ADF Participants that are requesting a migration to the ADF will use the platform or will pay for a portion of the specific costs FINRA incurs to migrate ADF Participants if they do not thereafter use the platform.[6] Neither of these reasons address why it is equitable and fair for FINRA to charge ECNs, regardless of proposed volume, the same Proposed Participant Fee.

(i) FINRA Failed to Establish that ADF Participant Fee is Equitable as Among All FINRA Members

FINRA has failed to provide a sufficient basis upon which the Commission can make a determination that the Proposed Participant Fee and corresponding market data rebates are equitably

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5 See Securities Exchange Act Release No. 69622 (May 23, 2013), 78 FR 32510 (May 30, 2013) at text following Footnote 288. The Commission questioned whether the New York Stock Exchange performed an adequate analysis of costs associated with processing proxies in its order to begin disapproval proceedings. The Commission stated that "neither the Exchange nor the PFAC have articulated a sufficient analysis of Broadridge's cost of providing proxy processing services, including with respect to issuers of various sizes, or of the costs incurred by broker-dealers that may go beyond the services provided by Broadridge. Accordingly, the Commission lacks a sufficient basis upon which to assess whether the incremental changes proposed to the existing fee structure…are consistent with the statutory standard, including whether the overall level and structure of the fees reflected in the Exchange's rules are "reasonable" or an "equitable" allocation of fees."

6 See ADF Proposal at text following Footnote 22.

allocated among FINRA members as required by Section 15A(b)(5) of the Exchange Act. FINRA stated that its proposal enhances the "equitable and transparent" nature of its registration process. However, this statement is insufficient to meet the test that the ADF Participant Fee is equitably allocated among FINRA members and, in fact, the equitable and transparent nature of the registration process is irrelevant when determining whether a fee is fair and equitably allocated among members. Again, FINRA provides an assertion that the ADF Proposal is consistent with Section 15A(b)(5) of the Exchange Act without clearly articulating facts evidencing that it has met this standard.

Furthermore, FINRA assumes that it is equitable for all member firms to fund the ADF platform regardless of whether that member uses the facility. FINRA provides no basis for this assumption. Without further justification, FINRA must evidence that the ADF will be self-funded.

(ii) FINRA Failed to Establish that Fixed ADF Participant Fee is Equitable Among ADF Participants

FINRA also failed to explain why it is equitable and fair to charge all ADF Participants the same Proposed Participant Fee regardless of an ECN's projected volume. FINRA provides that this structure is fair and equitable because market volume does not significantly impact the cost associated with building out the ADF Platform. However, FINRA then appears to contradict this statement when it explained that it needed monthly volume projections in order to (i) recover a portion of costs related to "building out the ADF platform to accommodate the member's volume projections"[7], and (ii) to, among other things, pay for SIP capacity usage.[8] FINRA's conflicting statements prevent the Commission from finding that it is equitable and fair to charge small or new ECNs that have little or no volume, the same fee as a market participant that comprises a majority of the ADF's processing and regulatory functions.

(iii) FINRA Failed to Establish that Agreements Between FINRA and the ADF Participants are Equitable

The ADF Proposal provides FINRA with flexibility to negotiate the terms of any agreement with a potential ADF Participant. FINRA did not provide a justification as to how this flexibility will not be (i) unfairly discriminatory if different terms are given to ADF Participants, (ii) an inequitable allocation of fees and dues, or (iii) a burden on competition which is not necessary or appropriate.

(iv) FINRA Failed to Disclose the ADF Platform's Transaction Costs

FINRA does not provide the Commission with sufficient information to determine whether FINRA's ADF Proposal allocates fees and dues among its members in an equitable and fair manner. The Commission should require FINRA to disclose any other fee it intends to charge ADF Participants, including transaction and communication costs, so that market participants can determine how FINRA will cover the costs associated with the ADF platform. Nor does it disclose any limits on quoting or trading activity as it had limited past participant to 10 million quotes per day.

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7 Id. at text following Footnote 19.

8 Id. at text preceding Footnote 20.

II. Protection of Investors and the Public Interest – Section 15A(b)(6)

The Commission should carefully review FINRA's payment of market data rebates for the Quote and Trade Commitment to ensure that such rebates are consistent with the protection of investors and the public interest. The arrangement creates a conflict of interest between the regulator (FINRA) and ADF Participants. FINRA is mandating quotes representing order flow to be displayed on the ADF platform when doing so may be inconsistent with the ADF Participant's best execution obligation, which if not satisfied, could result in a regulatory sanction imposed by FINRA. The Commission should consider whether FINRA can mandate that an ADF Participant display quotes on the ADF platform and also effectively regulate whether that ADF Participant is complying with the federal securities laws as well as FINRA's rules, and whether such an arrangement is consistent with the protection of investors and the public interest.

III. Burden on Competition – Section 15A(b)(9)

The Commission is unable to determine whether the ADF Proposal creates burdens on competition that are necessary and appropriate in furtherance of the purposes of the Exchange Act. FINRA has failed to adequately articulate the impact of the ADF Proposal on the competition that exists today. FINRA states in the ADF Proposal that the proposed rule change does not impose a burden on competition because FINRA members may choose to (i) pay the costs associated with accelerating migration to the ADF platform; (ii) use the ADF to display quotations or orders; (iii) recover through the payment of rebates the Proposed Participant Fee by complying with the Quote and Trade Commitment; or (iv) quote or trade through another trading venue.

However, FINRA's analysis fails to meet the statutory burden in that it does not address whether the ADF Proposal imposes a burden on competition for other self regulatory organizations such as the NSX. The Proposed Participant Fee and the Quote and Trade Commitment impose a clear burden on competition that is not necessary or appropriate. The Commission should preserve competitive forces for ECN quotes or trades, as well as competition between ECNs, as much as possible.

A. Proposed Participant Fee

FINRA must provide a competitive offering for ADF transaction services. The Commission should only approve an offering that competes with existing self regulatory organizations in a fair and equitable manner. Additionally, the Commission should disapprove an offering that unfairly benefits one or few ECNs at the expense of other or future ECNs. Market participants should be able to fairly compete among themselves, and choose between service providers that provide order display solutions that are competing on a level playing field. One market participant should not be able to unfairly subsidize its trading facility. Nor should one member receive a competitive benefit from the ADF Proposal.

FINRA has failed to sufficiently articulate why it is not a burden on competition to offer the ADF platform at a subsidized rate which does not include the costs associated with the development, operation and regulation of the ADF platform. FINRA has not disclosed the actual cost for the ADF platform. Nor has FINRA disclosed all other transaction charges it intends to collect from ADF Participants. Without this information, the Commission cannot determine whether the ADF will pose a burden on competition that is necessary or appropriate.

B. QUOTE AND TRADE COMMITMENT

The ADF Proposal requires members to send 75% of their quotes and trades to FINRA.[9] This unprecedented requirement is a burden on competition for any SRO that is seeking to offer ECN quote display, and it is not necessary and appropriate. Should the largest ECN agree, 60% of all ECN quotes and trades in the national market system would be committed to be displayed on and reported to FINRA. It is unlikely that any SRO could compete with FINRA for ECN transaction services given the costs of operating and regulating an SRO that provides order delivery functionality in a fair and nondiscriminatory manner.

Current and future ECNs would have no choice but to become ADF Participants if NSX ceased to offer order delivery functionality. If this occurs within 90 days of an accelerated launch, the four remaining ECNs will need to provide FINRA with $500,000 for deposit in an escrow account. The alternative for existing ECNs would be to cease displaying their quotes into the national market system for 90 days in order to avoid paying for accelerated functionality that they did not request. For new ECN entrants, their alternatives would be to delay their launch until the expiration of the 90 day period or remain a nondisplayed ("grey market") facility to save $500,000, or not launch their displayed business because the barrier to entry has become too high.[10] By negatively affecting competition between ECNs and creating a large barrier to entry, the ADF Proposal unnecessarily and inappropriately impedes competition between markets in violation of Section 15A(b)(9) and Section 11A of the Exchange Act.

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The NSX appreciates the Commission's consideration of this comment letter. If you have any questions, please contact the undersigned.

Sincerely,

David Harris
Chairman and CEO
National Stock Exchange, Inc.

CC: Mary Jo White, Chair
Luis A. Aguilar, Commissioner
Daniel M. Gallagher, Commissioner
Kara M. Stein, Commissioner
Michael S. Piwowar, Commissioner

10 By contrast, NSX charges a monthly membership fee of $500 and offers free display of ECN quotes for those ECNs that choose to forgo market data revenue and liquidity rebates. Please see the NSX fee schedule at http://www.nsx.com/content/nsx-fee-schedule.