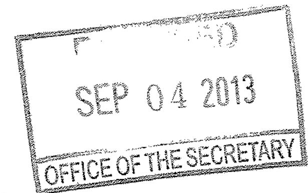

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

In The Matter of: The Application of SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION For Review of Action Taken by NYSE Arca, Inc.	Admin. Proc. File No. 3-15350

BRIEF OF APPLICANT SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN RESPONSE TO ORDER REGARDING PROCEDURES TO BE ADOPTED IN PROCEEDINGS

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Applicant Securities Industry and Financial Markets Association ("SIFMA") respectfully submits this consolidated response to the Commission's Orders dated July 3, 2013, requesting briefing on several preliminary matters regarding two applications that SIFMA submitted in the above-captioned proceedings, which seek review of actions taken by various self-regulatory organizations ("SROs") that limit access to market data made available by those SROs.

BACKGROUND

At issue in these applications are certain rule changes unilaterally adopted by various securities exchanges (collectively, the "Exchanges") that impose fees for access to specified market data products. By the terms of these rule changes, any party who does not pay these newly imposed fees—including SIFMA members and their customers—will be unable to access the market data made available by the Exchanges.

The Securities Exchange Act of 1934 (the "Exchange Act") and the Commission's regulations impose limits on the fees that SROs like the Exchanges may charge for market data. An SRO must, among other things, "provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities," 15 U.S.C § 78f(b)(4), and "not impose any burden on competition not necessary or appropriate in furtherance of the purposes of" the Exchange Act, *id.* § 78f(b)(8). In addition, because each of the Exchanges is an "exclusive processor" of securities information, *id.* § 78c(a)(22)(B), the fees they charge for market data must be "fair and reasonable" and "not unreasonably discriminatory," *id.* § 78k-1(c)(1)(C)-(D); *see* 17 C.F.R. § 242.603(a) (same).

In May 2006, NYSE Arca filed a proposed rule change with the Commission seeking to impose fees for access to the depth-of-book data it makes available, which is provided to it by market participants and consolidated by the exchange, and which, like many other exchanges, it had previously made available for no cost. *See NetCoalition v. SEC* (*NetCoalition I*), 615 F.3d

525, 531 (D.C. Cir. 2010). Under the law in effect at the time, the rule change could not take effect unless first approved by the Commission based on a finding that the rule change was consistent with the Exchange Act. *See id.* In an order dated December 9, 2008, the Commission approved the new fees despite NYSE Arca's failure to provide any cost data supporting the fees, concluding instead that the fees were consistent with the Exchange Act because, notwithstanding NYSE Arca's conceded status as an exclusive processor of its data, NYSE Arca was subject to "'significant competitive forces'" in setting the fees. *Id.* at 532; *see Order Setting Aside Action by Delegated Authority and Approving Proposed Rule Change Relating to NYSE Arca Data*, 73 Fed. Reg. 74770 (Dec. 9, 2008).

On petition for review, the United States Court of Appeals for the D.C. Circuit expressly vacated the order because it failed to "disclose a reasoned basis" for concluding that NYSE Arca [was] subject to significant competitive forces in pricing" access to its depth-of-book data product. *NetCoalition I*, 615 F.3d at 544 (citation omitted). In reaching this conclusion, the Court held that the Commission's finding of competition was not supported by substantial evidence, *id.* at 528, and explained that the cost of producing market data is relevant to whether competition constrains the Exchanges' fees because pricing that greatly exceeds costs "may be evidence of 'monopoly,' or 'market,' power," *id.* at 537. NYSE Arca sought rehearing on the issue of whether the Court should have allowed the rule to remain in effect pending proceedings on remand. *See* No. 09-1042, Dkt. No. 1266631 (Sept. 17, 2010). The Court denied the petition.

After this ruling, the Exchanges nonetheless filed a series of proposed rule changes imposing fees for various market data products. The rule change at issue in No. 3-15350 proposes essentially the same fees as the ones the Commission approved in the order vacated in

NetCoalition I.[1] The rule changes at issue in No. 3-15351 propose to impose fees for various other market data products.[2] Each of these rule changes invokes the same purported economic justifications that the D.C. Circuit explicitly rejected in *NetCoalition I*, and none is supported by any evidence of the cost of producing the data in question.

Pursuant to then-recent amendments by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010), each of these rule changes took effect immediately upon filing. *See* 15 U.S.C. § 78s(b)(3)(A). Within 60 days of each filing, the Commission had summary authority to "temporarily suspend" the rule change if such action was "necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of [the Exchange Act]." *Id.* § 78s(b)(3)(C). The Commission did not exercise this authority as to any of the proposed rule changes.

SIFMA and NetCoalition petitioned for review in the D.C. Circuit of the Commission's refusal to suspend the rule changes. *NetCoalition v. SEC* (*NetCoalition II*), 715 F.3d 342 (D.C. Cir. 2013). In its brief, the Commission argued that the court lacked authority to review the petitions because, *inter alia*, Section 19(b)(3)(C) of the Exchange Act withdraws the court's jurisdiction to review the Commission's failure to suspend a rule change that took effect upon filing. *See* Final Brief of Respondent Securities and Exchange Commission at 31-51, *NetCoalition II*, D.C. Cir. Nos. 10-1421, 10-1422, 11-1001, 11-1065 ("SEC Brief"). The Commission assured the D.C. Circuit that this interpretation of Section 19(b)(3)(C) would not leave the rule changes unreviewable by the courts because Section 19(d), which authorizes any

[1] *See Proposed Rule Change by NYSE Arca, Inc. Relating to Fees for NYSE Depth-of-Book Data*, Release No. 34-63291, File No. SR-NYSEArca-2010-97 (Nov. 9, 2010), *available at* http://www.sec.gov/rules/sro/nysearca/2010/34-63291.pdf.

[2] A full list of the rule changes at issue in No. 3-15351 is available at Exhibit A to SIFMA's application in that matter.

person who has been "limit[ed] … in respect to access to services offered by" an SRO to seek Commission review of the decision, 15 U.S.C. § 78s(d), "provides a mechanism through which the consistency with applicable law of a rule that takes effect upon filing may be determined." SEC Brief at 44. The Commission explained that "[j]udicial review of a Commission order in a [Section 19(d)] proceeding permits a court to consider directly whether a fee is consistent with the Act." *Id.* at 46.

On April 30, 2013, the D.C. Circuit held that the Commission's failure to suspend the rule changes was not reviewable under Section 19(b)(3)(C), as amended. *NetCoalition II*, 715 F.3d at 347. In reaching this conclusion, the court expressly relied upon the Commission's representations regarding Section 19(d), explaining that "we take the Commission at its word … that it will make the section 19(d) process available to parties seeking review of unreasonable fees charged for market data, thereby opening the gate to our review." *Id.* at 353. The court also cautioned that the Dodd-Frank amendments did not render the decision in *NetCoalition I* "moot," and that the *NetCoalition I* decision "remains a controlling statement of the law as to what sections 6 and 11A of the Exchange Act require of SRO fees." *Id.* at 354.

Following the Commission's guidance regarding the Section 19(d) process, SIFMA filed the applications in Proceedings Nos. 3-15350 and 3-15351. These applications request that the Commission set aside the rule changes because they limit the access of SIFMA's members and their customers to market data made available by the Exchanges and are inconsistent with the Act.

ARGUMENT

The Commission has requested that the parties address the following preliminary questions:

1. The primary issues the Commission will have to decide in considering the applications;

2. Whether and to what extent the Commission's standard of review in these proceedings pursuant to Exchange Act Sections 19(d) and (f) differs from the standard of review applicable to the Commission's decision whether to suspend a rule under Exchange Act Section 19(b)(3);

3. Whether the applications for review in Proceedings Nos. 3-15350 and 3-15351 should be consolidated, or whether Proceeding No. 3-15351 should be stayed pending the Commission's consideration of the application in Proceeding No. 3-15350;

4. Whether further development of the record would be helpful to the Commission's consideration of the application and whether it would be appropriate to assign an administrative law judge to conduct an evidentiary hearing for the purpose of issuing an initial decision in these matters; and

5. Any other matters the parties believe would assist the Commission in determining the appropriate procedures for, and other issues related to, the proceedings.

SIFMA's responses to these questions are set forth below.

I. The Primary Issue In These Proceedings Is Whether The Fee Rule Changes Comply With The Exchange Act And Applicable Regulations.

The primary issue before the Commission in these proceedings is whether the Exchanges' rule changes are "fair and reasonable," § 78k-1(c)(1)(C), and otherwise comply with the Exchange Act and applicable regulations.

As the Commission has recognized, Section 19(d) of the Exchange Act "authorizes the Commission, on its own motion or on application of any aggrieved person, to review any decision by an SRO that 'prohibits or limits any person in respect to access to services offered by such organization.'" SEC Brief at 45 (quoting 15 U.S.C. § 78s(d)(1)). Section 19(f) provides the standard of review to be applied in such a proceeding and directs that the Commission "shall set aside the action of the [SRO]" and "grant such person access" unless it finds that (1) "the specific grounds on which such ... prohibition or limitation is based exist in fact"; (2) the prohibition or limitation "is in accordance with the rules of the [SRO]"; and (3) "such rules are,

and were applied in a manner, consistent with the purposes of [the Exchange Act]." 15 U.S.C. § 78s(f). Even if the Commission makes these findings, it still must set aside the action and grant access if it finds that the prohibition or limitation "imposes any burden on competition not necessary or appropriate in furtherance of the purposes of [the Exchange Act]." *Id.*

As the Commission has explained, this standard is substantively identical to "the standard the Commission applies in decid[ing] whether to approve or disapprove a rule under Section 19(b)(2)(C)." SEC Brief at 45; *see NetCoalition II*, 715 F.3d at 352 (noting same). Under Section 19(b)(2)(C), the Commission "shall approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of [the Exchange Act] and the rules and regulations thereunder applicable to such organization." 15 U.S.C. § 78s(b)(2)(C)(i). Accordingly, when the prohibition or limitation at issue in a Section 19(d) proceeding is a fee that restricts access to data made available by an Exchange, Section 19(f) requires the Commission to set aside the fee, and to grant access, unless it finds that the fee is consistent with the requirements of the Exchange Act and applicable regulations. This interpretation is further supported by Section 19(b)(3)(C) of the Exchange Act, which provides that an SRO rule is enforceable only "to the extent it is not inconsistent with the provisions of [the Exchange Act or] the rules and regulations thereunder." 15 U.S.C. § 78s(b)(3)(C).

Thus, the issue before the Commission is whether the rule changes are consistent with the Exchange Act and applicable regulations, including the requirement that the fees be "fair and reasonable." 15 U.S.C. § 78k-1(c)(1)(C); 17 C.F.R. § 242.603(a). More specifically, the issue is whether, absent evidence regarding the cost of producing the market data, there is a sufficient basis for finding the fees to be fair and reasonable based on the alleged existence of competition. In resolving this issue, the Commission will need to consider whether, and to what extent, the

D.C. Circuit's decision in *NetCoalition I* permits a fee to be found fair and reasonable based on alleged competitive forces, and what evidence would be necessary to support such a finding. *See NetCoalition II*, 715 F.3d at 354 (*NetCoalition I* "remains a controlling statement of the law as to what sections 6 and 11A of the Exchange Act require of SRO fees").

II. The Standard Of Review In These Proceedings Under Section 19(d) Of The Exchange Act Differs From The Standard For Suspension Under Section 19(b)(3)(C).

The standard of review in these proceedings under Section 19(d) differs from the standard of review that the Commission would apply under Section 19(b)(3)(C) when deciding whether to suspend a rule change that took effect upon filing. Under Section 19(b)(3)(C), the Commission "summarily may temporarily suspend" a rule change if "it appears to the Commission" that one of three statutory criteria is satisfied. 15 U.S.C. § 78s(b)(3)(C). This standard calls upon the Commission to evaluate whether a suspension "is necessary or appropriate" (1) "in the public interest"; (2) "for the protection of investors"; or (3) "otherwise in furtherance of the purposes of [the Exchange Act]." *Id.* In contrast, the standard in a Section 19(d) proceeding requires the Commission to determine directly whether a limitation on access (whether by rule change or otherwise) is consistent with the Exchange Act and applicable regulations. *See supra* § I. Unless the Commission affirmatively finds the limitation to be consistent with these requirements, it "shall" set the limitation aside. 15 U.S.C. § 78s(f). Of course, if there is no evidence in the administrative record sufficient to allow such a finding, then the Commission has no choice but to set aside the rule.

III. Proceeding No. 3-15351 Should Be Stayed Pending Consideration Of Proceeding No. 3-15350.

SIFMA believes that the most appropriate and efficient way to proceed with these parallel applications is to hold the application in Proceeding No. 15351 in abeyance pending a

decision on the application in Proceeding No. 15350. This course would avoid burdening the parties and the Commission with the complication, expense, and administrative inconvenience of proceeding simultaneously on applications regarding multiple rule changes that raise the same fundamental issues. Each of the rule changes at issue involves fees for market data that the relevant exchange has purported to justify based on the alleged existence of competition, without providing any evidence of cost. As a result, the core legal issue presented by each of these rule changes is the same—*i.e.*, what evidence is necessary to show that a fee is consistent with the requirements of the Exchange Act and applicable regulations, consistent with the decision in *NetCoalition I*.

By first considering the rule change at issue in Proceeding No. 15350, while holding SIFMA's other application in abeyance, the Commission would be able to resolve this common legal question in a timely and cost-effective manner that would expedite the subsequent consideration of other rule changes. Moreover, proceeding in this manner would not prejudice the Exchanges because (1) their rule changes will remain in effect during the pendency of the proceedings, *see* 15 U.S.C. § 78s(b)(3); SEC Rule of Practice 420(d); (2) any Exchange that wishes to present its views to the Commission in Proceeding No. 15350 has a mechanism by which it may seek leave to do so, *see* SEC Rule of Practice 210; and (3) the Exchanges would retain the ability in future proceedings to defend their rule changes under the legal rule the Commission adopts in Proceeding No. 15350.

In contrast, consolidation of these proceedings would be unwieldy. Far from being "appropriate to avoid unnecessary cost or delay," SEC Rule of Practice 201(a), consolidation would significantly complicate the proceedings and likely would increase both the cost and length of time required to resolve the fundamental legal issue before the Commission.

Proceeding No. 15351 involves 23 separate rule changes by 15 different SROs, implicating a variety of market data products. Although these rule changes likely could be addressed quickly and efficiently once the applicable legal standard is resolved in Proceeding No. 15350, it would be highly inefficient to attempt to resolve the common legal question in a proceeding that required the consideration of two dozen separate rule changes involving different limitations to different products and services. Moreover, given that the Exchanges continue to file new rule changes imposing fees for market data, and continue to assume competition without providing any evidence of their costs,[3] it would not be practicable to address in a single consolidated proceeding every rule change that implicates the same legal issues as will be resolved in Proceeding No. 15350.

The Nasdaq Stock Market LLC, NASDAQ OMX PHLX, and EDGX Exchange, Inc. have represented that they "do not object to holding proceedings regarding the merits of the majority of these rule changes in abeyance until the NYSE Arca application [in Proceeding No. 15350] is resolved," but requested that "one of the rule challenges not be held in abeyance and be considered in conjunction with the NYSE Arca matter" in order to ensure that they "have a full and fair opportunity to represent their interests in future proceedings." Notice of Appearance of The Nasdaq Stock Market LLC, *In re Application of Securities Industry and Financial Markets Association*, Admin. Proc. No. 3-15351 (June 18, 2013); *see* Notice of Appearance of EDGX Exchange, Inc., *In re Application of Securities Industry and Financial Markets Association*, Admin. Proc. No. 3-15351 (June 18, 2013) (same). For the reasons set forth above, this requested

[3] *See* Application for an Order Setting Aside Rule Changes of Certain Self-Regulatory Organizations Limiting Access To Their Services, *In re Application of Securities Industry and Financial Markets Association*, Admin. Proc. No. 3-15364 (June 17, 2013); Application for an Order Setting Aside Rule Changes of Certain Self-Regulatory Organizations Limiting Access To Their Services, *In re Application of Securities Industry and Financial Markets Association*, Admin. Proc. No. 3-15394 (July 29, 2013).

action is not necessary to preserve these exchanges' rights, particularly given that they may seek leave to participate in Proceeding No. 15350. *See* SEC Rule of Practice 210. Instead, this action would needlessly complicate and delay the Commission's resolution of the common legal questions by putting multiple fees for multiple data products at issue simultaneously. Moreover, such complication and delay would be exacerbated if the Commission were to grant similar requests by other exchanges.

To the extent the Commission concludes that it would be appropriate to proceed at this time with one of the rule changes at issue in Proceeding No. 15351, SIFMA requests that the challenge not to be held in abeyance be the one to Nasdaq Stock Market LLC Release No. 34-62907, File No. NASDAQ-2010-110 (Sept. 14, 2010), *available at* http://www.sec.gov/rules/sro/nasdaq/2010/34-62907.pdf. Like the NYSE Arca rule change at issue in Proceeding No. 15350, this rule change involves fees for a depth-of-book data product, and thus would limit the complication and delay that might be caused by factual variations, which may exist for other rule changes.

IV. There Is No Need For Further Factual Development Through An Evidentiary Hearing Or Other Proceedings.

Proceedings to further develop the factual record, whether through an evidentiary hearing or otherwise, are neither necessary nor appropriate for the consideration of SIFMA's applications. Section 19(f) provides that the hearing in a proceeding under Section 19(d) "may consist solely of consideration of the record before the self-regulatory organization and opportunity for the presentation of supporting reasons to dismiss the proceeding or set aside the action." 15 U.S.C. § 78s(f). In these proceedings, the "record before the self-regulatory organization" is clearly identifiable and should be considered closed.

When, as in these proceedings, the limitation on access is imposed by the terms of a rule change, the "record before the self-regulatory organization" consists of the materials submitted in support of the change pursuant to Section 19(b)(1), which requires the SRO to file with the Commission not only a copy of the rule change itself, but a statement of the "basis and purpose" for the change. 15 U.S.C. § 78s(b)(1). Pursuant to the Commission's regulations, that submission must provide the SRO's full justification for the rule change, complete with supporting materials. *See* General Instructions, Form 19b-4 (17 C.F.R. § 249.819); 17 C.F.R. § 240.19b-4(b)(1) (requiring filings under Section 19(b)(1) to be made using Form 19b-4). In particular, the submission must "[e]xplain why the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder," General Instructions § I.3.b, Form 19b-4, and "should be sufficiently detailed and specific to support [such] a finding," *id.* § I.3.a. These requirements are necessary because the filing "is intended to elicit information necessary for the public to provide meaningful comment on the proposed rule change ... and for the Commission to determine whether the proposed rule change ... is consistent with the requirements of the [Exchange] Act and the rules and regulations thereunder." *Id.* § B.

Neither the Exchange Act nor the applicable rules and regulations provide for this record to be supplemented in a Section 19(d) proceeding. And for good reason. If an SRO were to present additional evidence in a Section 19(d) proceeding to show that its rule change is consistent with the Exchange Act and applicable regulations, it would mean that the materials submitted with its filing under Section 19(b)(1) were incomplete and did not provide the complete record necessary for the Commission and the public to evaluate the merits of the rule change, as Form 19b-4 requires. Moreover, where, as here, the rule change is one that takes effect upon filing with the Commission, an SRO should not be permitted to implement the new

rule and later, when challenged, rely upon additional evidence that was not available at the time for public comment or during the window for temporary suspension under Section 19(b)(3)(C).

V. Preliminary Briefing On Other Issues Is Not Necessary At This Time.

SIFMA is not aware of any other issues on which briefing would be appropriate at this time, although it is possible that other issues will arise as the matter proceeds.

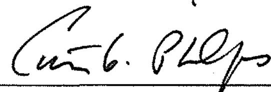
CONCLUSION

For the foregoing reasons, SIFMA respectfully requests that the preliminary matters on which the Commission requested briefing be resolved in the manner set forth above.

Dated: August 30, 2013

Respectfully submitted,

SIDLEY AUSTIN LLP



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