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Jonathan G. Katz, Secretary  
United States Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549-0609

**Re: Regulation NMS, File No. S7-10-04**

Dear Mr. Katz:

Charles Schwab & Co., Inc. (“Schwab”)<sup>1</sup> appreciates this opportunity to comment on proposed Regulation NMS. Schwab’s focus on market structure reform continues to be enhancing transparency and equal access to the markets for all investors. Accordingly, our comments primarily focus on the market data elements of the proposing release. In Parts IV and V below, we also include our views regarding the proposed trade-through, market access, and sub-penny rules.

Broad access to meaningful securities pricing information is critical to achieving and maintaining fair and transparent markets. The more it costs investors to access securities pricing information, the less access there will be. The more information available to investors, the more transparent the markets will be in terms of enabling them to make informed trading decisions. But the stock and options exchanges are unique among industries, in that they charge consumers a fee for accessing the going price to buy the products for sale in their marketplace. The pricing information itself has become the revenue generating product. This is not a natural response to market forces. As Commissioner Goldschmid has stated: “[O]nce you conclude that . . . there has to be one central source of it, then you’re not talking about the market doing it.”<sup>2</sup> Rather, the exchanges’ protected status under SEC rules grant them exclusive franchise to deal in securities pricing data and require investors to consume that data as a condition to accessing the markets to trade securities. The SEC’s Quote Rule requires broker-dealers to report their bids and offers and their clients’ order information to the exchanges for free, while the SEC’s Display Rule requires broker-dealers and investors to buy back that information in a prescribed consolidated format.<sup>3</sup>

The exchanges (including Nasdaq) set prices and other terms of access through four cartels or “Network Plans.” They operate without any fear of antitrust protection for consumers because they are shielded under SEC rules. The result is not surprising: excessive fees leading to profits used to fund activities in areas where the exchanges do face competition. This includes rebates for order flow and trade prints, marketing for listings, and paying exorbitant executive compensation in some cases. The proposing release documents some of the untoward behaviors that have resulted.<sup>4</sup> Not mentioned in the proposing release is the fact that the former chairman of the New York Stock Exchange (NYSE) was awarded \$139.5 million last year, while NYSE took in \$148 million in market data revenue through its allocations from the Network Plans.

The Commission’s current market data proposal fails to deal directly with this problem. Simply put, there is too much unaccountable money washing through the system.<sup>5</sup> The proposing release indicates that last year three of the four Network Plans collected in the aggregate \$424 million in revenue while incurring only \$38 million in expenses.<sup>6</sup> That is a 1,000 percent markup in price. There is no objective justification in any past or present filing approved by the Commission that supports making investors pay these high fees, even as the quality and depth of market data reflected in the consolidated quotation has decreased post-decimalization (see Part III below). Today we have a lower quality “product” investors are required to buy at unjustifiably high prices despite advancing scale in distribution technologies that has made the unit cost of market data negligible.<sup>7</sup>

There is a long history leading us to the point where the Commission staff in proposed Regulation NMS felt the need to suggest a complicated allocation formula to regulate where the excessive profits go and how they are used. As Robert Greifeld, the CEO of The Nasdaq Stock Market, testified with remarkable candor at the April 21, 2004 hearing:

So we have a monopoly price that was set almost twenty years ago without any active review . . . . And any time you’re dealing with a monopoly price, then the participants have the right to understand how that price derived.<sup>8</sup>

This was the point of Schwab’s June 1999 Petition for Rulemaking, in which we asked the Commission to review the unreasonable fee structure unrelated to costs that discriminates against retail investors accessing quotation information online.<sup>9</sup> The Commission then issued its 1999 Concept Release on the Regulation of Market Information Fees and Revenues, in which it expressed the concern that “the current arrangements for setting fees and distributing revenues may need to be revised.”<sup>10</sup> The reforms considered by the Commission in 1999 included:

- an “approach to evaluating the fairness and reasonableness of fees that, among other things, could establish a link between the cost of market information and the total amount of market information revenues”;
- “greater public disclosure concerning fees, revenues, and the SROs’ use of revenues”; and
- “broader industry and public participation in the process of setting and administering fees.”<sup>11</sup>

In 1999 the Commission was asking all of the right questions, and had already concluded that “[i]ts review thus far particularly has indicated the importance of adapting market information fees to the increasing retail investor demand for real-time information and the changing structure of the securities industry.”<sup>12</sup>

But when some of the exchanges, not surprisingly, filed negative comment letters about the loss of potential revenue, the Commission deferred action and formed the Advisory Committee on Market Information in 2000. After the Advisory Committee failed to answer the basic questions about the market data fee setting process despite its charter,<sup>13</sup> the Commission held Market Structure hearings in 2002 at which it raised the same questions again.<sup>14</sup> Following issuance of the present proposal, the Commission held another market structure hearing in April 2004 which resulted in more testimony about control of market data, its cost of production, and the unreasonableness of fees.<sup>15</sup> Meanwhile, the exchanges have continued to enjoy the spoils of market data revenues from investors simply seeking access to the markets through real-time electronic data.<sup>16</sup>

The Commission should resist the temptation to delay action on these issues, as it has before, in misplaced reliance on the well-worn and unfounded argument that “market data fees must be preserved to fund self-regulation.”<sup>17</sup> This argument has been exposed in recent years for what it is: a scare tactic to preserve certain exchanges’ profits that flow from market data revenues to pay rebates on trade prints and lavish executive compensation. No one who argues for fair and reasonable market data fees is in favor of reduced regulatory funding. Rather, regulation should be paid for directly in the manner contemplated by the Exchange Act: SROs should explain what is necessary to pay for self-regulation and fund it through a fair and transparent allocation method to collect regulatory fees from members.<sup>18</sup> Market data has a critical purpose distinct from self-regulation under the Exchange Act, and the Commission should address it as a market structure issue and not as a self-regulatory funding issue.

Instead of tinkering with the status quo or deferring action, the Commission should move immediately to propose and then adopt a “Regulation Market Data Fair Access” that would be based on the following principles to promote access and transparency for all investors:

- Fees for consolidated market data must be set based on the cost of consolidation.
- Market data costs and fees should be publicly and independently accounted for through a process that facilitates public participation, and the burdens on firms and investors in administering market data should be minimized.
- Consolidated market data must be of a quality and depth that does not place individual investors at a disadvantage to market professionals when accessing the markets to buy and sell securities.

Below we provide our recommendations for reform and how best to implement these principles.<sup>19</sup>

**I. Fees for consolidated market data must be set based on the cost of consolidation.**

Market data reforms must promote the investor protection purpose of market data. In 1999 the Commission stated: “One of the most important functions that the Commission can perform for retail investors is to ensure that they have access to the information they need to protect and further their own interests.”<sup>20</sup> Market data’s purpose under the Exchange Act is not to create or assure profits for the exchanges to divide among themselves according to a complicated formula like the one in the proposing release. The purpose is not to “directly reward those market centers that generate the highest quality quotes,”<sup>21</sup> which is simply competition for trading business. Rather, market data’s purpose - as mandated by Congress - is to protect investors by creating transparency in the prices investors receive for buying and selling securities. This helps assure that they are treated fairly and receive best execution for their orders. If investors do not have equal access to market data that creates transparency for their orders, they are placed at a disadvantage when it comes to buying and selling against professionals, and they are not able to see whether they received best execution.

Congress enacted Section 11A of the Securities Exchange Act to further these purposes, stating that the requirements for market data distribution are: “to assure . . . the availability to brokers, dealers, *and investors* of information with respect to quotations for and transactions in securities”<sup>22</sup> through registered securities information processors that are prohibited from limiting access to their services<sup>23</sup> and that must provide market data on terms that are “fair and reasonable” and “not unreasonably discriminatory.”<sup>24</sup> Soon after Section 11A was enacted, the Commission recognized its oversight responsibilities to enforce the congressional mandate:

Because Congress was concerned that exclusive processors of securities information, as monopoly facilities, could frustrate the goals of an NMS, Congress made the Commission “a first line of defense against anti-competitive practices . . . [by granting] the SEC broad powers over any exclusive processor

and [imposing] on [the Commission] a responsibility to assure the processor's neutrality and the reasonableness of its charges in practice as well as in concept."<sup>25</sup>

In practice, the Commission has failed to adopt a clear benchmark to assess the reasonableness of the fees charged for the consolidated quotation or NBBO. It needs to do so, and there is a widely recognized standard that should apply: the cost of producing the consolidated data.<sup>26</sup> This is a standard that enjoys widespread historical and current industry support:

- In 1975 when it established the framework for the national market system, Congress viewed exclusive processors as similar to public utilities “whose rates traditionally have been set on cost bases,” and the Exchange Act’s language of “fair and reasonable” indicates cost-based fees appropriately apply.<sup>27</sup>
- In 1984 the Commission applied a cost-based standard to settle a dispute between Instinet and the NASD in determining appropriate fees that the NASD could charge Instinet’s professional subscribers for accessing NQDS (Nasdaq “level two”) data through Instinet’s terminals. The Commission rejected the NASD’s value-of-service approach to setting the fees in favor of a cost-based approach. Although a primary reason for requiring the cost-based approach was to assure fair access to a vendor that was in competition with the NASD, the Commission also emphasized that the cost-based method was necessary “to ensure the neutrality and reasonableness of the NASD’s charges to Instinet *and its subscribers*,” and to do otherwise would require “*Instinet subscribers* to subsidize other NASDAQ services.”<sup>28</sup> Today, through the Internet and other electronic means, subscribers include individual investors as well as professionals, and the same logic applies: they are entitled to neutral and reasonable charges based on cost without having to subsidize other SRO activities.
- In its 1999 Concept Release, the Commission recognized that “[o]ne standard commonly used to evaluate the fairness and reasonableness of fees, particularly those of a monopolistic provider of a service, is the amount of costs incurred to provide the service.”<sup>29</sup> The Commission stated its belief that “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. . . . The Commission therefore believes that the total amount of market information revenues should remain reasonably related to the cost of market information.”<sup>30</sup>

- In 2002, Chairman Pitt questioned at a public hearing why market data was not provided for free like corporate data, or at least based on the cost of production.<sup>31</sup>
- In April 2004, the head of one of the exclusive processors, Robert Greifeld of Nasdaq, stated at the Commission's hearing on Regulation NMS that "[i]f this market data is a part of the public good, then a government mandated utility is a natural consequence." Further, "you've got certain data that's required by all investors, that's part of the public good, then the natural corollary is that the government should set the rate for that data."<sup>32</sup>
- Today the Securities Industry Association, representing hundreds of exchange members that serve both retail and institutional clients, is calling for a cost-based approach to market data fees in its comment letter to the Regulation NMS proposing release.

In the absence of a cost-based standard to assess the fairness, reasonableness, and neutrality of market data fees, Robert Greifeld of Nasdaq has testified that "data is not provided at a low enough cost and it does create . . . unintended results and distortions in our market. The [exchanges] today are the beneficiaries of that excessive rent."<sup>33</sup> This is proven by the numbers. According to the Commission's figures, in 1994 the excessive rent baseline (revenues minus consolidation processing expenses) was \$246.1 million, and by 1998 it had skyrocketed to \$410.6 million.<sup>34</sup> In 2003, the excessive rent baseline remains at an estimated \$425 million.<sup>35</sup> In contrast, the Network Plan costs in the aggregate have remained relatively flat at about \$40 million a year.<sup>36</sup> This represents a 1,000 percent markup in fees over processing costs.

Some of the exchanges have tried to justify the markup by arguing that there are additional costs at the exchange level for distribution of consolidated data, yet they have never come forward with evidence of those costs. The Commission also does not know what those costs are, if any.<sup>37</sup> During a colloquy at the recent hearing on Regulation NMS, Robert Britz of the New York Stock Exchange claimed that it cost NYSE "\$488 million last year to produce market data" beyond the cost to SIAC its exclusive processor and Network Plan A, and referenced the NYSE annual report to "bring a little clarity to that number."<sup>38</sup> Robert Greifeld of Nasdaq countered:

[I]t is inconceivable to me as someone who is now responsible for the SIP in the Nasdaq world, who has the technology background, to figure out any way to spend anywhere near the \$488 million, and certainly we would welcome the opportunity to take a contract from New York Stock Exchange to maybe run it a little more efficiently.<sup>39</sup>

A review of the NYSE 2003 annual report fails to uncover the source of the \$488 million in expense relating to consolidating market data; that would be about half of the NYSE's overall annual expenses.<sup>40</sup>

The excessive fees unlinked to exchange costs resulting in unjustifiably high profits are clearly documented in the Commission's record, yet it has failed to adopt a cost-based standard (or apply any apparent standard) in part for fear of having to engage in "rate making."<sup>41</sup> But public interest regulation over rates charged for consolidated market data is the Commission's delegated obligation under Section 11A of the Exchange Act and it should not avoid this responsibility simply because it is difficult. The Commission, moreover, is not without tools to oversee a cost-based approach to consolidated market data fees. There is its own precedent of the 1984 Instinet case to follow, the allocated cost approach described in the 1999 Concept Release, and it could require the exchanges, by rule, to submit through the Network Plans a cost basis subject to independent audit and review, which the Commission could publish for public comment. Administrative reforms would assist the Commission considerably in this process, as described below in Part II.

**II. Market data costs and fees should be publicly and independently accounted for through a process that facilitates public participation, and the burdens on firms and investors in administering market data should be minimized.**

Although the Congressional mandate for market transparency through access to market data is clear, the basis and process through which the Network Plans set market data fees and grant access to market data is opaque. Today the Commission oversees a process that does not reveal the costs of exchange market data consolidation and dissemination, does not include public representation in the Network Plans' governance, affords little opportunity to comment when material changes are made affecting the fee schedule (typically after they have already taken effect, if at all), and does not consider the extensive burdens placed on investors and broker-dealers as the hidden extra price to see real-time stock quotes. The net result of unreasonably high fees coupled with unreasonable administrative burdens is that firms are forced to ration their employees' and clients' access to consolidated real-time data. This must change so that consolidated data is administered for the protection of investors and not for the proprietary benefit of the exchanges.

Accounting of Costs and Fees. As discussed above, the Commission does not know how much the exchanges spend on the process of consolidating and distributing market data and the exchanges have not reported any costs for that function outside of the Network Plans. Without audited data from the exchanges it is not possible to assess properly the reasonableness of fees. This failure on the exchanges' part ought to create a presumption against them that, unless rebutted, means the cost of production is simply the Network Plans' expenses. The only conclusion would be that the consolidated data

fees - currently marked-up by 1,000 percent over Network Plans' expenses - are not reasonably related to the cost of production.

**Reforms:**

- Amend the Network Plans to require each to file independently audited financial statements annually for Commission and public review that covers details about expenses, revenues, and projections. This is what the Commission itself proposed five years ago in the Market Data Concept Release.
- Adopt a rule under Section 11A that requires, as a condition for receiving an allocation of market data fees, each Network Plan participant to file an independently audited report annually that details the revenues received from market data, how those revenues are spent, and the costs the participant incurs for market data consolidation that are separate and apart from the Network Plans' costs.
- Amend the Network Plans to require cost, revenue, and volume projection data, and competitive impact analysis to support any proposed fee or user classification change that would have an effect on the fees assessed against one or more categories of market participants.

Meaningful Public Participation. The Commission by default has delegated rate-making to the exchanges operating through the Network Plans. Accordingly, Network Plan governance should be independent and open and follow the corporate governance principles the Commission requires of the exchanges. The conflict of interest in having the exchanges alone set their own fees for a monopoly product is apparent, more so when that product is a cornerstone of market transparency and investor protection. Currently, there is no requirement that the Network Plans' governance committees that set and oversee market data fees and administrative policies have any public or investor representation at all.

To address this problem, the proposing release suggests a new non-voting advisory committee consisting of members, selected by the exchanges, who would represent a retail broker-dealer, an institutional broker-dealer, an ATS, a data vendor, and an investor.<sup>42</sup> Schwab believes that such a committee would simply give the exchanges a fig leaf of credibility without introducing any meaningful reform. A non-voting advisory committee also would be inconsistent with the Commission's recent actions and statements regarding the need for independent mutual fund directors and public governors on the boards of SROs. When participating in the national market system for the consolidation and dissemination of data to make the markets transparent and fair, the exchanges should be viewed as acting in their quasi-governmental capacity for the public interest and the protection of investors and principles of independence and public representation in governance should prevail.<sup>43</sup>

**Reforms:**

- Amend the Network Plans to include voting members representing institutional investors, retail investors, broker-dealers, and vendors on the board and operating committees that review, set, and change market data fees and the conditions under which market data is distributed. Nominations for these slots could come from associations that represent the interests of these different constituencies.

Public participation also occurs through the notice and comment process. Unlike the Commission's own rulemaking process, there is little or no opportunity to comment meaningfully when the Network Plans change market data fees and distribution requirements. Such changes are now implemented through "effective upon filing" procedures,<sup>44</sup> "pilot programs" that are not filed at all, notices published on the Network Plan administrators' Web sites, and unilateral changes to and interpretations of market data contracts. The Commission's recent order in the Bloomberg matter is on point, and the principles applied to the distribution of non-consolidated market data in that case should apply with equal force to consolidated data.<sup>45</sup> The current process is wholly one-sided in favor of the exchanges and is ineffective in terms of public notice and the ability to raise challenges or issues to the Commission's attention. The Commission has noted these problems in the past,<sup>46</sup> and should now propose rule changes to address them.

**Reforms:**

- Amend Exchange Act Rules under Section 11A and Rule 19b-4, and corresponding provisions in the Network Plans, to eliminate the "effective upon filing" process for market data fee changes, including changes that would impact the treatment of market data users and market data distribution policies.
- Amend the Network Plans to eliminate "pilot" programs that affect market data fees or could result in different treatment of market data users, unless the details of the pilot are first filed for public notice and comment.
- Amend the Network Plans to adopt the definition of "rule" under Exchange Act Rule 19b-4 and require them to file their material policy changes as rules for public notice and comment prior to adoption.

Minimizing Administrative Burdens. "The Commission believes that assuring retail investors ready access to consolidated prices is a vital benefit of the current model of market consolidation."<sup>47</sup> Today, access is anything but "ready." The NMS proposing release does not address the extensive public record documenting the unjustifiable burdens placed on vendors, broker-dealers, and investors in complying with the Network Plans' arcane contracting, classification, and reporting requirements as a condition to accessing consolidated market data.<sup>48</sup> Those requirements impede access to market information and are a natural result of unchecked cartel behavior where there is no

consequence or regulatory redress from over-burdening the users of the service. The most egregious burdens are:

- The Network Plans use multiple user definitions and interpretations, fee categories and classifications that result in complex, unique and inconsistent monthly reporting requirements of data usage to each Network Plan. Charges are pegged to these reports and the method by which an investor accesses data (through a registered representative, through an automated phone system, or over the Web). This fee method based on type of user and mode of access discriminates by charging duplicative fees against investors using firms that offer multiple channel access or simultaneous access to consolidated market data.
- The Network Plans require vendors and broker-dealers to seek prior approval of any new systems or services that incorporate market data. This is anti-competitive, delays innovation, and requires firms to divulge proprietary information.
- The Network Plans use non-uniform and non-negotiable vendor contracts whose provisions place limitations on access to market data and impose burdensome requirements that have the effect of rules that have not been approved by the Commission with the benefit of public notice and comment. Similarly, policy changes are issued by decree on the Network Plan administrators' Web sites. Some of these policy changes are rules that should be subject to SEC approval after notice and opportunity to comment.<sup>49</sup> For example, higher fees are generated through inconsistent and expansive interpretations of the “professional” definition under which investors (the Network Plans call them “subscribers”) pay higher fees for the same market data. The Network Plans have applied the professional definition to anyone who accesses market data through an account that is in a non-natural person’s name or for a use that is not strictly “personal,” regardless of whether that person is linked in any way to the securities industry. This discriminates against small business owners who are required to pay the same rate as institutional investors and broker-dealers.<sup>50</sup> The distinction is critical. A case in point is Network B for Amex-listed securities, which has no per quote fee schedule for professionals. Thus, if an investor meets the definition of professional, he or she must pay a flat “device” rate of \$27.25 per month, even if that investor only accesses a single quote online that month to make one trade.
- Non-uniform, confusing, and lengthy online "subscriber" agreements that broker-dealer clients are required to sign before being able to access a quote to make an investment decision.
- Disparity from Network Plan to Network Plan in the quote counting and reporting requirements (form, time period, type of data), requiring multiple and redundant administrative work hours and systems. Disparities in the types of internal and

external devices subject to market data fee liability require unique internal systems and processes to capture quote data usage.

- Time consuming and invasive annual audit process by each Network Plan to review each of the arcane elements noted above. The audits' purpose is to find technical non-compliance to generate additional fees. Audits often require divulging confidential data about a brokerage firm's customers, raising privacy and competitive concerns.<sup>51</sup>

In a footnote, the NMS proposing release states the hope that “the Plans continue their cooperative efforts with the industry to streamline administration.”<sup>52</sup> This statement is not based on facts. The administrative burdens are greater than ever, and there is no incentive for the exchange cartels to reduce them. This will require action by the Commission.

**Reforms:**

- To protect the interest of market participants and investors, the Commission should require the Network Plans to publish for public comment a proposal for a single monthly or annual fee at the firm or enterprise level based on costs which would remove virtually all of the administrative burdens noted above.
- Require the Network Plans to propose for public comment and Commission review and approval clear definitions and applications of fee categories such as “professional” and “nonprofessional” and limitations on the redistribution of data under one uniform rule for all four Network Plans.
- Require the Network Plans to work together to propose and then issue one uniform vendor agreement and one plain-English short subscriber agreement for retail investors.
- Require the Network Plans to estimate, under Paperwork Reduction Act standards that the Commission itself is subject to, the number of person hours and costs its various “collections of information” impose on broker-dealers, vendors, and investors.

**III. Mandatory market data must be of a quality and depth that does not place individual investors at a disadvantage to market professionals when accessing the markets to buy and sell securities.**

In the Regulation NMS Proposing release section on market access, the Commission states:

- “In a system with so many competing market centers and pools of liquidity, market participants . . . need to know what the best prices are and in which market they are available . . . .”<sup>53</sup>
- “The price at which an order can be executed is of paramount importance for most investors . . . .”<sup>54</sup>

- “[There is] general agreement that the Commission should further the interests of investors by promoting a market structure that encourages the robust interaction of buying and selling interest.”<sup>55</sup>

The Commission also states in the market data section: “[Depth of order book] has become increasingly important as decimal trading has spread displayed depth across a greater number of price points”<sup>56</sup>; and “[r]etail investors should not be required to become experts on market structure to participate directly in the equity markets with confidence that they will receive a fair deal.”<sup>57</sup>

Schwab could not agree more with the Commission’s views. But the Commission’s rules today maintain an unfair playing field for retail investors, because the content of the consolidated quotation is grossly inferior to the deeper data that market professionals rely on. There is no “fair deal”: retail investors cannot see what the best prices are for orders above a minimal size, cannot monitor their own order execution quality, and do not have the information to contribute to robust (meaning well-informed) interaction of buying and selling interest. This has increased retail investors’ dependency on broker-dealers and has increased their disadvantage compared to professional traders who have ready access to depth of book information.

Before decimalization, a retail investor typically would see, in the consolidated quotation, bid and offer interest up to 1,000 shares. After decimalization, a retail investor often can see a bid or offer size of only 100 or 200 shares. Ironically decimalization, a reform that was well intentioned to reduce the spread between bid and offer prices thereby reducing costs to individual investors, has also resulted in making the markets less transparent to them. This works to the advantage of the professional who may be trading against the retail investor.

For example, a retail client who wants to sell 2000 shares in some cases may only see 100 or 200 share size in a static consolidated quote at the best bid and offer. The retail investor has no idea what he or she will receive for the remaining shares, whether buying interest is strong or weak, or whether it makes the most sense to place a market order or a limit order as an opportunity to try for a better price. Meanwhile, a professional, using a Nasdaq TotalView service or NYSE LiquidityQuote service, can see streaming bid and offer prices to a depth of thousands of shares and can ascertain if there is an imbalance in buying and selling interest and which way the market is likely to move. This places a self-directed online retail investor at a huge disadvantage.

Because the consolidated quotation in many cases does not include buying and selling interest away from the minimum bid and offer size, a retail investor would have to pay the significant additional fees to subscribe to the exchanges’ premium quote services to get that depth of book information.<sup>58</sup> Professionals, who consult that data constantly all day long, can afford that extra expense. Retail investors cannot.

Schwab is in favor of allowing competition outside of the Network Plan cartel structure for deeper, more innovative market data products. However, SRO fees for those products should continue to be subject to SRO rulemaking procedures. (The Bloomberg matter is a case in point why this is still necessary.) In the interest of investor protection and to further the Commission's own national market system goals noted above, the Commission should also amend the Display Rule to include up to five ticks on each side of the market in the consolidated quotation to have some assurance that displayed quote size in the NBBO will be representative of a typical range of retail orders.<sup>59</sup> This is the only way to level the playing field between retail investors and professionals. Retail investors should benefit from decimalization and not be penalized by it.

**IV. In the interest of competition, the Commission should abolish the trade-through rule, or as a first step implement a pilot for certain ITS securities.**

Advances in technology have radically changed the way investors' orders are routed and executed. Entrepreneurial broker-dealers, new exchanges and unregistered entities have leveraged these new technologies to compete with the old-line exchanges and market maker community. Spreads are narrower, execution costs are lower, and customers have access to execution speeds that were unthinkable a few years ago. On balance, we see these developments as extremely positive and urge the Commission to act to remove the remaining impediments that restrict the efficiency of the national market system.

The most significant impediment to competition is the trade-through rule that currently applies to securities subject to the rules of the Intermarket Trading System ("ITS"), *i.e.*, securities listed on the NYSE and the Amex. Alarming, the Commission has proposed expanding the trade-through rule to all national market system securities, including those traded on the Nasdaq Stock Market. This is the market structure issue that has generated the most controversy among market participants.<sup>60</sup> In Schwab's view, competition has long been stifled in NYSE and Amex-listed securities by the trade-through rule, while trading of Nasdaq-listed securities has become more and more competitive in large part because of the absence of a trade-through rule. Before considering any final adoption of a uniform trade-through rule for NYSE-, Amex-, and Nasdaq-listed securities, the Commission should first implement a pilot to allow a subset of NYSE and Amex securities to be traded without being subject to the ITS trade-through rule, analyze the results, and only then determine whether to impose or eliminate market-wide restrictions on execution alternatives.

Summary of proposed rule. The proposed trade-through rule would require any order execution facility, national securities exchange, and national securities association to establish, maintain, and enforce policies and procedures reasonably designed to prevent the execution of a trade-through, which is the execution of any incoming order for a security at a price that is inferior to the best price displayed in another market. The

rule would apply to all National Market System (“NMS”) securities, which are defined to be securities listed on the NYSE, Amex and Nasdaq Stock Market.

The proposal has two major exceptions. The first would allow an automated market -- a market that provides immediate responses to an incoming order up to the full size of the best displayed bid or offer without restriction -- to trade-through a non-automated market up to a certain amount, but would not allow a manual market to trade-through an automated market. Following the hearing on Regulation NMS, the Commission requested comment in the Supplemental Release on whether the automated/manual exception should apply to quotes rather than applying to markets as a whole. Market centers could become hybrid markets by disseminating both manual and auto-execution eligible quotes depending on the circumstances. The hybrid market would attach an identifier to its manual quote disseminated into the national quotation stream. Automated market centers would then be free to trade-through the manual quote as long as it remained manual.

The second major exception is the opt-out provision. A customer, or a broker-dealer acting for its own account, would be able to choose on an order-by-order basis to have its order executed in one market, without regard to the prices in another market. Customers or broker-dealers could choose to opt-out of the best price protection of the trade-through rule by bypassing quotes in other markets, even if the other quotes were superior in price.

Threshold question: Is there a need for a trade-through rule? At the NMS Hearing, the threshold question was: “Is there really a need for a trade-through rule?”<sup>61</sup> Schwab believes that the simple answer is “no.” Support for our position is found in the diverging competitive landscape for NYSE-listed and Nasdaq-listed securities. Competition is flourishing in one and stagnating in the other.

Trading in NYSE-listed securities has been subject to the ITS trade-through rule for over 20 years. While purporting to protect investors from inferior prices, the ITS trade-through rule has actually insulated the NYSE and its specialist system from the dynamism brought on by competition. While other exchanges and Nasdaq have offered programs to trade NYSE-listed securities for many years, the ITS trade-through rule prevents any market from challenging NYSE’s market share. Competing markets cannot offer independent and superior price discovery because should they rightly trade at a price outside the NYSE quote, *i.e.*, beat the NYSE to the true price of a security, the competing market violates the ITS trade-through rule. The net effect of the trade-through rule is the erosion of the quality and timeliness of NYSE security executions as compared to Nasdaq security executions.

Nasdaq, in contrast to the NYSE, has been at the epicenter of seismic competition since the adoption of the order handling rules and Regulation ATS in the mid-1990s. Dynamic new market players have led a technology revolution driving spreads and

trading costs lower while improving execution quality. This competition has caused the old Nasdaq players, the market makers, to alter dramatically the way they do business by enhancing their automation and improving customer service. The superior execution quality of the Nasdaq market has come without a trade-through rule.

The NYSE, the principle champion of the trade-through rule, argues that investors' orders, particularly limit orders, are protected by the trade-through rule. John Thain, CEO of the NYSE, stated at the NMS Hearings: "investors who provide liquidity to the market by entering limit orders are protected from their orders being ignored."<sup>62</sup> The protection Mr. Thain refers to is presumably the fact that before an order in ITS eligible securities may trade at an inferior price, it must trade at the displayed price.

There is no claim, however, that the displayed investor limit order, the order that set the best price, will be executed when other markets trade "at" the same price. Under both the ITS trade-through rule and the Commission's proposed trade-through rule displayed limit orders are not protected when trades occur at the same price as the displayed price. Markets are free to execute at the then current national best bid and offer ("NBBO") without regard to an order previously displayed on another market. In other words, an investor may step up to create the NBBO, but not be guaranteed an execution when the security trades at that price. If the NYSE truly wanted to protect investor orders providing liquidity, orders they claim to be protecting, they should be demanding that the markets institute cross-market price and time priority.<sup>63</sup>

This very issue was raised to the Commission at the NMS Hearings. Ed Nicoll, CEO of Instinet, stated that: "And it seems to me that the notion that some put forth in which they conflate the duty of best execution with the trade-through rule, that somehow, supporting the trade-through rule is about protecting people's limit orders, is disingenuous unless they take the view, which very few people do, that those limit orders have to be respected both from a time-priority basis and a price-priority basis."<sup>64</sup>

A trade-through rule does not provide time and price priority. That would require the creation of a central limit order book ("CLOB") so that orders can be executed across all markets on a first come, first serve basis at any price point. If an order sets the best price, in a CLOB that order receives the next contra side order at that price. But very few market participants - including NYSE - support the institution of a CLOB. A CLOB would be a disincentive to innovate to improve service and handling of investor orders. Moreover, a CLOB would create a system with a single point of failure that could harm the efficiency and effectiveness of the national market system.

The problem with a trade-through rule is that it fails on three counts: it fails to provide the limit order protection of a CLOB, it suspends the price discovery process thereby harming the efficiency of the overall market, and acts as an impediment to investor choice in seeking execution efficiency. The Commission recognized these defects in its proposal by off-setting them with numerous carve-outs including an

automatic/manual opt-out, intermarket sweep, and basket trading exceptions. Clearly the trade-through rule fails to meet the complex needs of market participants.

Market forces and best execution requirements already protect investors, and short of trade-through rule elimination the Commission should institute a pilot to gather data. The Commission should allow market forces to determine which system best executes orders and in so doing provides protection to limit orders. We believe that when securities are traded in an automated environment without a trade-through rule, as they are in Nasdaq today, investors obtain greater order protection, faster executions and better prices. These are the positive results from fierce competition among market makers and ECNs competing for order flow. Investors are protected, not by a trade-through rule, but by the overriding legal obligation to provide best execution to investor orders. As stated during the NMS Hearings: “I would point out in fact, Nasdaq market makers have a best-execution requirement. And I believe if you ask most of them, they think that means that they have to honor the NBBO. . . I think that in effect, there is a quasi trade-through rule being honored in the Nasdaq marketplace.”<sup>65</sup>

Schwab recommends that the Commission observe the rule of “First, do no harm.” Do not impose a rule where the overriding principal of investor protection is already at work in a competitive market. The unnecessary systems costs and the ongoing regulatory costs to manage the risk of inadvertent violations of the rule argue against imposing a new rule that is already a part of the regulatory fabric.

Instead of applying a new rule to the Nasdaq market, trade-through reform should be focused on the ITS Plan and the operation of the trade-through rule on securities listed on the NYSE and Amex. In a manner similar to that adopted by the Commission in revisiting the Commission’s short sale rule, Regulation SHO,<sup>66</sup> the Commission should first implement a pilot program in NYSE and Amex securities that allows for trading without the application of a trade-through rule.

The Commission could also adopt a pilot program similar to Regulation SHO that imposes the proposed automatic/manual market<sup>67</sup> and the opt-out exceptions on the ITS Plan for a subset of ITS eligible securities. Indeed, the Commission could run two pilots at the same time: one without the trade-through rule for some ITS securities, and another that applies the proposed trade-through rule exceptions to a second group of ITS securities. During this pilot, the Commission should require specific disclosure of trade-throughs executed by broker-dealers as part of the Rule 11Ac1-5 disclosures already in place. Disclosure data of this type will inform both investors and the Commission of broker-dealer execution practices, particularly as they relate to limit order protection and best execution.

If the Commission does not believe that it can repeal the trade-through rule at this time, we believe the recommended pilot will provide the data necessary for broader Commission action in the near future.

**V. Access fees should be limited, and sub-pennies banned.**

Regulation NMS also contains proposed rules governing access among market centers and quoting and trading in sub-penny denominations. Schwab commends the Commission for supporting market forces in seeking solutions by permitting indirect linkages among market centers rather than imposing ITS-like hard linkages. Schwab supports independent third party linkages among order execution facilities and believes such linkages have a much better chance of remaining efficient and effective because they are subject to competitive forces.

The more important issue for Schwab, however, is not “how you access” a particular quote but what are the rules of engagement that apply when routed orders interact with quotes displayed in the national market system. These rules of engagement, whether in the form of fees for access or manual execution practices, cause many of the market dysfunctions we see today. The proliferation of locked and crossed markets is a direct result of quote gaming to earn fees that are paid by market makers seeking liquidity to meet their best execution obligations. Regardless of whether the Commission adopts our proposal to implement a pilot program for the trade-through rule or whether it implements trade-through reform as proposed, the Commission must act to eliminate these practices that are harming our markets today.

Because of these concerns, Schwab supports the Commission’s limitation on access fees charged by quoting market participants. We believe that standardizing these fees will restore validity to the quoted market while leveling the playing field for order execution venues.

With respect to sub-penny penny quotations and trades, we join the nearly unanimous call for the ban on quoting and trading in sub-pennies. We urge the Commission to implement this portion of Regulation NMS as quickly as possible.

**CONCLUSION**

Schwab recognizes the challenge of the Commission’s approach of addressing the key market structure issues in one set of proposals. The Commission has a historic opportunity to move forward while addressing the significant comments and testimony it has gathered as part of this rulemaking process. Abolishing the trade-through rule or at least implementing a pilot for certain ITS securities will enable competition to flourish for the benefit of investors in NYSE and Amex stocks the way it has for investors in Nasdaq stocks. The Regulation NMS proposal, however, fails to tackle the fundamental market structure issue relating to market data: the unjustifiably high cost of market data to generate fees that subsidize other aspects of the exchanges’ business. Directly confronting the issue of market data fees will solve the resulting problems apparent in the

record compiled by the Commission over the last five years. A complicated revenue allocation formula will not.

The high cost of market data and the Network Plans' Byzantine approach to market data administration burdens investor access to the markets. Without readily available, reasonably priced, and meaningful market data, investors are placed at a substantial disadvantage compared to professional traders and are unable to make informed trading decisions and monitor the quality of their executions. A "Regulation Market Data Fair Access" would require fees be set based on the cost of consolidation as established through an independent accounting, public participation in the governance of the Network Plans and the rulemaking process, a simple fee structure under one uniform contract and set of rules that minimizes administrative burdens, and inclusion of additional information in the consolidated quote stream so that investors are not disadvantaged by the advent of decimalization in terms of the data they see.

Schwab will continue to advocate for these reforms in the interest of our clients, and we would welcome the chance to discuss our views with the Commission and staff.

Respectfully submitted,

(signed)

Carrie E. Dwyer

cc: Chairman William H. Donaldson  
Commissioner Paul S. Atkins  
Commissioner Roel C. Campos  
Commissioner Cynthia A. Glassman  
Commissioner Harvey J. Goldschmid  
Annette L. Nazareth  
Robert L.D. Colby  
David Shillman  
Dan Gray  
Sapna Patel

## Endnotes

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<sup>1</sup> Charles Schwab & Co., Inc. is a wholly owned subsidiary of The Charles Schwab Corporation. Schwab serves approximately 8 million accounts and is one of the nation's largest financial services firms.

<sup>2</sup> Hearing before the Securities & Exchange Commission, Proposed Regulation NMS ("NMS Hearing"), File No. S7-10-04 (April 21, 2004), at 240. A full transcript of the NMS hearing is available on the Commission's web site at <http://www.sec.gov/spotlight/regnms/nmstrans042104.txt>

<sup>3</sup> See Exchange Act Rules 11Ac1-1(c)(1) and 11Ac1-2(e).

<sup>4</sup> *Regulation NMS*, Release No. 34-49325, 69 Fed. Reg. 11126, 11180 (March 9, 2004) ("NMS Release").

<sup>5</sup> See testimony of Robert Greifeld, CEO of Nasdaq, NMS Hearing Tr. at 244.

<sup>6</sup> NMS Release at 11179 (combined revenues and expenses of Network A (NYSE listed securities), Network B (Amex listed securities), and Network C (Nasdaq securities)). Excluded from the release is data from the fourth Network Plan, the Options Price Reporting Authority ("OPRA").

<sup>7</sup> "[T]he Commission remains concerned that retail investor fees have not properly kept pace with changing technology and increased demand." *Regulation of Market Information Fees and Revenues*, Release No. 34-42208, 64 Fed. Reg. 70613, 70614 (Dec. 12, 1999) ("Market Data Concept Release"). "[I]t is important to recognize that the basic information stream (all of the transaction reports and quotations in a Network's securities) will be the same, and have the same production costs no matter how many vendors and subscribers receive the information." *Id.* at 70630.

<sup>8</sup> NMS Hearing Tr. at 253.

<sup>9</sup> Petition for Rulemaking under Section 11A, Letter from Sam Scott Miller on behalf of Charles Schwab & Co., Inc. (June 29, 1999).

<sup>10</sup> Market Data Concept Release at 70615.

<sup>11</sup> *Id.*

<sup>12</sup> *Id.* at 70630.

<sup>13</sup> Under its charter, the advisory committee was charged among other things with evaluating "how market information fees should be determined, including the role of public disclosure of market information costs, fees [and] revenues." *Charter of the Securities & Exchange Commission Advisory Committee on Market Information*, October 10, 2000 (<http://www.sec.gov/divisions/marketreg/marketinfo/a.htm>). Although the advisory committee's final report acknowledges that it was supposed to consider "how the fairness and reasonableness of fees should be evaluated," it failed to make any recommendations. See Report of the Advisory Committee on Market Information: A Blueprint for Responsible Change, at section VII.D.3 (Sept. 13, 2001), available at: <http://www.sec.gov/divisions/marketreg/marketinfo/finalreport.htm>. This was because the committee process did not address the key questions head-on or engage in any real fact-finding about costs of market data production. See, e.g., Charles Schwab & Co., Inc. memorandum, "Unanswered Questions on Market Data Pricing," attached as Appendix L to the Report of the Advisory Committee on Market Information, <http://www.sec.gov/divisions/marketreg/marketinfo/appendixl.pdf>.

<sup>14</sup> “Specific Topics for Discussion at the Commission’s Market Structure Hearings” (Oct. 24, 2002) (“Who should pay for real-time market data? Who should get paid for real-time market data?”); <http://www.sec.gov/news/extra/mktstr-topix.htm>.

<sup>15</sup> See NMS Hearing Tr. at 223, 226, 228, 230, 237 (testimony of representatives from Nasdaq, National Stock Exchange, Schwab, Ameritrade, and Reuters, respectively), plus extensive question and answer session beginning on page 239 about cost of production and reasonableness of fees.

<sup>16</sup> Some exchanges continue to argue that they “own” market data and therefore should be able to charge what they can for it and impose conditions on its distribution as they see fit. Quotation and last sale information, however, are simply facts about current prices in the stock and options markets and therefore cannot be copyrighted or otherwise “owned.” The exchanges no more “own” quotations and last sale prices than do the broker-dealers and investors who create the data. Moreover, the Commission has already rejected the exchanges’ argument: “[T]he practical effect of comprehensive federal regulation of market information is that proprietary interests in this information are subordinated to the Exchange Act’s objectives for a national market system.” Market Data Concept Release at 70615.

<sup>17</sup> Nothing in Section 11A or its legislative history permits exclusive securities information processors to charge inflated rates for market data in order to pass through profits to the exchanges to fund other activities.

<sup>18</sup> As Robert Greifeld said at the Regulation NMS Hearing: “Regulation requires its own direct and completely attributable and secure source of funding.” NMS Hearing Tr. at 225. This will result in a stronger regulatory budget instead of it being hidden within the market data fee schedule.

<sup>19</sup> In doing so, Schwab has focused on the Commission’s supplemental request for comments “addressing the reasonableness of market data fees and whether the Commission should modify its approach to reviewing such fees,” and on “one of the Commission’s primary goals with respect to market data . . . to assure reasonable fees that promote the wide public availability of market information.” *Regulation NMS Extension of Comment Period and Supplemental Request for Comment*, Release No. 34-49749, 69 Fed. Reg. 30141, 30148 (May 26, 2004). Schwab is also responding to the Commission’s request “to consider and respond to the views reflected in the public record,” *id.*, including the Commission’s previous views and findings.

<sup>20</sup> Market Data Concept Release at 70614.

<sup>21</sup> Regulation NMS Release at 11176.

<sup>22</sup> Exchange Act Section 11A(a)(1)(C)(iii) (emphasis added).

<sup>23</sup> Exchange Act Section 11A(b)(1) & (b)(5)(A).

<sup>24</sup> Exchange Act Section 11A(c)(1)(C) & (D).

<sup>25</sup> *In re Instinet*, 49 Federal Register 17640 (April 24, 1984) (“Instinet Order”) at Lexis page 2 (quoting Senate Comm. On Banking, Housing & Urb. Affs., *Report to Accompany S. 249: Securities Acts Amendments of 1975*, S. Rep. No. 75, 94<sup>th</sup> Congr., 1<sup>st</sup> Sess. 12 (1975) (“Senate Report”), *aff’d NASD v. SEC*, 801 F.2d 1415 (D.C. Cir. 1986).

<sup>26</sup> The NMS proposing release is mistaken when it says “there does not appear to be any widely-accepted, objective, and workable standard.” NMS Release at 11178. The release states that the Seligman

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“Advisory Committee did not support the primary criterion . . . that an SRO’s data fees should be reasonably related to the SRO’s costs to generate and disseminate the data.” *Id.* It would not be accurate to ascribe to the industry as a whole the views presented in the Seligman Advisory Committee final report given the narrow scope of the committee’s work, the way meeting agendas were set, its lack of a disciplined process, and its over-representation by the exchanges. *See* Letter from Schwab, Reuters, Knight and Datek to Chairman Pitt and Commissioners Hunt and Unger re Report of the Advisory Committee on Market Information (Oct. 16, 2001) (dissenting from the approach taken in the final report of the Advisory Committee and asking the Commission and its staff not to “assume that the report reflects industry consensus or that all views have been heard”).

<sup>27</sup> Instinet Order at Lexis page 13 (citing Senate Report to the 1975 Securities Acts amendments, as well as the similar statutory standard under the Federal Communications Act and various federal court decisions and regulatory authority in the fee-setting context).

<sup>28</sup> Instinet Order at Lexis pages 6-7 (emphasis added). The United States Court of Appeals for the District of Columbia Circuit agreed with the Commission’s findings and approach to cost-based analysis. *See NASD v. SEC*, 801 F.2d 1415, 1419-22 (D.C. Cir. 1986).

<sup>29</sup> Market Data Concept Release at 70619 (citing rate making cases and authorities).

<sup>30</sup> *Id.* at 70627.

<sup>31</sup> *See* Mary Schroeder, *SEC Again Questions Market Data Fees*, Securities Industry News, November 18, 2002, at 4 (quoting Chairman Pitt).

<sup>32</sup> NMS Hearing Tr. at 223 and 253.

<sup>33</sup> *Id.* at 224.

<sup>34</sup> Market Data Concept Release at 70625 (market data revenues distributed to the exchanges in 1994 and 1998 from Tape A (NYSE), Tape B (Amex), Tape C (Nasdaq), and OPRA).

<sup>35</sup> This is the 2003 “preliminary and unaudited” figure for net income earned by Networks A, B, and C combined (see NMS Release at 11179), plus an estimated figure of \$39 million net income from OPRA. The NMS Release does not include data from OPRA for 2003, so the estimate of \$39 million is the OPRA net income available for distribution to the exchanges from 1998 (*see* Market Data Concept Release at 70637) and assumes that amount remained flat through 2003.

<sup>36</sup> *Compare* Market Data Concept Release at Tables 5-8 (1998 operating expense of approximately \$37 million including OPRA and assigning an average expense for Nasdaq) *with* NMS Release at 11179 (2003 operating expense of \$38 million not including OPRA).

<sup>37</sup> *See* Market Data Concept Release at 70625-26.

<sup>38</sup> NMS Hearing Tr. at 241.

<sup>39</sup> *Id.* at 244.

<sup>40</sup> New York Stock Exchange, 2003 Annual Report at 21-22. There is no line item for market data consolidation and distribution expense in NYSE’s annual report. NYSE expenses are broken down as follows: \$522 million for compensation; \$146 million for systems and related support; \$114 million for

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“professional services”; \$67 million for depreciation and amortization; \$65 million for occupancy; \$56 million for general and administrative expenses; \$14 million for advertising.

<sup>41</sup> For example, the NMS proposing release in rejecting the so-called “deconsolidation model” proffered through the Seligman Advisory Committee process, expressed concern that it “could prompt calls for active rate regulation.” NMS Release at 11177.

<sup>42</sup> *Id.* at 11184.

<sup>43</sup> The Commission has stated on a number of occasions that it relies on a belief that the exchanges “negotiate” with broker-dealers, vendors, and investors over terms and conditions governing market data, implying that this is why the Commission has not practiced closer oversight. *See* Market Data Concept Release at 70622. The Commission’s reliance is misplaced when it comes to protecting the interests of investors, and is not supported by the facts. Because there is no requirement or incentive for the Network Plans or exchanges to negotiate terms before they make unilateral decisions, they in fact do not negotiate.

<sup>44</sup> The fact that the Commission may abrogate a proposal and require re-filing does not equate to a substantive review or enable a sufficient challenge to the fees. The Commission recently expressed its concern with incompletely justified SRO rule filings. *See* Securities Exchange Act Release No. 49505 (Mar. 30, 2004), 69 Fed. Reg. 17863 (Apr. 5, 2004). We agree with the points the Commission made in that rule proposal, and urge that the same reforms apply to the Network Plans in terms of enhancing public and industry participation in the rulemaking process and providing clear notice of changes that affect fees, user classifications, distribution requirements, and billing practices.

<sup>45</sup> *See In the Matter of Bloomberg L.P. for Review of Action Taken by the New York Stock Exchange, Inc.* (“Bloomberg Action”), SEC Release No. 34-49076 (Jan. 14, 2004). In finding for Bloomberg in its denial of access claim, the Commission concluded that the vendor contract provisions at issue operated as “rules of the exchange,” and because NYSE failed to file them with the SEC for review and approval after public notice and comment they were not valid as applied against Bloomberg.

<sup>46</sup> *See* Market Data Concept Release at 70634.

<sup>47</sup> NMS Release at 11177.

<sup>48</sup> Market Data Concept Release at 70618 (citing Securities Industry Association commissioned study by Arthur Andersen LLP, *Report on Market Data Pricing* 8-15 (June 1999)); Charles Schwab & Co. Inc. memorandum, *Burdens of Market Data Administration* (July 12, 2001), attached as Appendix V to the Report of the Advisory Committee on Market Information, <http://www.sec.gov/divisions/marketreg/marketinfo/appendixv.pdf>

<sup>49</sup> *See generally* Bloomberg Action, discussed above.

<sup>50</sup> Neither retail investors nor small business owners with brokerage accounts “are likely to monitor real-time information for anywhere near as many hours [as professionals] during a month,” explaining why market data fees for non-professionals are and should be much lower than professional fees. Market Data Concept Release at 70631.

<sup>51</sup> *See* Instinet Order at Lexis page 16 (“Customer lists are proprietary and often can be extremely valuable to a vendor’s competitors.”).

<sup>52</sup> NMS Release at 11183.

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<sup>53</sup> *Id.* at 11154.

<sup>54</sup> *Id.* at 11153.

<sup>55</sup> *Id.*

<sup>56</sup> *Id.* at 11184.

<sup>57</sup> *Id.* at 11177.

<sup>58</sup> NYSE describes its new depth of book quotation product, LiquidityQuote, as “assist[ing] with the search for market ‘size’ and depth, that has become more critical since the introduction of decimal increments and penny spreads.” The example given is that instead of bid and offer size of 400 x 700 in the consolidated quote, LiquidityQuote might show 20,000 x 25,000 shares. See “NYSE LiquidityQuote, Adding Transparency to the Market,” [www.nyse.com/pdfs/LiquidityQuote.pdf](http://www.nyse.com/pdfs/LiquidityQuote.pdf). LiquidityQuote is available with a subscription to NYSE OpenBook, which is \$50 per month whether you are a professional or not. That may be a great deal for a professional, but \$600 a year means it is inaccessible to the vast majority of non-professional investors whose orders are reflected in LiquidityQuote. Nasdaq’s new depth of book market data product is “TotalView,” which provides aggregate size of all Nasdaq market participants’ quotations and orders available for execution at the top five price levels. To Nasdaq’s credit, there is a non-professional fee of \$14 per month. But \$168 per year is still out of reach for the vast majority of retail investors.

<sup>59</sup> There would be no incremental cost to the Network Plans or exchanges to provide this data in the consolidated quotation; they already provide it in the data stream distributed to market data vendors and professional investors today.

<sup>60</sup> NYSE supports the trade-through rule, including its expansion into the trading of securities listed on the Nasdaq Stock Market, while opposing the opt-out provisions as harming investors that place limit orders on the NYSE. At the other end of the market structure spectrum, ECNs oppose the trade-through rule, although the opposition is tempered by support for the opt-out provision. ECNS, however, are opposed to the access fee limitations and see them as directly harmful to their business model. The market maker community may come out on both sides of the trade-through rule because, while the Nasdaq Stock Market operates without such a rule, market makers rarely trade-through because of their best execution obligations. Market makers generally support a less constricted opt-out and oppose access fees as distorting the publicly displayed quote.

<sup>61</sup> NMS Hearing Tr. at 8 (quoting Annette Nazareth, Director of the Division of Market Regulation).

<sup>62</sup> *Id.* at 9.

<sup>63</sup> *Id.* at 14.

<sup>64</sup> *Id.* at 13.

<sup>65</sup> *Id.* at 21 (statements by Mr. Sauter, Chief Investment Officer, Vanguard Group).

<sup>66</sup> Regulation SHO was approved by the Commission on June 23, 2004. Beginning January 3, 2005, the Commission will suspend the operation of the current “tick” test in Rule 10a-1 and any short sale price test of any exchange or national securities association for approximately one-third of the stocks in the Russell 1000 index.

<sup>67</sup> Schwab also would support the use of an automated/manual quote exception to the ITS rule in the pilot program, although we believe that cost and delay of developing the systemic solution argues for implementing a simpler exception that reflects the execution methodology of the market as a whole.