UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In The Matter of the Application of

SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION

Admin. Proc. File No. 3-15350

For Review of Action Taken by Certain Self-Regulatory Organizations

BRIEF OF THE NASDAQ STOCK MARKET LLC IN OPPOSITION TO SIFMA'S AMENDED REQUEST FOR ISSUANCE OF SUBPOENAS PURSUANT TO RULE 232 OF THE COMMISSION'S RULES OF PRACTICE

The Nasdaq Stock Market LLC ("Nasdaq") respectfully opposes the Securities Industry and Financial Markets Association's ("SIFMA") Amended Request for Issuance of Subpoenas Pursuant to Rule 232 of the Commission's Rules of Practice (the "Amended Requests"). The Amended Requests remain oppressive and unduly burdensome notwithstanding SIFMA's revisions. *See* SEC Rule 232(b). Moreover, as Your Honor stated during the December 18, 2014 prehearing conference, the exchanges have the right to define the scope of the evidence on which they will rely to defend their fees and cannot be compelled by these subpoena requests to relinquish that right. Accordingly, Nasdaq respectfully asks that the Amended Requests be quashed.

Nevertheless, Nasdaq is willing voluntarily to provide some of the evidence sought by SIFMA, in the form of the materials upon which its expert will rely, which it will disclose along with its prehearing submissions due on January 20, 2015. Unlike the materials that SIFMA seeks in its Amended Requests, these materials are closely associated with Nasdaq's presentation and can be produced without delaying or expanding the proceedings. Moreover, to the extent that SIFMA will be presenting testimony or other evidence from its members at the hearing, or if SIFMA's experts will be relying on documents from, or communications with, SIFMA's members in forming their opinions, Nasdaq requests that it be provided with discovery from those members that parallels the discovery that is required from the exchanges.

I. BACKGROUND

On December 4, 2014, SIFMA submitted a request pursuant to Rule 232 of the Commission's Rules of Practice for issuance of subpoenas directed to Nasdaq and NYSE Arca, Inc. ("NYSE Arca"). Nasdaq and NYSE Arca responded with a December 17, 2014 letter explaining that SIFMA's requests are oppressive and unduly burdensome. During the December

18, 2014 prehearing conference—in which Request Numbers One, Two, Three, Five, and Ten were resolved—Your Honor agreed with the exchanges that the five remaining requests were unduly burdensome. *See, e.g.*, Tr. at 34 ("[R]ight off the top, this seems to me to be a very burdensome kind of thing."); *id.* at 38-39 ("This request seems awfully nebulous. . . . And these kinds of questions are open-ended."). In an effort to salvage its overly broad requests, SIFMA asked for "the equivalent of a mulligan, a do-over," *id.* at 26, which Your Honor granted, instructing SIFMA to "whittle . . . down" its far-reaching requests, *id.* at 43.

SIFMA filed its Amended Requests on December 19, 2014. SIFMA's filing provides proposed revisions to Request Numbers Four, Six, Seven, and Nine and withdraws Request Number Eight.

II. ARGUMENT

A. SIFMA's Amended Requests Are Unduly Burdensome

Notwithstanding SIFMA's revisions, the Amended Requests remain oppressive and unduly burdensome, and should therefore be quashed. SEC Rule 232(b). By way of example, Request Number Four now seeks:

> Existing non-public Documents provided to Your decision-makers on setting fees for Your depth-of-book products challenged in this proceeding sufficient to identify Your considerations and reasons for setting or maintaining the fees for those products, including Documents sufficient to identify: Your reasons for setting prices at a particular level; and/or the relationship between Your challenged depth-of-book data fees and Your order flow.

Amended Requests at 3. Like the previous version of this request, this revised version would impose undue costs and burdens on Nasdaq by requiring a full review and production from the email and other custodial files for all "key . . . persons" involved in setting market-data fees. *Id.* at 2. The Amended Requests for Numbers Six, Seven, and Nine would require similarly oppressive culling and review of documents from numerous custodians with a role in the pricing,

and overall competitive and strategic positioning, of the Nasdaq depth-of-book product at issue in this proceeding. Compliance with these requests is not possible within the current case schedule, even if Nasdaq were to divert all of its resources away from preparing its submission on the merits and instead focus solely on producing documents. As Your Honor recognized, the collection and review process requested by SIFMA imposes extreme burdens. *See, e.g.*, Tr. at 41-42 ("I'm sorry, Mr. Warden, but this is the -- I think it's the 18th of December, and they're going to give you a lot of material on January 20th, and you want them to give you additional material. And I just -- it -- to me it's just not something that they can just do a computer run and give it to you. This is going to be a -- the way these questions are framed, they would have to really hold interviews with a lot of people and put together a lot of material . . . ."). Thus, even these "narrowed" versions of the requests would inevitably require a continuance of the existing case schedule.

SIFMA's proposal to limit the requests to "those books, records, or individually-held documents as are created or maintained in the ordinary course of business" does nothing to ease the burdens placed on Nasdaq by the Amended Requests. Amended Requests at 2. Even if no new documents must be created, the burden of searching for and analyzing existing documents is substantial. *Cf.* Tr. at 39 ("You know, around the Commission they send around and they'll tell all of us, if we've ever had anything to do with any specific case, we have to go through our files and -- it's just -- it's just an awful lots of responsibility to take on.").

Moreover, SIFMA's purportedly narrowed requests continue to seek all documents stretching back for over *eight* years, to August 1, 2006, even though the two rule changes at issue

here were filed in 2010.[1] SIFMA's ongoing demand for documents pre-dating the relevant rule changes by over four years belies any suggestion that its Amended Requests are narrow. If SIFMA's still-overbroad requests have "significantly narrowed," Amended Requests at 3, it is only because its original requests were—in Your Honor's own words—so "burdensome," "nebulous," and "open-ended" in the first place, Tr. at 34, 38-39.

In addition, SIFMA has failed to show any need that could justify the burdens these requests would impose on Nasdaq. As discussed in the exchanges' previous letter, SIFMA has already represented to the Commission that Nasdaq's rule changes "limit access to critical market data for anyone unwilling to pay the onerous, supracompetitive fees" Nasdaq is charging, *Application for an Order Setting Aside Rule Changes of Certain Self-Regulatory Organizations Limiting Access to Their Services*, Admin. Proc. File No. 3-15351, at 2 (May 30, 2013), and has submitted nine declarations claiming that members are "aggrieved because [they] believe[] that the level of the prices charged . . . is so high as to be outside a reasonable range of fees" under the Exchange Act, *Brief of SIFMA Regarding Satisfaction of Jurisdictional Requirements*, Admin. Proc. File No. 3-15350, at Ex. 1 (July 28, 2014). Presumably SIFMA and its members had some factual basis for making these claims, and they can present those facts at the hearing. If, on the other hand, SIFMA and its members submitted their petitions and declarations without facts to support them, that absence of factual support should be acknowledged and cannot

[1] The Nasdaq rule change at issue modifies Nasdaq Rule 7019 by requiring distributers receiving the data feed containing the Level 2 entitlement to pay distributer and direct access fees for Nasdaq-listed securities. *See* Release No. 34-62907, File No. SR-NASDAQ-2010-110 (Sept. 14, 2010). The relevant NYSE Arca rule change authorizes market data fees for the receipt and use of its ArcaBook product. *See* Release No. 34-63291, File No. SR-NYSEArca-2010-97 (Nov. 9, 2010).

provide a basis for an immense fishing expedition. The more appropriate result would be dismissal of SIFMA's petitions.

As Your Honor acknowledged, the burdens placed on Nasdaq by SIFMA's Subpoena Requests are particularly acute at this late stage of the proceeding, when Nasdaq is preparing its submission on the merits under Your Honor's scheduling order. Tr. at 38-39. Nasdaq is currently "preparing a positive presentation, and the people involved in making decisions of what [Nasdaq] should submit to the Commission as part of that presentation are the same people who are going to be answering this kind of a request." *Id.* at 39. Accordingly, SIFMA's request for wide-ranging discovery would unfairly prejudice Nasdaq by forcing it to divert its resources and attention away from addressing this significant case on the merits. SIFMA's proposal to set a compliance deadline for Requests Numbers Four and Nine of February 9, 2015—while imposing a January 20 deadline for Requests Numbers Six and Seven—does not come close to relieving the serious prejudice that Nasdaq would face if it were forced to process a massive document production and review at the same time it was preparing its affirmative evidentiary presentation.

In light of the short time available for Nasdaq to prepare its case, and the broad and unduly burdensome nature of SIFMA's Amended Requests, Nasdaq respectfully submits that the requests should be quashed based on prior Commission precedent. *See, e.g., Order on Subpoenas*, Admin. Proc. File No. 3-14848 (Aug. 20, 2012) (Murray, Chief ALJ) (denying motion for issuance of a subpoena on the grounds that it was "unreasonable, excessive in scope, and unduly burdensome at this late date," because the subpoena would "require a party to undertake data collection just as it is preparing to submit a prehearing brief . . . and is preparing its case in chief," and because the party seeking the subpoena "gave no notice that he was going to file the motion at . . . the prehearing conference"); *see also Order on Application to Quash,*

Admin. Proc. File No. 3-14697 (Apr. 27, 2012) (Murray, Chief ALJ) (concluding that subpoena requests were unreasonable and unduly burdensome where gathering the requested information would take weeks or months due to, in part, the passage of four years and the changes in personnel and computer systems); *Order on Portion of Motion to Dismiss and Motion to Issue Subpoena*, Admin. Proc. File No. 3-14676 (Feb. 21, 2012) (Murray, Chief ALJ) (denying motion for subpoena as unreasonable and excessive where "Respondents did not mention their intent to request subpoenas at the prehearing conference").

B. The Exchanges Should Be Permitted To Define The Scope Of The Evidence On Which They Will Rely To Defend Their Fees

In addition to being oppressive and unduly burdensome, SIFMA's Amended Requests improperly seek to interfere with the exchanges' right to define the scope of the evidence on which they will rely to defend their fees by forcing them to provide data regarding their costs and profitability. *See, e.g.*, Amended Requests at 4, 6 (seeking documents identifying "the costs of Your data collection and distribution infrastructure" and "the profitability and revenue of Your depth-of-book data products"). SIFMA's effort in this regard will only serve to—and is plainly designed to—expand the scope of these proceedings by creating a sideshow surrounding cost and profitability data that will not be introduced by the exchanges themselves. As Your Honor stated repeatedly at the prehearing conference, Nasdaq cannot be compelled to present its case in any particular manner.

SIFMA has sought for years to have the Commission jettison its market-based approach to evaluating fees in favor of a cost-based rate-making approach, but the Commission has consistently rejected SIFMA's efforts. Indeed, in establishing this proceeding, the Commission ordered that this Tribunal's analysis should be "informed by the two-part test set out in [the Commission's] 2008 ArcaBook Approval Order," *Order Establishing Procedures and Referring*

Applications for Review to Administrative Law Judge for Additional Proceedings, Admin. Proc. File No. 3-15350, 3-15351, at 20 (May 16, 2014), in which the Commission expressly rejected SIFMA's proposed cost-based approach. Likewise, the Commission ordered that this Tribunal be informed by the decision in *NetCoalition I*, in which the D.C. Circuit expressly *approved* the Commission's market-based approach against challenges requesting a cost-based approach, but required further evidence regarding the existence of competitive forces that constrain pricing. *NetCoalition v. SEC (NetCoalition I)*, 615 F.3d 525, 534 (D.C. Cir. 2010). As the exchanges' December 17, 2014 letter explains, SIFMA's requests for cost data are merely thinly veiled attempts to turn this proceeding into the type of agency ratemaking that the Commission and other agencies have sought to limit in recent decades—and to do so without any congressional authorization. *See, e.g., Elizabethtown Gas Co. v. FERC*, 10 F.3d 866, 870 (D.C. Cir. 1993) (upholding FERC's decision to "rely upon market-based prices in lieu of cost-of-service regulation"); *Report of the Advisory Committee on Market Information: A Blueprint for Responsible Change*, at § VII.D.3 (SEC Sept. 14, 2001) ("[T]he 'public utility' cost-based ratemaking approach . . . is resource-intensive, involves arbitrary judgments on appropriate costs, and creates distortive economic incentives.").[2]

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[2] SIFMA disagrees with this assessment, claiming that "in requesting this information, it is not seeking to transform this proceeding into anything akin to cost-based ratemaking." Amended Requests at 6. However, in representing that the "relationship between price and marginal cost" is relevant to this proceeding, *see id.*, SIFMA is necessarily taking the position that depth-of-book pricing is not constrained by competition, and that prices must therefore be constrained by some form of regulation or regulatory oversight comparing prices to costs. Thus, although SIFMA may not be advocating strict, cost-of-service ratemaking, its position has the well-known drawbacks of cost-based price regulation. Moreover, SIFMA's position directly contradicts *NetCoalition I*, in which the D.C. Circuit explained that "the SEC itself intended in Regulation NMS that 'market forces, rather than regulatory requirements' play a role in determining the market data . . . to be made available to investors and at what cost." *See NetCoalition I*, 615 F.3d at 537 (citation omitted). By expressly rejecting an argument

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In light of the Commission's express and consistent rejection of SIFMA's calls for cost-based pricing in favor of an analysis of the extent to which competitive forces constrain market data pricing, SIFMA should not be permitted to sidetrack this proceeding into an exercise in cost-based pricing. Nor should Nasdaq be compelled to present such data in this proceeding. Your Honor appropriately expressed this position throughout the prehearing conference, explaining to SIFMA that the exchanges have the burden of proof and can decide how best to present their case:

> But Mr. Warden, what you're forgetting is they've got the burden of proof. They have to prove the things are reasonable. You've got -- you know you -- you're not in the catbird seat, but they've got the burden of proof. They've got to come in with evidence and you're going to see what they come in with. I mean, we've got a schedule and they have to give you the exhibits and they have to give you the list of witnesses, which I've limited -- number. So I just don't go along with what you say.

Tr. 26-27. In response to SIFMA's insistence that the exchanges will simply "cherry pick" the most favorable materials in building their case, Your Honor made clear that the evidence provided by the January 20, 2015 disclosures will be adequate for SIFMA to test the exchanges' claims. *See id.* at 40 ("No, wait a minute. Wait a minute, I'm going to answer that first part. You're going to answer it because you're going to get the person's name and you're going to get the exhibits that the person's going to use to support his position on January 20th."). Your Honor further emphasized that the exchanges have no obligation to turn over other evidence that might support, detract from, or otherwise be relevant to their arguments—as long as the

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that "Congress intended 'fair and reasonable' to be determined using a cost-based approach" and instead agreeing with the Commission that "its market-based approach is fully consistent with the Exchange Act," *id.* at 534, the D.C. Circuit made clear that where an exchange presents evidence of competitive constraints on pricing (which Nasdaq will provide here), cost-based analysis is unnecessary.

exchanges do not introduce that evidence in defense of their fees. *See id.* at 41-42 ("[Y]ou say pick and choose; of course they're going to pick and choose. That's their job. . . . They're going to make the best case they can for their client, and you're going to make the . . . best case for your client. . . . there's no impetus on them to give you any kind of Brady material or Jencks material. So you know, you got a hard row to hoe, but that's it. That's the name of the game."). Finally, Your Honor stated clearly and unequivocally that the exchanges have the right to define the scope of evidence on which they will rely in defending their fees:

> And if they decide that what he's described as the route that they're going to take to show that these costs . . . or changes in the charges are reasonable, that's their -- that's their choice. If I decide that they've left a very strong element out of their proof, you know, that's something else to be considered. If you make the position that they should have produced costs and they failed to do so, and that's a major deficiency, and I buy it, well, then that's fine. But I can't tell them how to present their case, and I'm not going to do that. That's their choice. So if they're not going to cover costs, fine, they're not going to cover costs.

Id. at 47. Consistent with Your Honor's statements at the prehearing conference, the Amended Requests should be quashed because granting them would preclude Nasdaq from deciding "how to present [its] case" and from exercising its option "not . . . to cover costs." *See id.*

C. SIFMA Will Receive More Than Adequate Evidence From Nasdaq Without The Amended Requests

Despite the oppressive and unduly burdensome nature of SIFMA's Amended Requests, Nasdaq is prepared to produce some of the evidence sought by SIFMA. As indicated during the prehearing conference, the exchanges do not object to providing SIFMA with the facts and data upon which their testifying experts rely in forming their opinions. *See* Tr. at 29 ("We have no objection to . . . giving them the reliance data, so the underlying data that, you know, the experts are going to use to prepare charts and whatever it is that they end up producing."); *id.* at 37 ("Obviously, if there's something that we are going to rely on as part of our case in chief or procedure in chief, we are going to produce that under Your Honor's schedule. You know, if it's

a document that one of our -- that our fact witness, for example, is going to testify about, then we're going to produce that."). As Your Honor recognized, the disclosure of this evidence is sufficient to permit SIFMA to build its case. *See, e.g., id.* at 26-27 ("They've got to come in with evidence and you're going to see what they come in with.").

Nasdaq will produce its expert reliance materials on January 20, 2015, simultaneously with its prehearing submissions due that day.

D. Nasdaq Is Entitled To Reciprocal Discovery If SIFMA Directly Or Indirectly Introduces Evidence From Its Members

Finally, in the event that SIFMA intends to present evidence from its members, directly or indirectly, Nasdaq respectfully requests that it be provided with discovery from those members that parallels the discovery required from the exchanges. Basic fairness requires that the parties be treated equally with respect to the benefits and burdens of discovery. With regard to each category of discovery already required from the Exchanges—and any additional categories that Your Honor might require—Nasdaq requests reciprocal discovery from SIFMA's members to the extent that SIFMA intends to introduce or otherwise rely on evidence from its members. Nasdaq sought SIFMA's position on this request on Friday, December 26, 2014, but SIFMA has not yet provided a position.

Nasdaq initially requested reciprocal discovery from SIFMA's members during a meet and confer discussion on December 16, 2014. In response, counsel for SIFMA stated that he does not represent SIFMA's members and has not collected any evidence from them. At the same time, he indicated that SIFMA members would be providing input and information to SIFMA's experts. Based on those representations, we understand that SIFMA will not be presenting testimony or other evidence at the hearing directly from SIFMA's members but will be using its experts to present such evidence indirectly.

It would be unfair to permit SIFMA to filter information in this manner—simultaneously claiming that it does not have access to members' information while supplying materials from its members to its experts for presentation in this proceeding. Quite simply, if SIFMA will be presenting testimony or other evidence from its members at the hearing, or if SIFMA's experts will be relying on documents from, or communications with, SIFMA's members in forming their opinions, Nasdaq requests that it be provided with reciprocal discovery from those members. Such discovery is necessary to permit Nasdaq to effectively cross-examine SIFMA's witnesses. Likewise, it would be unfair to afford SIFMA the benefit of discovery regarding the depth-of-book products at issue without also affording Nasdaq comparable discovery regarding the basis for SIFMA's affirmative evidentiary presentation.

To the extent SIFMA's presentation encompasses, directly or indirectly, evidence from SIFMA's members, Nasdaq would request the following discovery from all SIFMA members who provide documents or communications to SIFMA's expert witnesses, those SIFMA members from whom SIFMA will present evidence or testimony, and the nine SIFMA members who submitted jurisdictional declarations (collectively, the "Relevant Members"):

- Documents sufficient to identify, for each Relevant Member who redistributes the specific depth-of-book products that are the subject of the rule change at issue, the total number of subscribers for each product and any changes in the number of subscribers on a monthly basis from the time the rule change was adopted to the present.

- Documents sufficient to identify, for each Relevant Member who redistributes the specific depth-of-book products that are the subject of the rule change at issue, the aggregate fees charged to subscribers for the products on a monthly basis from the time the rule change was adopted to the present.

- Documents sufficient to identify, for each Relevant Member who subscribes to the specific depth-of-book products that are the subject of the rule change at issue, NYSE's and Nasdaq's share of the SIFMA member's order flow and any changes in that share throughout the period from the time the rule change was adopted to the present.

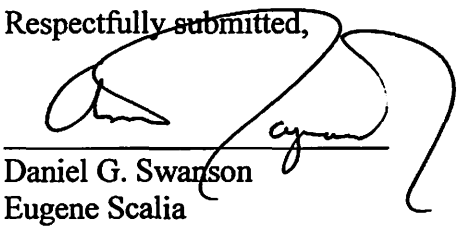
- Marketing, promotion, and advertising materials, for each Relevant Member who redistributes the specific depth-of-book products that are the subject of the rule change at issue, used to promote the products from the time the rule change was adopted to the present.

Nasdaq reserves the right to request additional discovery from SIFMA's members in the event that Your Honor grants additional discovery to SIFMA.

III. CONCLUSION

For the foregoing reasons, SIFMA's amended Subpoena Requests should be quashed.

Respectfully submitted,



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Dated: December 29, 2014

CERTIFICATE OF SERVICE

I hereby certify that on December 29, 2014, I caused a copy of the foregoing Brief of the Nasdaq Stock Market LLC in Opposition To SIFMA's Amended Request for Issuance of Subpoenas Pursuant to Rule 232 of the Commission's Rules of Practice to be served on the parties listed below via First Class Mail. Service was accomplished on SIFMA and the Exchanges via First Class Mail because of the large service list.

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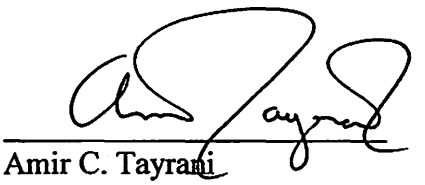

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