

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

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**Petition**

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**for**

Re: Securities Exchange Act Release No. 54597 (October 12, 2006), :

File No. SR-NYSEArca 2006-21 :

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NOW COMES NETCOALITION,<sup>1</sup> PETITIONER, requesting that the U.S. Securities and Exchange Commission (the “SEC” or “Commission”), pursuant to Rule 430 of the Commission’s Rules of Practice, 17 C.F.R. § 201.430, review and set aside the action of the Division of Market Regulation approving by delegated authority a proposed rule change filed by NYSEArca, Inc. (“NYSEArca”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Exchange Act”), 15 U.S.C. § 78s(b)(1), as announced in the above-captioned release.

**Background**

On May 23, 2006, NYSEArca filed with the Commission, pursuant to Exchange Act Section 19(b)(1) and Rule 19b-4 thereunder, 17 C.F.R. § 240.19b-4, a proposed rule change to establish fees for the receipt and use of certain market data that NYSEArca has up until now made available without charge. The Commission published the proposal for comment in the Federal Register on June 9, 2006. Securities Exchange Act Release No. 53952 (June 7, 2006), 71 FR 33496. The Commission received four comment letters regarding the proposal.<sup>2</sup> On July

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<sup>1</sup> NetCoalition is a public policy voice for some of the world’s most innovative companies on the Internet. Its trustees include CNET Networks, Bloomberg L.P., Google, IAC/Interactive Corp and Yahoo!.

<sup>2</sup> Letters from Gregory Babyak, Chair, Market Data Subcommittee, the Securities Industry Association (“SIA”), and Christopher Gilkerson, Chair, Technology and Regulation Committee, SIA, to Nancy M.

*(Footnote continued)*

25, 2006, and August 25, 2006, NYSEArca filed letters responding to the issues raised in the comment letters.<sup>3</sup> The proposed rule change was approved by the Division of Market Regulation pursuant to delegated authority on October 12, 2006. Release No. 34-54597 (October 12, 2006). The order was published in the Federal Register at 71 FR 62029 (October 30, 2006). On November 6, 2006, Petitioner filed notice with the Commission of its intention to file this Petition.

### **Applicable Legal Requirements**

Rules 430 and 431 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.430 and 201.431, provide for Commission review of staff action taken by delegated authority upon request by, *inter alia*, a person aggrieved by the staff's action. Rule 430 states the procedural (including timing) requirements to file a petition for review, and Rule 431 contains the requirements pertaining to the Commission's review of the petition. Rule 431 provides that the Commission, in determining whether to grant review in response to a petition such as this one, shall look to the standards set forth in Rule of Practice 411(b)(2), 17 C.F.R. § 201.411(b)(2), *viz.*, whether the decision embodies, *inter alia*, (a) a conclusion of law that is erroneous, or (b) an exercise of discretion or decision of law or policy that is important and that the Commission should review.

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Morris, Secretary, SEC, June 30 and August 18, 2006; web comment from Steven C. Spencer, Esq., June 18, 2006; and letter from Markham C. Erickson, Executive Director and General Counsel, NetCoalition, to the Honorable Christopher Cox, Chairman, SEC, August 9, 2006.

<sup>3</sup> Letters from Janet Angstadt, Acting General Counsel, NYSE Arca, Inc., to Nancy M. Morris, Secretary, SEC, July 25 and August 25, 2006.

To be appropriate for review, an action by delegated authority needs to meet only one of these criteria. As we demonstrate below, however, the instant action by delegated authority meets both. The Commission's staff has reached an erroneous conclusion of law by misapplying the Exchange Act standards applicable to NYSEArca in approving the instant rule proposal. Its action is therefore inconsistent with the Exchange Act and should be set aside. The staff's action by delegated authority, moreover, involves an exercise of discretion or decision of law or policy that is important and that the Commission should review. For the reasons stated below, the subject matter of the instant rule filing goes to the heart of market data distribution and may well threaten the national market system objectives enunciated by the Congress in the Securities Acts Amendments of 1975, Act of June 4, 1975, 89 Stat. 114 (the "1975 Amendments"), which imposed rulemaking requirements on the exchanges in Exchange Act Section 6(b), 15 U.S.C. § 78f(b), and added to the Exchange Act Section 11A, which calls for the Commission to use its statutory authority to facilitate the development of a national market system. Section 11A(a)(2), 15 U.S.C. § 78k-1(a)(2).

Petitioner's members, and the many millions of public investors who access their web sites daily, have been and will be injured by the unreasonable fees permitted by the staff's approval of the rule change and therefore are aggrieved by the staff's actions within the meaning of Rule 430. The instant rule proposal imposes fees that put access to the NYSEArca quotations beyond the reasonable economic reach of an advertiser-supported medium like the Internet, thereby harming the investors and the Internet service providers that are Petitioner's members. The cumulative impact of this and other pending and recently approved market data proposals threaten to place this critical data, which should be readily available to the general public, altogether beyond the reach of the average retail investor.

The instant rule filing pertains to fees for market data. Exchange Act Section 6(b)(4), 15 U.S.C. § 78f(b)(4), requires NYSEArca's rules to provide for the "equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities." In turn, Exchange Act Section 11A(c)(1)(C), 15 U.S.C. § 78k-1(c)(1)(C), and Exchange Act Rule 603(a)(1) of Regulation NMS, 17 C.F.R. §242.603(a)(1), require NYSEArca's market data fees, and other terms on which market data is being distributed, to be "fair and reasonable" where, as here, NYSEArca functions as an exclusive securities information processor. In addition, Exchange Act Rule 603(a)(2), 17 C.F.R. §242.603(a)(2), requires NYSEArca — as a national securities exchange that distributes information with respect to quotations for an NMS stock to a securities information processor, broker, dealer, or other persons — to do so on terms that are not unreasonably discriminatory. Exchange Act Section 19(b)(2), 15 U.S.C. §78s(b)(2), permits the Commission to approve a proposed rule change of NYSEArca only if it finds the rule change to be consistent with the Exchange Act provisions applicable to NYSEArca. If the Commission cannot make that finding, it must institute proceedings to determine whether the proposed rule change should be disapproved. In a doubtful case, therefore, the institution of disapproval proceedings is the only permissible Commission action.

The Congress was concerned about the market power of monopolies and made it clear in the legislative history of these provisions that exchanges enjoying monopoly franchises should be treated as public utilities:

*The Committee believes that if economics and sound regulation dictate the establishment of an exclusive central processor for the composite tape or any other element of the national market system, provision must be made to insure that this central processor is not under the control or domination of any particular market center. Any exclusive processor is, in effect, a public utility, and thus it must function in a manner which is absolutely neutral with respect to*

*all market centers, all market makers, and all private firms.* Although the existence of a monopolistic processing facility does not necessarily raise antitrust problems, serious antitrust questions would be posed if access to this facility and its services were not available on reasonable and nondiscriminatory 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 processor's neutrality and the reasonableness of its charges in practice as well as in concept.<sup>4</sup>

NYSEArca is, to be sure, an exclusive processor with respect to the data that is exclusively in its possession and that is the subject of the instant filing, depth-of-market data. In keeping with that congressional policy, the Commission itself has concluded that, in passing on a self-regulatory organization's fees, it must apply a cost-based standard. *See, e.g.*, Securities Exchange Act Release Nos. 42208 (December 14, 1999), 64 FR 70627 (Concept Release on Market Data), quoted below (the "1999 Concept Release"), and 50700 (November 18, 2004), 69 FR 71273 (Concept Release Concerning Self Regulation). In approving NYSEArca's filing, the staff did not apply a cost-based standard and, for that reason, its action should be set aside.

All self-regulatory organization rule filings, including those pertaining to fees for market data, are subject to the requirements of Form 19b-4. NYSEArca must explain and justify burdens on competition that will result from a proposed rule filing. Filings that fail to meet the requirements of Form 19b-4 are deficient as a matter of law. As explained below, the instant filing does not comply with Form 19b-4 and therefore is deficient. The staff's action by delegated authority should be set aside for that additional reason.

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<sup>4</sup> S. Rep. No. 94-75, at 11-12 (1975) (emphasis added).

## Discussion

The staff's action pursuant to delegated authority should be set aside for two principal reasons: (1) in approving the rule change by delegated authority, the staff misapplied the legal standards under the Exchange Act applicable to NYSEArca rule filings; and (2) the staff's action in approving NYSEArca's filing was arbitrary, capricious, an abuse of discretion and otherwise not in accordance with law since NYSEArca did not provide any cost analysis or justification for the level of proposed data fees, and the staff did not provide any economic analysis to support its decision to approve the rule change.

*Non-compliance with Form 19b-4.* NYSEArca's failure to observe the disclosure requirements in the Commission's own Form 19b-4 causes its filing to be legally insufficient *per se*. That legal insufficiency would, by itself, be a sufficient ground for the Commission to set aside the staff's approval by delegated authority. NYSEArca's unsubstantiated assertion that its rule change satisfies the requirements of Exchange Act Section 6(b)(4), 15 C.F.R. § 78f(b)(4), and its mere repetition in its filings *in haec verba* of the statutory standard in Exchange Act Section 6(b)(8), 15 C.F.R. § 78f(b)(8)<sup>5</sup> is inadequate. NYSEArca fails to provide any discussion or any demonstration at all that it does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of

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<sup>5</sup> Section 6(b)(8) prohibits NYSEArca rules from imposing any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act.

the Exchange Act. This lack of substantiation does not satisfy the requirements of the Commission's Form 19b-4 that such burdens be explained and justified in detail.<sup>6</sup>

As a result, NYSEArca's filing does not provide a sufficient basis for public comment on, or Commission approval of, the proposed rule change. Given the inadequacy of the record, the public is effectively deprived of a meaningful opportunity for comment on the proposed rules.<sup>7</sup> The Commission, in turn, is denied the benefit of the comments that could arise

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<sup>6</sup> As the Commission is aware, the General Instructions to Form 19b-4, 5 Fed. Sec. L. Rep. (CCH) ¶ 32,356, are explicit on the point. They provide, with respect to "Information to be Included in the Completed Form," as follows:

4. *Self-Regulatory Organization's Statement on Burden on Competition*

State whether the proposed rule change will have an impact on competition and, if so, (i) state whether the proposed rule change will impose any burden on competition or whether it will relieve any burden on, or otherwise promote, competition and (ii) specify the particular categories of persons and kinds of businesses on which any burden will be imposed and the ways in which the proposed rule change will affect them. If the proposed rule change amends an existing rule, state whether that existing rule, as amended by the proposed rule change, will impose any burden on competition. If any impact on competition is not believed to be a significant burden on competition, explain why. Explain why any burden on competition is necessary or appropriate in furtherance of the purposes of the [Exchange] Act. In providing those explanations, set forth and respond in detail to written comments as to any significant impact or burden on competition perceived by any person who has made comments on the proposed rule change to the self-regulatory organization. *The statement concerning burdens on competition should be sufficiently detailed and specific to support a Commission finding that the proposed rule change does not impose any unnecessary or inappropriate burden on competition* (emphasis added).

*Id.* at 22,318.

<sup>7</sup> To assist the Commission in its adjudicatory proceedings under the Exchange Act, NYSEArca must provide an adequate basis for comment on its rule proposals and, where significant competitive issues are involved, must provide an opportunity for the public to comment meaningfully on the issues involved. Perfunctory recitals do not provide that basis. See *Connecticut Light and Power Co. v. NCR*, 673 F.2d 525, 530-31 (D.C. Cir. 1982):

The purpose of the comment period is to allow interested members of the public to communicate information, concerns, and criticisms to the agency during the rule-making process. If the notice of proposed rule-making fails to provide an accurate picture of the reasoning that has led the agency to the proposed rule, interested parties will not be able to comment meaningfully upon the agency's proposals. As a result, the agency may operate

(Footnote continued)

from the fully-informed dialogue and genuine interchange of data, views, and arguments the Congress envisioned in fashioning the rule-approval process embodied in Section 19(b) of the Exchange Act.<sup>8</sup>

*Failure to justify fees.* The instant filing also is deficient in its purported justification of the fees to be charged. NYSEArca does not provide any data to support the summary conclusion that the fees are “an equitable allocation of overall costs” and are “fair and reasonable.” There is no information provided to help guide the Commission in determining whether the fees bear any relationship to costs, or whether the fees represent an equitable

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with a one-sided or mistaken picture of the issues at stake in a rule-making. . . . To allow an agency to play hunt the peanut with technical information, hiding or disguising the information that it employs, is to condone a practice in which the agency treats what should be a genuine interchange as mere bureaucratic sport.

<sup>8</sup> The rigorous approach built into the Commission’s Rule 19b-4 and Form 19b-4 responds to a direct, specific and unequivocal congressional mandate. *See* S. Rep. No. 94-75 at 29-30 (1975):

In order to facilitate expeditious Commission review and evaluation of [proposed rule changes] and to assure informed public comment on them, Section 19(b)(1) would require all self-regulatory organizations to file with the SEC in connection with any proposed rule change a “concise general statement of the basis and purpose” of the proposed rule change. *It is the Committee’s intention in adopting this standard to hold the self-regulatory organizations to the same standards of policy justification that the Administrative Procedure Act imposes on the SEC....*

[T]he Committee believes interested persons should have a meaningful opportunity to obtain accurate information about proposed changes in self-regulatory rules and to comment on the need or justification for these changes. Section 19(b)(1) would require the SEC to give notice and provide an opportunity for interested persons to participate in the process of reviewing a proposed change in a self-regulatory organization’s rules. In addition, this section would require that all comment and all correspondence between the SEC and the self-regulatory agency concerning the proposal be available for public inspection. . . .

The Committee believes the Commission has a responsibility to see that self-regulatory rules are fully responsive to regulatory needs. By explicitly providing that the Commission’s oversight authority encompasses major self-regulatory policies, the bill would make this responsibility clear and substantially decrease the possibility of slippage between regulatory need and self-regulatory performance [emphasis added]. . . .

allocation of the costs associated with using exchange facilities. No data are provided as to the formula — if any — on which NYSEArca relied in computing these fees. Without this information, the staff and the Commission lack a legally sufficient foundation to approve the proposed fee.

The absence of supporting cost data — and the suggestion that large fees are necessary to cover these undefined costs — are particularly noteworthy when one considers that, as an independent entity, Arca thrived while *giving away* its market data. This model of giving away market data — which was the norm for ECNs — suggests that additional trading volume has generated sufficient fees to offset the apparently modest costs of consolidation and dissemination. The policy of giving away market data was true not only of new ECNs, attempting to establish a foothold in the market, but also of established ECNs — INET, Island, Archipelago, and BRUT — which often commanded a larger share of Nasdaq volume than Nasdaq itself.

NYSEArca's new owners are legally entitled under the Exchange Act to change this free data policy and to charge for this data. They are not, however, legally entitled to do so without evidence of a cost basis to support the proposed fees. There has been offered no reason to suspect that the cost of producing this data — which seems to have been minimal — has suddenly skyrocketed.

The Securities Industry Association, in its comments opposing the NYSEArca filing, speaks to the fatal shortcomings of the NYSEArca filing, particularly the “compare to another monopoly” standard of setting market data fees:

In the absence of supporting data, the filing offers a circular argument that should be rejected by the Commission. The only justification offered in File No. SR-NYSEArca-2006-21 is that the NYSEArca Market Data fee “compares favorably” with Nasdaq's and NYSE's own depth-of-book products. Fees for Nasdaq's

depth-of-book product, TotalView, were approved without supporting information. Fees for NYSE's depth-of-book product, OpenBook, were approved with the NYSE referencing Nasdaq's unsubstantiated TotalView fees. Now, NYSEArca cites the NYSE's unsubstantiated fees that in turn cite Nasdaq's unsubstantiated fees to justify its own unsubstantiated fees. If any of these fees had been set by market forces, there would be some justification for citing them as part of the documentation in support of a fee filing, but that is not the case here.<sup>9</sup>

The Commission has long recognized that exchange market data fees should be subject to a rigorous cost-based analysis. The Commission itself recognized this in its 1999 Concept Release on Regulation of Market Data Fees and Revenues:

Congress did not include a strict, cost-of-service standard in Section 11A of the Exchange Act, opting instead to allow the Commission some flexibility in assessing the fairness and reasonableness of fees. Nevertheless, the fees charged by a monopolistic provider of a service (such as the exclusive processors of market information) need to be tied to some type of cost-based standard in order to preclude excessive profits if fees are too high or underfunding or subsidization if fees are too low. The Commission therefore believes that the total amount of market information revenues should remain reasonably related to the cost of market information. . . .

The first step in determining the cost of market information is to identify, in theory, the categories of costs that are incurred to generate and disseminate market information. The second step is to allocate appropriately the amount of the costs included in these categories, which requires a determination of whether the relevant categories are 'direct costs' of market information or 'common costs.' Direct costs (also referred to as incremental, separable, or traceable costs) are incurred only to provide market information and therefore can be allocated entirely to the cost of market information. Common costs, in contrast, are incurred for the provision of services in addition to market information and therefore should be allocated among each of the various services they support.

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<sup>9</sup> Letter from Gregory Babyak, Chair, Market Data Subcommittee, the Securities Industry Association ("SIA"), and Christopher Gilkerson, Chair, Technology and Regulation Committee, SIA, to Nancy M. Morris, Secretary, SEC, June 30, 2006, *available at* <http://www.sec.gov/comments/sr-nysearca-2006-21/gbabyak5693.pdf>. *See, e.g.*, letter dated July 25, 2006 to the Commission from Janet Angstadt, Acting General Counsel, NYSE Arca Inc., in SEC File No. SR-NYSEArca 2006-21, *available at* <http://www.sec.gov/comments/sr-nysearca-2006-21/nysearca200621-3.pdf>.

Failing to allocate common costs in this way would improperly inflate the cost of market information.<sup>10</sup>

The staff has departed markedly from the Commission's wise counsel and has applied its own monopoly-to-monopoly standard of review, which amounts to a non-review and is inconsistent with the Exchange Act. Investors have no protection when one entity operating as a monopoly justifies its fees by pointing to the unexamined fees of another monopoly. The Exchange Act intended that the Commission protect investors from monopolies, not that the Commission ensure parity among monopolies. Certainly the Commission's interpretation of the Exchange Act, articulated in the 1999 Concept Release, bears this out.

### **Market Data and the Internet**

The Internet is one of the most dynamic forces in our economy, creating new ways of doing business and providing unprecedented convenience, choice and access to information for hundreds of millions of users worldwide. The ready availability of market data coupled with the technology of the Internet has helped revolutionize the financial services sector. The phenomenon of the "Investor Class" — in which unprecedented numbers of Americans are actively managing their own portfolios to plan for retirement, education, major purchases and more — would be unimaginable without the Internet. The individual investor has been empowered with information, and our capital markets have been the beneficiaries.

Financial web sites received 48,802,000 "unique visitors" in May of 2006.<sup>11</sup> As each unique visitor is tied to the IP address<sup>12</sup> of the user, this is essentially a fingerprint that

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<sup>10</sup> 1999 Concept Release in text accompanying n.119 [footnote omitted].

<sup>11</sup> ComScore Media Matrix Releases May Top 50 Web Rankings at <http://www.comscore.com/press/release.asp?press=906>.

suggests that, indeed, approximately 50 million Americans visit a major Internet financial web site every month. A recent study demonstrates that financial web sites are the number one source of financial news and investment information used by U.S. investors. Financial web sites are relied upon by 54% of U.S. investors, outpacing local newspapers (43%), magazines (32%), television (28%), and radio (11%).<sup>13</sup> These web sites offer a variety of financial information, but our members' experience suggests that the overwhelming majority of these visitors are looking for the market data that is essential to trading.

Historically, ECNs have made their books available for free. Our members' customers were able to use that free ECN data, not only to facilitate informed trading on those ECNs, but also as a proxy to provide some insight into prices on Nasdaq, and, to a lesser extent, the NYSE. As a result of the mergers and transformation into for-profit entities, the NYSE and Nasdaq have removed the option of retail investors obtaining any meaningful sense of the Nasdaq and NYSE markets, short of purchasing Nasdaq, NYSE or NYSEArca data.

The Division of Market Regulation has opined to us that charging for the book — as the NYSE and Nasdaq intend — is a smarter business decision than the ECN practice of providing it for free. We are told that NetCoalition's members and their customers can expect to

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<sup>12</sup> Wikipedia defines IP address as follows:

An IP address (Internet Protocol address) can . . . be thought of as the equivalent of a street address or a phone number . . . for a computer or other network device on the internet. Just as each street address and phone number uniquely identifies a building or telephone, an IP address can uniquely identify a specific computer or other network device on a network.

*Wikipedia*, available on the Internet at: [http://en.wikipedia.org/wiki/IP\\_address](http://en.wikipedia.org/wiki/IP_address).

<sup>13</sup> e-Rewards Market Research commissioned by Scottrade, August 2006.

pay a great deal of money for market data. The offsetting virtue of this additional cost is, according to the Division staff, the belief that investors are going to see much greater “innovation” from the exchanges than we have in the past.

We are skeptical. Certainly there is nothing in any of the filings, or in our experience, to support the assertion that “innovation” will be on the rise, certainly not enough innovation to offset the diminution of transparency inherent in millions of investors being summarily cut-off from this data. In our experience, innovation in this market has come from ECNs, competing without the benefit of a government-sponsored market data monopoly. Indeed, on the trade-execution side, the market-driven ECN innovation has been so complete that the NYSE and Nasdaq have, of course, purchased their largest ECN competitors and are transforming themselves into ECNs. The idea that there will be enormous innovation on the market data side if the Commission simply permits the NYSE and Nasdaq to extract monopoly rents from its captive rate-base strikes us as unlikely.

We would suspect instead that there would be a net diminution of innovation as the NYSE and Nasdaq attempt to leverage their monopolies over regulatory and sole-source data downstream into the value-added data market<sup>14</sup> or simply use their government-sponsored monopoly to cross-subsidize ventures in historically competitive markets. In short, we are convinced real innovation is likely to arise where market forces and competition are real. Innovation will not be maximized where a monopoly can extract fees unrelated to the cost of

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<sup>14</sup> See letters of NetCoalition dated August 9, 2006, Bloomberg L.P. dated July 14 and August 22, 2006 and SIA dated July 14, 2006 to the Commission re: File No. SR-NASD-2006-056; SEC Release No. 34-54003 (June 16, 2006) (the Nasdaq Analytics Data Package) and File No. SR-NASD-2006-072; SEC Release No. 34-54002 (June 16, 2006) (the Trading and Compliance Data Package).

providing the monopoly service. The Commission might best spur innovation and the exploitation of market forces by exploring the separation of monopoly functions from competitive functions. In fact, this is exactly what the Commission wisely did in its decision in the matter of Nasdaq's FSI exemption.<sup>15</sup> We trust competition to be a greater source of innovation and excellence than monopolist enterprises.

The proposals made to Internet companies by the now for-profit exchanges have been exorbitant. They have ranged from \$75 per unique visitor per month for Nasdaq data to \$15 to \$30, or \$10 or \$9 per unique visitor, per month for NYSEArca data to the \$1 per unique visitor per month for the NYSE non-professional rate. At \$75 per month for the roughly 49 million Americans visiting financial web sites, fees would theoretically run more than \$3.6 billion per month, or \$44.1 billion annually. (These numbers are, of course, in addition to the hundreds of millions of dollars already collected annually from the broker-dealer community). If all Internet users of financial pages sought NYSEArca data at the \$9 rate, that would still run \$441 million a month, \$5.3 billion annually. Even the "bargain basement price" of \$1 per month for NYSE non-professional data would still render the not-so-Spartan sum of \$49 million per month, or \$588 million per year. Any and all sums would be, of course, in addition to the actual transaction charges that would be levied on retail investors if they opt to engage in a transaction.

Relatively few of our members' customers are going to purchase market data at \$75 per month. It is unclear how many would buy NYSEArca data at \$9 per month, but clearly even at \$1 per month — where one might expect more user participation — the Commission

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<sup>15</sup> Securities Exchange Act Release No. 42713 (April 24, 2000) (2000 SEC LEXIS 807).

staff is authorizing a transfer from retail investors to a for-profit monopoly of hundreds of millions of dollars annually, with literally zero showing of any cost basis.

By not submitting any information to provide a factual justification for its proposed fees, NYSEArca prevents the Commission from considering, for example, whether charging Internet companies for access to real-time market data based on the number of users — or “eyeballs” — that visit the site can be justified against the mandate that fees be “fair and reasonable.” Given the fact that the ECNs were providing real-time market data to Internet companies at no cost, it seems reasonable that a “flat rate” for access to market data is more appropriate than a “per user” structure that puts the availability of real-time market data out of reach for the vast majority of Internet users.

Effectively, the Market Regulation staff is ruling that an advertiser-supported medium like the Internet cannot provide this most critical of all financial data. As indicated in the attachments to our November 6, 2006 notice to the Commission,<sup>16</sup> the NYSEArca fees make it financially untenable for Internet companies to provide real-time market data to their users, as this feature has been removed from major Internet web site financial pages.

The real uniqueness of the Internet, both the cornerstone of its remarkable success and the promise for an even more remarkable future, is its ability to provide access to information in a way impossible anywhere offline. Consumers can find and compare literally millions of different facts — from airline fares to restaurants, from sports scores to a seemingly infinite number of goods and services — all in a matter of seconds.

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<sup>16</sup> Notice from Markham C. Erickson, Executive Director and General Counsel, NetCoalition to The Honorable Christopher Cox, Chairman, U.S. Securities and Exchange Commission, Nov. 6, 2006.

The vast majority of this available information can be provided to consumers because the cost is underwritten, at least in substantial part, by advertising revenues. In some cases, Internet companies pay database producers a fee for access to certain information, but even in these cases, the fees are offset to some degree by advertisements.

Allowing the exchanges to charge our members in amounts that make it impractical for them to provide real-time market data—without a rigorous examination to determine whether the proposed fees are tethered to the costs of consolidating the data—has meant that the Internet’s revolutionary, universally accessible information forum is not available for the vast majority of the investing public.

This seems to run counter to the thrust of the securities laws’ commitment to investor protection, as well as counter to the 1975 Amendments’ commitment to fostering a free and open market. Exchange Act Section 6(b)(5), 15 U.S.C. § 6(b)(5).

It also undermines and indeed subverts more recent initiatives of the Commission. Chairman Cox has invested substantial effort in promoting an XBRL initiative. The XBRL initiative is intended to assist retail investors by encouraging more user-friendly corporate filings that better exploit modern technology. This important effort will be for naught if the Commission staff simultaneously erects significant barriers between retail investors and the market data that is absolutely essential for their trading. Likewise, the imposition of substantial monopoly fees without benefit of any economic data undermines the Commission’s recently articulated commitment to bolster decisions with a more thorough economic analysis.

The uncertainty surrounding the status of market data — more specifically exchange efforts to exploit that uncertainty — have left our members’ users quite literally in the dark. In addition, some of our members have been informed that any and all fees will be

retroactive. Counsel to our members have advised that, rather than risk retroactive application of ruinous fees, the only course of action they would dare to take is ceasing to carry real-time market data. The result has been the widespread elimination of real-time market data from the Internet, thus depriving average investors of the basic information necessary to make informed investing decisions.

Without a rigorous review of how market data fees relate to the cost of consolidating the data, the Commission implicitly allows the NYSE and Nasdaq to proceed as if they “own” this factual data and can charge users whatever the market will bear for access to the this “property.” In fact, although NYSE and Nasdaq have tried mightily to create an ownership right in this factual data, NYSE and Nasdaq do not “own” this data — which is, of course, information that broker-dealers are legally required to provide to them at no cost.

Historically, the basic information policy of our country has held that facts — the building blocks of information — cannot be owned. That policy was underscored in the unanimous U.S. Supreme Court decision in *Feist v. Rural Telephone Service Company, Inc.*, 499 U.S. 340 (1991). From 1996 through 2004, however, the NYSE and Nasdaq were active participants in various coalitions that were committed to the enactment of far-reaching “database protection” legislation intended to create an unprecedented property right in facts and to overturn the policy embodied in *Feist*.

Congress repeatedly rejected this effort to create a property right in facts. The extraordinarily diverse group successfully urging the Congress to reject the NYSE- and Nasdaq-backed approach included NetCoalition, the Securities Industry Association, the U.S. Chamber of Commerce, the National Academy of Sciences, the American Conservative Union, the American Civil Liberties Union, Consumers Union and numerous other prominent organizations.

Indeed, congressional concerns regarding the specific issue of the free availability of market data via mass media prompted Senator John McCain, the then-Chairman of the Senate Committee on Commerce, Science, and Transportation, to introduce the “Trading Information Act,” a bill to “amend the Communications Act of 1934 to ensure that public availability of information concerning stocks traded on an established stock exchange continues to be freely and readily available to the public through all media of mass communication.”<sup>17</sup>

The concerns of NetCoalition during the database debate were straightforward. It was clear to us that an ownership right in facts would fundamentally change the nature of the Internet. By sanctioning monopolies in facts, the database proposals would have resulted in skyrocketing prices for the data itself and would have severely limited users’ access to information on the World Wide Web. Sanctioning the monopoly control of facts would also have allowed sole source providers to leverage their monopolies in the raw data market downstream into currently competitive markets for value-added products. This is a formula for higher prices, reduced transparency and less innovation in both the primary and downstream markets.

Apparently wanting both a “belt and suspenders,” the NYSE and Nasdaq backed this legislation while simultaneously claiming that they already owned the quotes. Indeed those who took issue with the exchanges’ property claims were derided by the NYSE’s General Counsel:

Those trying to shift the debate and focusing on this question are obfuscating the real issue: the apportionment of costs of generating market data among broker-

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<sup>17</sup> The Trading Information Act, S. 95, 106<sup>th</sup> Cong. (1999).

dealers and investors. Those focusing on ‘property rights’ conveniently ignore the fact that those who approve the Exchange’s budget and market data (and other) fees are the ones who pay.<sup>18</sup>

The NYSE was certainly correct in saying the real issue is the “apportionment of costs of generating market data among broker-dealers and investors.”<sup>19</sup> The relevant sections of the securities laws have not changed since that statement. Indeed, the fact that we now have for-profit exchanges should increase, not diminish, the scrutiny necessary to control conflicts of interest. The assertion that the public is protected because “those who approve the Exchange’s budget and market data (and other) fees are the ones who pay”<sup>20</sup> has certainly never been true for Internet companies and is not true now of the broker-dealer community. The only effective restraint on abusive monopoly behavior is the SEC’s enforcing the securities laws.

Having lost the database debate on Capitol Hill, the NYSE and Nasdaq are now at the Commission with a series of proposals that would abuse the exchange monopoly in market data facts by proposing extortionate fees. Other proposals — the Nasdaq Analytics Package and the Nasdaq Trading and Compliance Data Package — would leverage exchange monopolies over regulatory and other sole source data downstream in an effort to gain an anti-competitive

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<sup>18</sup> *Market Data: Implications to Investors and Market Transparency of Granting Ownership Rights over Stock Quotes: Hearing before the H. Subcomm. on Capital Market and Government Sponsored Enterprises of the H. Comm. on Financial Services, 107th Cong. (2001) (statement of Richard P. Bernard, Vice President and General Counsel, NYSE).*

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

advantage in the value-added data market.<sup>21</sup> Both efforts run afoul of not only the Exchange Act, but also the congressional rejection of a proposed new property right in facts.

These efforts also seem to be founded on the premise that fees for a monopoly product might be based upon the product's "value" rather than the cost-basis mandated by the Exchange Act. We find no basis in the Exchange Act for this "value" theory, and with good reason. It is clear that pricing a monopoly good on the basis of its "value" is tantamount to allowing the monopolist to charge whatever he or she wants. Such charges currently reduce market transparency — and would in the future continue to do so — while simultaneously diminishing innovation.

The transforming effect of modern technology could be harnessed much more effectively to promote the interests of markets and investors. For example, the broader distribution of critical market data on the Internet could generate significant trading revenues for for-profit exchanges. The broader distribution of critical market data on the Internet could generate significant new liquidity for our capital markets, and expand the universe of participants who amortize the costs of producing market data, thus reducing the fees of all market participants. The broad distribution of market data on a non-discriminatory basis would likely catalyze innovation with the entire market having an equal opportunity to develop value-added products, instead of allowing exchanges to leverage their existing monopolies downstream.

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<sup>21</sup> See letters of NetCoalition dated August 9, 2006, Bloomberg L.P. dated July 14 and August 22, 2006 and the Securities Industry Association dated July 14, 2006 to the Commission re: File No. SR-NASD-2006-056; SEC Release No. 34-54003 (June 16, 2006) (the Nasdaq Analytics Data Package) and File No. SR-NASD-2006-072; SEC Release No. 34-54002 (June 16, 2006) (the Trading and Compliance Data Package) for comments supportive of the Commission's rejection of regulatory data being used for commercial purposes and critical of SRO market-data fee proposals.

The Internet creates these and many other possibilities in market data. They are worth exploring in depth before a series of piecemeal decisions are made that lock-in a world that not only fails to exploit this technology, but it is actively hostile to it — to the disadvantage of investors and the capital markets.

### **Conclusion**

In light of the foregoing, Petitioner respectfully submits that the action of the Commission's staff in approving the instant rule proposal of NYSEArca is arbitrary, capricious, an abuse of discretion and otherwise not in accordance with law and that the staff's action embodies, *inter alia*, (a) a conclusion of law that is erroneous, and (b) an exercise of discretion or decision of law or policy that is important and that the Commission should review. Accordingly, the Commission should set aside the staff action and should institute proceedings to determine whether the NYSEArca proposed rule change should be disapproved. Such action would permit a stay until such time as the Commission is able to consider and articulate principles guiding consideration of this and other pending proposals.<sup>22</sup> Both the Commission and the exchanges should welcome this pervasive hunger for market data the Internet demonstrates.

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<sup>22</sup> The Commission may wish, in addition to granting our petition, to revisit its delegation rules, to require that the Division of Market Regulation not approve by delegated authority any self-regulatory organization's proposed rule change that has been the subject of substantial adverse public comment, or that it not do so without the express concurrence of the Commission's General Counsel.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Markham C. Erickson". The signature is fluid and cursive, with a long horizontal stroke at the end.

Markham C. Erickson  
Executive Director and General Counsel  
NetCoalition

November 14, 2006