SECURITIES AND EXCHANGE COMMISSION


Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Modify Port Fees

July 30, 2012.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) ⁷, and Rule 19b–4 thereunder, ² notice is hereby given that on July 19, 2012, The NASDAQ Stock Market LLC (“NASDAQ” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II and III below, which Items have been published by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

NASDAQ proposes to modify the port fees charged to members and non-members for ports used to enter orders into NASDAQ systems, in connection with the use of other trading telecommunication protocols.

The text of the proposed rule change is below. Proposed new language is in italics. ³

7015. Access Services

(a)–(f) No change.

(g) Other Port Fees.

The following port fees shall apply in connection with the use of other trading telecommunication protocols:

• $500 per month for each port pair, other than Multicast ITCH® data feed pairs, for which the fee is $1000 per month for software-based TotalView-ITCH or $2,500 per month for combined software- and hardware-based TotalView-ITCH.
• An additional $200 per month for each port used for entering orders or quotes over the Internet.
• An additional $600 per month for each port used for market data delivery over the Internet.

(b) No change.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, NASDAQ included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NASDAQ has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

NASDAQ is proposing to amend NASDAQ Rule 7015 (Access Services) to modify the monthly fee it charges for ports used to enter orders in NASDAQ trading systems, such as the NASDAQ Market Center and the NASDAQ Options Market [sic], in connection with the use of other trading telecommunication protocols.

Specifically, the fee change is to establish an optional new $2,500 per month port fee for those customers that elect to take the hardware-based TotalView-ITCH equities depth feed that uses field-programmable gate array (“FPGA”) technology, ⁴ in addition to the software-based TotalView-ITCH version, to receive delivery of NASDAQ Depth-of-Book data, defined in NASDAQ Rule 7023 to include TotalView, OpenView, and NASDAQ Level 2 (collectively, “NASDAQ Depth data”). In offering this new optional port fee using a hardware-delivery mechanism, NASDAQ is serving those customers requiring a predictable latency profile throughout the trading day. By taking advantage of hardware parallelism, FPGA technology is capable of processing more data packets during peak market conditions without the introduction of variable queuing latency.

Currently, in accordance with NASDAQ Rule 7015(g), customers receiving TotalView-ITCH pay $1,000 per multiscast ITCH data feed port pair for the software-version of the depth feed. This optional new port fee enables a customer to opt to receive both the software- and hardware-based versions for a total of $2,500, meaning that for an additional $1,500 per month a customer can receive the hardware-based version. This new pricing option is available to all members and non-members and is in response to industry demand, as well as due to changes in the technology to distribute and consume market data.

Competition for depth data is considerable and the Exchange believes that this proposal clearly evidences such competition. The Exchange is offering a new port fee in order to keep pace with changes in the industry and evolving customer needs as new technologies emerge and products continue to develop and change. It is entirely optional and is geared towards attracting new customers, as well as retaining existing customers.

The proposed port fee is based on pricing conventions and distinctions that exist in NASDAQ’s current fee schedule, and the fee schedules of other exchanges. These distinctions for the proposed port fee for hardware-based delivery of NASDAQ Depth data are based on a careful analysis of empirical data and the application of time-tested pricing principles already accepted by the Commission and discussed in greater depth in the Statutory Basis section below. Also, the costs associated with the port fee using the hardware-based delivery system for NASDAQ Depth data are higher than a software-based solution due to increased operating expenditures associated with creating, shipping, installing and maintaining the new equipment and codebase. Because it uses a distinct technology, the overall costs of creation and maintenance of the hardware-based version of TotalView-ITCH are higher than the software-based version.

The proposed port fee for the hardware-based delivery of NASDAQ Depth data is completely optional. Accordingly, NASDAQ is offering this new port fee for the hardware-based delivery of NASDAQ Depth data so that customers may elect to receive NASDAQ direct data content in a predictable manner throughout the trading day.


2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 6 of the Act, in general, and with Section 6(b)(4) of the Act. According to a 2005 Commission Grant of Self-Regulatory Organization Status of the NASDAQ-OMIEX Corporation (70 FR 37496 (June 29, 2005)) the Commission granted self-regulatory organizations and broker-dealers increased authority and flexibility to offer new and unique market data to the public. It was believed that this authority would expand the amount of data available to consumers, and also spur innovation and competition for the provision of market data.

The Commission concluded that Regulation NMS—by deregulating the market in proprietary data—would itself further the Act’s goals of facilitating efficiency and competition:

Efficiency is promoted when broker-dealers who do not need the data beyond the prices, sizes, market center identifications of the NBBO and consolidated last sale information are not required to receive (and pay for) such data. The Commission also believes that efficiency is promoted when broker-dealers may choose to receive (and pay for) additional market data based on their own internal analysis of the need for such data. By removing “unnecessary regulatory restrictions” on the ability of exchanges to sell their own data, Regulation NMS advanced the goals of the Act and the principles reflected in its legislative history. If the free market should determine whether proprietary data is sold to broker-dealers at all, it follows that the price at which such data is sold should be set by the market as well.

Nasdaq Depth data is precisely the sort of market data product that the Commission envisioned when it adopted Regulation NMS.

On July 21, 2010, President Barack Obama signed into law H.R. 4173, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”), which amended Section 19 of the Act. Among other things, Section 916 of the Dodd-Frank Act amended paragraph (C) of Section 19(b)(3) of the Exchange Act to read, in pertinent part, “At any time within the 60-day period beginning on the date of filing of such a proposed rule change in accordance with the provisions of paragraph (1) [of Section 19(b)], the Commission summarily may suspend the change in the rules of the self-regulatory organization made thereby, if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this title. If the Commission takes such action, the Commission shall institute proceedings under paragraph (2)[B] [of Section 19(b)] to determine whether the proposed rule should be approved or disapproved.”

Nasdaq believes that these amendments to Section 19 of the Act reflect Congress’ intent to allow the Commission to rely upon the forces of competition to ensure that fees for market data are reasonable and equitably allocated. Although Section 19(b) had formerly authorized immediate effectiveness for a “due, fee or other charge imposed by the self-regulatory organization,” the Commission adopted a policy and subsequently a rule stipulating that fees for data and other products available to persons that are not members of the self-regulatory organization must be approved by the Commission after first being published for comment. At the time, the Commission supported the adoption of the policy and the rule by pointing out that unlike members, whose representation in self-regulatory organization governance was mandated by the Act, non-members should be given the opportunity to comment on fees before being required to pay them, and that the Commission should specifically approve all such fees. Nasdaq believes that the amendment to Section 19 reflects Congress’ conclusion that the evolution of self-regulatory organization governance and competitive market structure have rendered the Commission’s prior policy on non-member fees obsolete.

For the reasons stated above, Nasdaq believes that the proposed fee is fair and equitable, and not unreasonably discriminatory. As described above, the proposed fee is based on pricing conventions and distinctions that exist in Nasdaq’s current fee schedule, and the fee schedules of other exchanges. These distinctions (e.g., internal versus external distribution and hardware-based versus software-based system for delivering Nasdaq Depth data) are based on principles of fairness and equity that have helped for many years to maintain fair, equitable, and not unreasonably

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discriminatory fees, and that apply with equal or greater force to the current proposal. The optional port fee for the hardware-based delivery of Nasdaq Depth data is based on careful analysis of empirical data and the application of time-tested pricing principles already accepted by the Commission for many years.

As described in greater detail below, if Nasdaq has calculated improperly and the market deems the proposed fees to be unfair, inequitable, or unreasonably discriminatory, firms can diminish or discontinue the use of their data because the proposed fee is entirely optional to all parties. Firms are not required to purchase Nasdaq Depth data or to utilize any specific pricing alternative if they do choose to purchase Nasdaq Depth data. Nasdaq is not required to make depth data available or to offer specific pricing alternatives for potential purchases. Nasdaq can discontinue offering a pricing alternative (as it has in the past) and firms can discontinue their use at any time and for any reason (as they often do), including due to their assessment of the reasonableness of fees charged. Nasdaq continues to create new pricing policies aimed at increasing fairness and equitable allocation of fees among users, and Nasdaq believes this is another useful step in that direction.

B. Self-Regulatory Organization’s Statement on Burden on Competition

Nasdaq 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 the Act, as amended. Notwithstanding its determination that the Commission may rely upon competition to establish fair and equitable allocation of fees among users, Nasdaq believes this is another useful step in that direction.

Analyzing the cost of market data distribution in isolation from the cost of all of the inputs supporting the creation of market data will inevitably underestimate the cost of the data. Thus, because it is impossible to create data without a fast, technologically robust, and well-regulated execution system, system costs and regulatory costs affect the price of market data. It would be equally misleading, however, to attribute all of the exchange’s costs to the market data portion of an exchange’s joint product. Rather, all of the exchange’s costs are incurred for the unified purposes of attracting order flow, executing and/or routing orders, and generating and selling data about market activity. The total return that an exchange earns reflects the revenues it receives from both products and the joint costs it incurs. Moreover, an exchange’s customers view the costs of transaction executions and of data as a unified cost of doing business with the exchange. A broker-dealer will direct orders to a particular exchange only if the expected revenues from executing trades on the exchange exceed net transaction execution costs and the cost of data that the broker-dealer chooses to buy to support its trading decisions (or those of its customers). The choice of data products is, in turn, a product of the value of the products in making profitable trading decisions. If the cost of the product exceeds its expected value, the broker-dealer will choose not to buy it. Moreover, as a broker-dealer chooses to direct fewer orders to a particular exchange, the value of the product to that broker-dealer decreases, for two reasons. First, the product will contain less information, because executions of the broker-dealer’s orders will not be reflected in it. Second, and perhaps more important, the product will be less valuable to that broker-dealer because it does not provide information about the venue to which it is directing its orders. Data from the competing venue to which the broker-dealer is directing orders will become correspondingly more valuable.

Thus, a super-competitive increase in the fees charged for either transactions or data has the potential to impair revenues from both products. “No one disputes that competition for order flow is ‘fierce.’” NetCoalition at 24. However, the existence of fierce competition for order flow implies a high degree of price sensitivity on the part of broker-dealers with order flow, since they may readily reduce costs by directing orders toward the lowest-cost trading venue. A broker-dealer that shifted its order flow from one platform to another in response to order execution price differentials would both reduce the value of that platform’s market data and reduce its own need to consume data from the disfavored platform. Similarly, if a platform increases its market data fees, the change will affect the overall cost of doing business with the platform, and affected broker-dealers will assess whether they can lower their trading costs by directing orders elsewhere and thereby lessening the need for the more expensive data.

Analyzing the cost of market data distribution in isolation from the cost of all of the inputs supporting the creation of market data will inevitably underestimate the cost of the data. Thus, because it is impossible to create data without a fast, technologically robust, and well-regulated execution system, system costs and regulatory costs affect the price of market data. It would be equally misleading, however, to attribute all of the exchange’s costs to the market data portion of an exchange’s joint product. Rather, all of the exchange’s costs are incurred for the unified purposes of attracting order flow, executing and/or routing orders, and generating and selling data about market activity. The total return that an exchange earns reflects the revenues it receives from the joint products and the total costs of the joint products.

Competition among trading platforms can be expected to constrain the aggregate return each platform earns from the sale of its joint products, but different platforms may choose from a range of possible, and equally reasonable, pricing strategies as the means of recovering total costs. For example, some platform may choose to pay rebates to attract orders, charge relatively low prices for market information (or provide information free of charge) and charge relatively high prices for accessing posted liquidity. Other platforms may choose a strategy of paying lower rebates to attract orders, setting relatively high prices for market information, and
setting relatively low prices for accessing posted liquidity. In this environment, there is no economic basis for regulating maximum prices for one of the joint products in an industry in which suppliers face competitive constraints with regard to the joint offering. This would be akin to strictly regulating the price that an automobile manufacturer can charge for car sound systems despite the existence of a highly competitive market for cars and the availability of after-market alternatives to the manufacturer-supplied system.

The market for market data products is competitive and inherently contestable because there is fierce competition for the inputs necessary to the creation of proprietary data and strict pricing discipline for the proprietary products themselves. Numerous exchanges compete with each other for listings, trades, and market data itself, providing virtually limitless opportunities for entrepreneurs who wish to produce and distribute their own market data. This proprietary data is produced by each individual exchange, as well as other entities, in a vigorously competitive market.

Broker-dealers currently have numerous alternative venues for their order flow, including ten self-regulatory organization (“SRO”) markets, as well as internalizing broker-dealers (“BDs”) and various forms of alternative trading systems (“ATSs”), including dark pools and electronic communication networks (“ECNs”). Each SRO market competes to produce transaction reports via trade executions, and two FINRA-regulated Trade Reporting Facilities (“TRFs”) compete to attract internalized transaction reports. Competitive markets for order flow, executions, and transaction reports provide pricing discipline for the inputs of proprietary data products.

The large number of SROs, TRFs, BDs, and ATSs that currently produce proprietary data or are currently capable of producing it provides further pricing discipline for proprietary data products. Each SRO, TRF, ATS, and BD is currently permitted to produce proprietary data products, and many currently do or have announced plans to do so, including Nasdaq, NYSE, NYSE MKT, NYSEArca, and BATS.

Any ATS or BD can combine with any other ATS, BD, or multiple ATSs or BDs to produce joint proprietary data products. Additionally, order routers and market data vendors can facilitate single or multiple broker-dealers’ production of proprietary data products. The potential sources of proprietary products are virtually limitless.

The fact that proprietary data from ATSs, BDs, and vendors can by-pass SROs is significant in two respects. First, non-SROs can compete directly with SROs for the production and sale of proprietary data products, as BATS and Arca did before registering as exchanges by publishing proprietary book data on the Internet. Second, because a single order or transaction report can appear in an SRO proprietary product, a non-SRO proprietary product, or both, the data available in proprietary products is exponentially greater than the actual number of orders and transaction reports that exist in the marketplace.

Market data vendors provide another form of price discipline for proprietary data products because they control the primary means of access to end users. Vendors impose price restraints based upon their business models. For example, vendors such as Bloomberg and Thomson Reuters that assess a surcharge on data they sell may refuse to offer proprietary products that end users will not purchase in sufficient numbers. Internet portals, such as Google, impose a discipline by providing only data that will enable them to attract “eyeballs” that contribute to their advertising revenue. Retail broker-dealers, such as Schwab and Fidelity, offer their customers proprietary data only if it promotes trading and generates sufficient commission revenue. Although the business models may differ, these vendors’ pricing discipline is the same: They can simply refuse to purchase any proprietary data product that fails to provide sufficient value. Nasdaq and other producers of proprietary data products must understand and respond to these varying business models and pricing disciplines in order to market proprietary data products successfully.

In addition to the competition and price discipline described above, the market for proprietary data products is also highly contestable because market entry is rapid, inexpensive, and profitable. The history of electronic trading is replete with examples of entrants that swiftly grew into some of the largest electronic trading platforms and proprietary data producers: Archipelago, Bloomberg Tradebook, Island, RediBook, Attain, TracECN, BATS Trading and Direct Edge. A proliferation of dark pools and other ATSs operate profitably with fragmentary shares of consolidated market volume.

Regulation NMS, by deregulating the market for proprietary data, has increased the contestability of that market. While broker-dealers have previously published their proprietary data individually, Regulation NMS encourages market data vendors and broker-dealers to produce proprietary products cooperatively in a manner never before possible. Multiple market data vendors already have the capability to aggregate data and disseminate it on a profitable scale, including Bloomberg, and Thomson Reuters.

The court in NetCoalition concluded that the Commission had failed to demonstrate that the market for market data was competitive based on the reasoning of the Commission’s NetCoalition order because, in the court’s view, the Commission had not adequately demonstrated that the depth-of-book data at issue in the case is used to attract order flow. Nasdaq believes, however, that evidence not before the court clearly demonstrates that availability of data attracts order flow. For example, as of July 2010, 92 of the top 100 broker-dealers by shares executed on Nasdaq consumed Level 2/NQDS and 80 of the top 100 broker-dealers consumed TotalView. During that month, the Level 2/NQDS-users were responsible for 94.44% of the orders entered into Nasdaq and TotalView users were responsible for 92.98%.

Competition among platforms has driven Nasdaq continually to improve its platform data offerings and to cater to customers’ data needs. For example, Nasdaq has developed and maintained multiple delivery mechanisms (IP, multi-cast, and compression) that enable customers to receive data in the form and manner they prefer and at the lowest cost to them. Nasdaq offers front end applications such as its “Bookviewer” to help customers utilize data. Nasdaq has created new products like TotalView Aggregate to complement TotalView-ITCH and Level 2/NQDS, because offering data in multiple formatting allows Nasdaq to better fit customer needs. Nasdaq offers data via multiple extranet providers, thereby helping to reduce network and total cost for its data products. Nasdaq has developed an online administrative system to provide customers transparency into their data feed requests and streamline data usage reporting. Nasdaq has also expanded its Enterprise License options that reduce the administrative burden and costs to firms that purchase market data.

Despite these enhancements and a dramatic increase in message traffic, Nasdaq’s fees for market data have remained flat. In fact, as a percent of total customer costs Nasdaq data fees have fallen relative to other data usage costs—including bandwidth.
programming, and infrastructure—that have risen. The same holds true for execution services; despite numerous enhancements to Nasdaq’s trading platform, absolute and relative trading costs have declined. Platform competition has intensified as new entrants have emerged, constraining prices for both executions and for data.

The vigor of competition for depth information is significant and the Exchange believes that this proposal clearly evidences such competition. Nasdaq is offering a new port fee in order to keep pace with changes in the industry and evolving customer needs. It is entirely optional and is geared towards attracting new customers, as well as retaining existing customers.

The Exchange has witnessed competitors creating new products and innovative pricing in this space over the course of the past year. Nasdaq continues to see firms challenge its pricing on the basis of the Exchange’s explicit fees being higher than the zero-priced fees from other competitors such as BATS. In all cases, firms make decisions on how much and what types of data to consume on the basis of the total cost of interacting with Nasdaq or other exchanges. Of course, the explicit data fees are but one factor in a total platform analysis. Some competitors have lower transactions fees and higher data fees, and others are vice versa. The market for this depth information is highly competitive and continually evolves as products develop and change.

C. Self-Regulatory Organization’s Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A)(i) of the Act. At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission’s Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an email to rule-comments@sec.gov. Please include File Number SR–NASDAQ–2012–088 on the subject line.

Paper Comments

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090.

All submissions should refer to File Number SR–NASDAQ–2012–088. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission’s Internet Web site (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission’s Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–NASDAQ–2012–088 and should be submitted on or before August 24, 2012.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.9

Kevin M. O’Neill,
Deputy Secretary.

[FR Doc. 2012–18999 Filed 8–2–12; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–67540; File No. SR–
NYSEArca–2012–77]

Self-Regulatory Organizations; NYSE
Arca, Inc.; Notice of Filing and
Immediate Effectiveness of Proposed
Rule Change Amending the NYSE Arca
Equities Schedule of Fees and
Charges for Exchange Services

July 30, 2012.

Pursuant to Section 19(b)(1)10 of the
Securities Exchange Act of 1934 (the
“Act”) and Rule 19b–4 thereunder,11 notice is hereby given that, on July 18,
2012, NYSE Arca, Inc. (the “Exchange”
or “NYSE Arca”) filed with the
Securities and Exchange Commission
(the “Commission”) the proposed rule
change as described in Items I, II and III
below, which Items have been prepared
by the self-regulatory organization. The
Commission is publishing this notice to
solicit comments on the proposed rule
change from interested persons.

I. Self-Regulatory Organization’s
Statement of the Terms of Substance of
the Proposed Rule Change

The Exchange proposes to amend the
NYSE Arca Equities Schedule of Fees
and Charges for Exchange Services
(“Fee Schedule”). The text of the
proposed rule change is available on the
Exchange’s Web site at www.nyse.com,
at the principal office of the Exchange,
and at the Commission’s Public
Reference Room.

II. Self-Regulatory Organization’s
Statement of the Purpose of, and
Statutory Basis for, the Proposed Rule
Change

In its filing with the Commission, the
self-regulatory organization included
statements concerning the purpose of, and
basis for, the proposed rule change and
discussed any comments it received on
the proposed rule change. The text of
those statements may be examined at
the places specified in Item IV below.
The Exchange has prepared summaries,
set forth in sections A, B, and C below,