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THE NASDAQ STOCK MARKET
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December 8, 2005

Jonathan G. Katz
Secretary
United States Securities and Exchange Commission
Washington, D.C.

Re: SR-NASD-2005-13 – Second Response to Comments

Dear Mr. Katz:

The Nasdaq Stock Market welcomes the opportunity to again respond to comments submitted by Bloomberg Tradebook ("Bloomberg") in connection with above-captioned rule proposal that seeks to treat all Nasdaq Market Center system users fairly by charging them equal fees.[1] Bloomberg's latest comments on the proposal continue to demonstrate a fundamental misunderstanding of the legal standards governing the proposal's review as well as the competitive market environment supporting its adoption.

First, Bloomberg asserts that Nasdaq's proposal does not contain a sufficient discussion of its competitive impact, as required under Section 19 of the Act. Bloomberg is incorrect. As Nasdaq makes clear in its filing, Nasdaq believes that its proposal will not result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Further, Nasdaq's competitive discussion addressed the applicability of Sections 15A and 6(e) to its proposal, as well as alternatives available to disgruntled ECNs that did not wish to participate in the new uniform fee structure. The fact that Bloomberg doesn't like Nasdaq's views on these topics does not render Nasdaq's proposal inconsistent with Section 19, or any other section, of the Act. In short, Bloomberg's agitation over the prospect of losing its privileged pricing advantage in the Nasdaq Market Center, or the mere statement that the proposal confers benefits on others, does not transform Nasdaq's proposal into one implicating the overall competitive environment for the trading of Nasdaq securities.

Second, Bloomberg continues to take the self-serving view that Nasdaq is some sort of monopoly. Bloomberg's letter is rife with buzz words ("monopoly rents", "barriers to entry", "predatory behavior" ect.) that seek to raise the specter of anti-competitive activity. This is particularly true regarding Bloomberg's numerous references to Nasdaq's acquisition of the

1 Given that the bulk of Bloomberg's second comment letter merely reiterates positions taken in their May 20, 2005, comment letter, Nasdaq requests that the Commission incorporate in its entirety Nasdaq's August 5, 2005, letter as part of this response.

INET ATS. As far as Nasdaq can discern, Bloomberg's position amounts to the following: the Commission must allow Bloomberg to continue to use the Nasdaq Market Center to obtain higher access fees so that Bloomberg can have money to buy order flow and continue to "compete," because if Nasdaq buys INET, it will be better able to survive under a uniform fee structure than Bloomberg.

Nowhere, however, does Bloomberg openly acknowledge the voluntary nature of Nasdaq's system and Bloomberg's clear freedom to conduct its business activity elsewhere. Instead, Bloomberg pretends to be a prisoner of the Nasdaq system, albeit a special one, that must be allowed to continue to use Nasdaq under terms and conditions materially different than those applicable to the vast majority of other users. This includes the ability to charge unwilling counterparties an unjustified premium for accessing Bloomberg's liquidity. The false premise of a Nasdaq monopoly is essential to Bloomberg's ongoing assertions that Nasdaq's charging all customers equally is inconsistent with the competition laws and the Securities Exchange Act of 1934 ("Act"). It is also in keeping with Bloomberg's constant attempts to equate the impact of the proposal on its own business with those on the marketplace as a whole. As the example below demonstrates, the reality of Bloomberg's current method of participation in the Nasdaq Market Center cannot support that contention:

Here is how Nasdaq's current pricing structure works for the various entities that elect to participate in the Nasdaq Market Center:

Nasdaq Market Makers:

- If a market maker is providing liquidity, the firm accessing the market maker's liquidity pays between 27 and **30** cents per 100 shares. The market maker providing liquidity receives a rebate between 20 and 25 cents per 100 shares. This same pricing and rebate schedule also applies to ECNs that, like Nasdaq's Brut Facility, determine not to charge a separate liquidity access fee.

Nasdaq Order-Entry Firms

- If an order-entry firm is providing liquidity, the firm accessing the order-entry firm's liquidity pays between 27 and **30** cents per 100 shares, the order-entry firm providing liquidity receives a rebate between 20 and 25 cents per 100 shares.

Bloomberg and Other Fee Charging ECNs

- If an access fee-charging ECN, like Bloomberg, is providing liquidity, the firm accessing its liquidity currently pays Nasdaq 10 cents per 100 shares (capped at $10,000 per month for firms providing more than 2 million shares per day) for routing the order to the ECN, while the fee-charging ECN providing liquidity charges an additional separate fee to the firm of up to 30 cents per 100 shares. Overall, and usually, this results in total changes to an accessing firm of up to **40** cents per 100 shares.

In sum, it costs parties sending orders to the Nasdaq Market Center approximately **33%** more in execution costs when their orders are sent to a fee-charging ECN, like Bloomberg. Since the Nasdaq Market Center operates using execution algorithms that generally do not allow parties to avoid fee-charging ECNs, firms that route orders to multiple markets place the Nasdaq Market Center last in terms destination market preferences by assigning to it the higher fee-charging ECN rate in their routing tables. The result is that fewer orders are routed to the Nasdaq Market Center, and overwhelming majority of its participants (market makers, order-entry firms, and ECNs that do not charge separate access fees) have their opportunities to interact with available order flow diminished. Nasdaq notes that it is the only market that currently operates under this competitive burden as all other markets already have unified pricing schedules that do not allow their participants to charge extra fees when they are accessed through the market's system. Despite Bloomberg's best efforts to conjure one up, there is simply no reading of the Exchange Act, that would mandate that Nasdaq continue to be the method for Bloomberg to capture order flow from which it can extort uncompetitive and excessive access fees from other market participants.

Bloomberg's faulty interpretation of Exchange Act requirements also extends to its views on the ability of markets to set fees for system users. Bloomberg argues that Nasdaq is prohibited from adopting a uniform fee structure by Section 15(b) of that Act that prohibits a registered national securities association from imposing "any schedule or fix rates of commissions, allowances, discounts, or other fees to be charged by its members ...". This exact argument was specifically rejected by the Commission in its approval of an earlier Nasdaq proposal that capped the access fees of ECNs participating in the Nasdaq Market Center.[2] In that approval, the Commission found that the imposition of a maximum access fee cap by Nasdaq was not a fixing of commissions, but rather a condition for participation in Nasdaq's trading system. This is also the case with Nasdaq' instant proposal to establish a uniform fee structure, adherence to which would likewise be a condition for participation in the Nasdaq Market Center and not a general fixing of commission rates.

Section 15(b)'s restrictions on the fixing of fees applies only to those fees that a broker dealer charges it customers. This is borne out by the legislative history accompanying the adoption of that provision which provides in relevant part:

As safeguards against abuse, and to make clear that activities of associations under this paragraph are to be consistent with the operation of free and open markets, this paragraph provides that the rules of an association may not be designed to permit unfair

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2 See SEC Release No. 34-49220 (February 11, 2004).

> *discrimination between customers, or issuers, or brokers or dealers, nor to fix minimum profits, nor to impose any schedule of prices, nor to fix minimum rates or impose any schedule of commissions, allowances, discounts, or other charges. Thus, to provide safeguards against unreasonable profits, it is contemplated that associations may adopt rules designed to prevent each member thereof from exacting in any particular transaction a profit which reasonable men would agree was unconscionable in the light of all of the concrete facts and circumstances of that transaction; but an association, whether in a bona fide attempt to prevent or under the pretext of preventing unreasonable profits, may not impose any schedule of prices or commissions.*

It is only in the context of an association's attempt to dictate what a firm may charge its own customers directly that the above provision applies. Nasdaq's uniform fee proposal doesn't do that. It simply imposes, as a condition for participation in the Nasdaq Market Center, that participants not change any additional separate fee when orders are delivered to them by the system. Bloomberg remains free to charge its own customers whatever fee it wishes for services unrelated to its participation in the Nasdaq Market Center.[3] Indeed, to equate Nasdaq's uniform fee proposal with an improper fixing of commissions would mean that Nasdaq is not authorized to impose any fees for use of its systems – a result in direct contradiction to Section 15A(b)(5) of the Exchange Act authorizing such fees.

Sincerely,

Thomas P. Moran
Office of General Counsel

[3] While Bloomberg does not make its fee schedule public, it is Nasdaq's belief that Bloomberg charges customers directly accessing its system outside of the Nasdaq Market Center lower access fees to encourage direct connection to its system. This approach is also followed by other ECNs including the Track ECN that, according to its published fee schedule, charges less when accessed directly than when an order is delivered to it via Nasdaq.