



BETTER MARKETS

May 26, 2020

Mrs. Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Market Data Infrastructure Release (No. 34–88216; File No. S7–03–20; RIN 3235–AM61)

Dear Secretary Countryman:

Better Markets¹ appreciates the opportunity to comment² on the above-captioned notice (“Notice” or “Release” or “Proposal”) released for public comment by the Securities and Exchange Commission (“SEC” or “Commission”).³ We thank the Commission and staff for the immense amount of effort that must have required to put together this important reforms package.

Together with the “Rescission of Effective-Upon-Filing Procedure for NMS Plan Fee Amendments,”⁴ and the order directing NMS Plan sponsors—the self-regulatory organizations (“SROs”) such as exchanges and the Financial Industry Regulatory Organization (“FINRA”)—to create a new, single consolidated data plan and other governance reforms,⁵ the Commission will democratize access to data, better protect investors, and further instill market integrity.

We urge the Commission to approve the Proposal. Without access to timely, content-rich, and affordable market data, investors cannot make informed investment decisions and protect themselves. Without access to such data, financial professionals cannot serve the needs of their clients—retirees, investors, and savers—and cannot fulfill their regulatory obligations, such as best execution. And without such data and the market structure necessary to sustain it, the Commission

¹ Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans’ jobs, savings, retirements, and more.

²At the onset, we would like to notify the Commission that we may supplement this comment letter with additions to either offer further commentary on separate aspects of the Proposal or to rebut and respond to other commenters.

³ See Market Data Infrastructure Release (No. 34–88216; File No. S7–03–20; RIN 3235–AM61), 85 Fed. Reg. 16726 (March 24, 2020) available at <https://www.govinfo.gov/content/pkg/FR-2020-03-24/pdf/2020-03760.pdf>.

⁴ See Rescission of Effective-Upon-Filing Procedure for NMS Plan Fee Amendments, Release Nos. 34–87193, File No. S7–15–19, 84 Fed. Reg. 54794 (October 11, 2019) available at <https://www.federalregister.gov/documents/2019/10/11/2019-21770/rescission-of-effective-upon-filing-procedure-for-nms-plan-fee-amendments>.

⁵ See Commission’s announcement (May 6, 2020) available <https://www.sec.gov/news/press-release/2020-103>.

cannot protect investors and restore investors' confidence in the fundamental fairness of our markets.

Finally—since the Release requests general comments and comments on additional (or alternative) regulatory measures—we offer some further comments for the Commission to consider as it reforms the current market structure in general, and the conflicted-to-the-core nature of exchanges' grip on vital market data.

DESCRIPTION OF THE PROPOSAL

The Commission is proposing to expand the content of the so-called “core data” that is currently required to be collected, consolidated, and disseminated as part of the national market system under Regulation NMS. The Commission also proposes to “amend the method by which such NMS information is collected, calculated, and disseminated by introducing a decentralized consolidation model where competing consolidators replace the exclusive securities information processors.”⁶

Specifically, the Commission is proposing to define “core data” and expand its elements to include, “(1) information about orders in sizes smaller than the current round lot size for certain higher priced stocks; (2) information about certain orders that are outside of the best bid and best offer (i.e., certain depth of book data); and (3) information about orders that are participating in opening, closing, and other auctions.”⁷

Secondly, the Commission is proposing to require each SRO “to make all of its market data that is necessary to generate consolidated market data (as proposed to be defined) directly available to two new categories of entities: (1) Competing consolidators and (2) self-aggregators.” These competing consolidators could either be the current SROs or newly formed SIPs registered with the Commission (and subject to disclosure requirements and compliance with Regulation SCI) that would be responsible for collecting, consolidating, and disseminating consolidated market data to the public. And the self-aggregators would new entities (registered with the SEC and) that “would be brokers or dealers that elect to collect and generate consolidated market data for their own internal use.”⁸ In order for this new construct to work, each SRO would be required to make “all of its own data that is necessary to generate consolidated market data available to competing consolidators and self-aggregators directly from its data center, and in the same manner and using the same methods, including all methods of access and the same format, as it makes its proprietary market data products available to any market participant.”⁹

SUMMARY

We believe the expansion of “core data” would democratize market data—itsself a product of the decisions of thousands of market participants and millions of investors’—which would in turn promote fair and efficient markets and would facilitate the best execution of investor orders,

⁶ See Release at 16726.

⁷ See Release at 16730.

⁸ See Release at 16730.

⁹ See Release at 16730.

and reduce information asymmetries between market participants who currently rely on such data made available through the SIPs and those who have access to both SIPs data and proprietary data. We further believe the expansion of “core data” would serve as a countervailing check on the rampant increase of the cost of proprietary data, which should reduce the cost of intermediation and serve the interest of investors, savers, and retirees.

We support the inclusion of odd-lot information, depth-of-book data up to five levels above and below NBBO, and the inclusion of auction information. These information taken together amount would fill a significant gap that currently exists in the SIP data.

We further believe that by repealing the monopoly privileges exchanges enjoy—in creating, managing, setting the prices for, and controlling the SIPs and their data—the Commission would insert competitive and market forces, which should help market participants to more timely, efficiently, and in cost-effective manner access needed market data.

BACKGROUND AND GENERAL COMMENTS

As part of the National Market System, the SEC requires SROs to establish certain facilities and gather and consolidate certain market data that is used by market participants, including investors both retail and institutional, to make informed investment decisions and trades. These facilities include the securities information processors (“SIPs”) and in the future will include the CAT NMS.

These SIPs currently gather and consolidate the so-called “core data” that market participants are either regulatorily obligated to obtain or need to meaningfully participate in the markets. This core data includes: (1) the price, size, and exchange of the last sale; (2) each exchange’s current highest bid and lowest offer, and the shares available at those prices; and (3) the national best bid and offer (i.e., the highest bid and lowest offer currently available on any exchange, “NBBO”). Additionally, these SIPs collect, calculate, and disseminate certain regulatory data, including information required by the National Market System Plan to Address Extraordinary Market Volatility (“LULD Plan”), information relating to regulatory halts and market-wide circuit breakers (“MWCBS”), and information regarding short-sale circuit breakers.

The same exchanges that gather and supply the SIPs data are also permitted to gather, consolidate, and sell a much more robust dataset and are permitted to sell privileged access to such proprietary and more robust content-rich data to those market participants that can—or feel they must—purchase such data and access. This additional and more content-rich data includes certain depth-of-book (“DOB”) products that are “generally characterized as fast, low-latency products designed for automated trading systems that include additional content.”¹⁰ These DOB products include—in addition to the typical SIP data described above—information on odd-lots, orders at multiple levels above and below the NBBO, and information about auctions.

In addition to their ability to consolidate and sell proprietary, content-rich data, the exchanges sell a variety of privileged access to such data, such as “colocation at primary data

¹⁰ See Release at 16731.

centers, fiber optic connectivity, wireless connectivity, and point-of-presence connectivity at third-party data centers.”¹¹

The SROs are authorized to charge reasonable fees to market participants (i.e., subscribers of the data feeds) to access the core data they supply to SIPs. The SROs are permitted to distribute the excess “profits” among the sponsors of the particular NMS Plan. Total fees generated by the various NMS Plans, excluding the CAT NMS, from market participants (including investors) exceeded \$500 million in 2017. Importantly, they are permitted to charge—both in the case of SIPs and proprietary data—fees that could be in excess of the cost of producing such data.

A recent report analyzed the various costs that go into provisioning such data and the prices that market participants pay to access the same data. The report¹² compared one exchange’s costs—the Investors Exchange (IEX)—on a per user basis, to the fees charged by NYSE (ICE), Nasdaq, and Cboe. IEX is in a unique position to have done this sort of analysis because, to run its own exchange, IEX is required to pay for market data and connectivity at levels that are similar to what other industry firms must pay. The findings were eye-opening.

For example, the IEX report showed that the three large family of exchanges charge:

- For depth of book data products, fees between 900–1,800% over IEX’s costs to offer a comparable product;
- For physical connectivity in their data centers, fees between 2,000–4,200% over IEX’s costs to offer comparable services, and;
- For virtual sessions needed to trade (i.e., “logical connectivity,”) other exchanges charge fees 500–1,800% over IEX’s cost to offer comparable services.

The robust data in the report convincingly suggests that the fees these exchanges impose on market participants are neither fair nor reasonable, and that they go well-beyond what is necessary to produce and make available this data and connectivity services. It appears that these large exchanges are able to impose such burdensome, needless costs on market participants because—for market participants to meet their regulatory obligations—those market participants have no choice but to purchase these data and access rights.

Importantly, currently, the NMS plan sponsors fee-setting rules are self-effectuating, in that they are effective immediately upon filing with the Commission. The NMS Plan sponsors can begin charging users of their facility or data immediately after filing with the Commission and before these users—or anyone else—have an opportunity to read, review or comment to the Commission whether the fees are reasonable. The Commission can abrogate the filing within 60 days and require the plan sponsors to re-file according to a standard procedure which would in turn require the Commission to publish the fee-setting rule filing for notice and comment. But because commenters seldom comment on fee-filings that are effective-upon-filing (and often they do not even know a fee change is coming), the Commission seems to lack the knowledge and basis

¹¹ See Release at 16731.

¹² See Comment Letter from Brad Katsuyama, January 29, 2019. Available at <https://www.sec.gov/comments/4-729/4729-4845907-177246.pdf>.

to abrogate filings. Indeed, since 2010, of the 38 fee-setting filings, the Commission has only abrogated a total of three filings (and all three of these were in 2017 and 2018).

Data fees and Access Fees Are Substantial.

The fees charged by most of the exchanges (notable exception is IEX, which does NOT charge for any of its proprietary data) are substantial and investors must pay them either directly or indirectly through their brokers. All broker-dealers are under regulatory obligations to obtain access to “core data” produced by SIPs, and because, as noted above, the information contained in the package is often unavailable anywhere else, those producing such data have monopolistic economic power in setting its price. Because trading data is critical, and often SIP data is both too slow to obtain and too sparse to make competitive investment decisions relying on it, market participants are essentially obligated to purchase the proprietary data and low-latency access to such data offered at great premium by the exchanges.

The Exchanges Suffer from Conflicts of Interest in Setting Running both SIPs and Selling Their Own Data And Access Privileges.

Currently, the NMS Plan sponsors are the national securities exchanges and FINRA. Of these sponsors, all but one are profit-seeking exchanges. Of the 23 stock exchanges operating in the United States, 19 are owned by only three publicly traded conglomerates with their own shareholders and boards of directors that are focused on maximizing profits. This means three entities *de facto* control 19 of the 24 votes on NMS Plans, which gives them dominant power to set prices for accessing core data and their own proprietary data and access privileges.

Importantly, given the authority to impose fees beyond the cost necessary to produce the their own proprietary and content-rich data or run the facilities *and* the sponsors’ authority to share among themselves this excess revenue, the sponsors have all the incentives to use their regulatorily-granted near-monopoly power to increase the profits of their owners, the publicly traded holding companies. Some of these sponsors have a long rap-sheet for violating SEC rules and securities laws, in some cases harming their own members.¹³ It is in this environment that a Commission—statutorily mandated to protect investors and prioritize the public’s interest in perfecting the mechanisms of the securities markets—must would serve as a vital check against the clear conflicts of interest present in this arrangement.

COMMENTS

Current features of our market structure—including the dominant exchanges, certain unscrupulous high-frequency traders, and the rules that have enabled these—have meant that investors, savers, and retirees are preyed upon. These practices have driven investors (along with some of the brokers and market makers that serve them) to off-exchange and onto opaque, less-

¹³ See, for example, “SEC Charges Direct Edge Exchanges [owned by BATS Exchange] With Failing to Properly Describe Order Types.” Penalty: at least \$14 million. See, also, “SEC Charges NYSE, NYSE ARCA, and NYSE MKT for Repeated Failures to Operate in Accordance With Exchange Rules.” Penalty: at least \$4.5 million. See, also, “SEC Charges NASDAQ for Failures During Facebook IPO.” Penalty: at least \$10 million. See, also, “SEC Charges New York Stock Exchange for Improper Distribution of Market Data.” Penalty: at least \$5 million.

regulated trading venues. The resultant decline in transparency and displayed liquidity is a policy failure must be resolved by active Commission intervention. Some of these deep, structural, conflict-ridden practices cannot be left in the hands of the very entities—most of the exchanges and the HFT firms that take advantage of such exploits—that have created in the first place. It is now clear the self-regulation has failed as it relates to the provision of content-rich and timely data.

Legacy Exchanges’ Self-interest—And Unacceptably Lax Regulatory Shortcoming—Have Created a Vicious Cycle That Must Be Broken

The dominant exchanges have failed to protect investors, and worse they have enabled and profited from the predatory actions of certain market participants that have preyed upon retail investors, savers, and retirees. These practices of these exchanges have driven investors (along with some of the brokers and market makers that serve them) to off-exchange and onto opaque, less-regulated trading venues.

Today, firms with the fastest and technologically most up-to-date capabilities and access to most content-rich data can—and often do—exploit features of our current market infrastructure and rules that permit them to reap undue advantages. Profits earned by firms that engage in predatory trading strategies fund the purchase of exchange market data and connectivity (even as prices continue to rise) which are needed to execute predatory trading strategies. This has disenfranchised not just investors but also brokers and market makers that serve them. Early this year, Commission’s counterpart in the United Kingdom—the Financial Conduct Authority—published a groundbreaking study showing that these market structure failures cost investors in aggregate, over \$5 billion a year.¹⁴

These practices—and the market structure and rules that permit it—represent a hidden but enormous tax on savers and retirees. But unlike the taxes levied by governments, investors receive no benefits for it and have no ability to control it. Current market structure allows investors’ order to be traded at stale prices. Stale prices can occur when investors—and those serving them—do not have access to timely and content-rich data. This discourages liquidity providers from entering the market. As this rampant latency arbitrage goes unchecked, the flight away from exchanges and into dark pools is a policy nightmare: robbing investors and markets of transparency, impairing price discovery and driving volume into less-regulated venues.

Access to content-rich core data and ease-of-access to such data—both as proposed in the Release—put investors and those who serve them at a significant disadvantage. Only the Commission through its regulatory mandate can level the playing field and set fairness. And it must do so by approving this Release.

The Commission Must Do More to Rid Conflicts of Interests Present in NMS Plans And Require Public Oriented and Pro-Investor Mission and Policies at Current SIPs And The New Competing SIPs.

¹⁴ See “Ultrafast Trading Costs Stock Investors Nearly \$5 Billion a Year, Study Says,” Wall Street Journal (January 27, 2020), available at <https://www.wsj.com/articles/ultrafast-trading-costs-stock-investors-nearly-5-billion-a-year-study-says-11580126036>.

As a threshold matter, for-profit businesses should not be put in charge of and in control of the NMS Plans and its data. These facilities, including SIPs and FINRA CAT NMS, house (or will house) information that has commercial value for any for-profit company seeking to maximize profits (as opposed to the SEC with its mission of upholding the public interest and protecting investors). The Commission must do more to eliminate or mitigate the industry's conflicts of interest. To that end, the SEC must reconstitute the governance structure to reduce the industry's and SROs' dominance and increase the SEC's and the public's representation in the governance of NMS Plans, specifically—

- The Commission must alter the charter and corporate identity of the NMS Plans, turning them into a not-for-profit organization, and align their mission to that of the SEC. As currently constituted, NMS Plans are for-profit corporations with no discernable organizational mission. If these facilities are to be used to protect investors and perfect the mechanisms of the securities markets, then their charter must reflect that mission and purpose.
- The not-for-profit then must be led by a Board, the majority of which will be strictly independent directors with impeccable reputations and integrity. The benefits of including independent board members on corporate boards has been extensively studied. Independent board members increase a firm's operating performance,¹⁵ companies with independent board members are more innovative,¹⁶ and, firms with independent board members more effectively hold CEOs and other executives accountable.¹⁷ All firms that issue registered securities in the U.S. (public companies, investment companies, etc.) are required to have some independent board members. Additionally, all quasi-governmental bodies regulating the securities markets have board members that represent the public interest and are independent of the industry they regulate. For example, FINRA, the Municipal Securities Rulemaking Board (MSRB), and the Public Company Accounting Oversight Board (PCAOB) all have majority public, independent board members (in the cases of FINRA and MSRB) and **all** independent board members, in the case of PCAOB. There is no compelling reason why the NMS Plans—responsible for creating and operating mission-critical facilities that can become the most powerful regulatory tool and repository of information in SEC's history—should not have majority independent board members who pursue investor protection and market integrity.

¹⁵ See Knyazeva, Anzhela, Diana Knyazeva, and Ronald W. Masulis. "The supply of corporate directors and board independence." *The Review of Financial Studies* 26, no. 6 (2013): 1561-1605, available at https://www.researchgate.net/profile/Anzhela_Knyazeva/publication/250107467_The_Supply_of_Corporate_Directors_and_Board_Independence/links/02e7e51e95688dff83000000/The-Supply-of-Corporate-Directors-and-Board-Independence.pdf.

¹⁶ See Chen, Chung-Jen, Bou-Wen Lin, Ya-Hui Lin, and Yung-Chang Hsiao. "Ownership structure, independent board members and innovation performance: A contingency perspective." *Journal of Business Research* 69, no. 9 (2016): 3371-3379, available at <https://www.semanticscholar.org/paper/Ownership-structure%2C-independent-board-members-and-Chen-Lin/043a6b0315c70813620e31e7fc280e086a6e12e9>.

¹⁷ See Weisbach, Michael S. "Outside directors and CEO turnover." *Journal of financial Economics* 20 (1988): 431-460, available at <https://www.sciencedirect.com/science/article/abs/pii/0304405X88900530>.

- The chair of the Board must be a person without past, present or future conflicts who is appointed by the SEC in an open, public process. To avoid industry capture of the executive functions of the NMS Plans, including the CAT NMS, and to ensure that the leadership of the Plans are solely focused on advancing the mission of investor protection and market integrity, the Commission should appoint the Chair of the Board through an open and public nominations process. Importantly, the Commission has extensive experience constituting Advisory Committees tasked with assessing complex, highly technical matters of our securities markets. These Advisory Committees invariably have non-industry yet highly capable, knowledgeable and public-interest-oriented individuals. The Commission has all the contacts and experience necessary to select a conflict-free individual as Chair of the Board.
- The Director of the Division of Trading and Markets must serve on the Board as the permanent sole vice-Chair. One of the significant challenges the SEC is facing with the CAT NMS is that it has no direct involvement in decision-making of the CAT NMS. With a permanent seat at the board table, the Commission would be maximally informed of the undertakings, successes, and failures of the CAT NMS, and be in a position to quickly react to such developments. The Division of Trading and Markets has the technical expertise to guide the Board and could offer regulatory user's perspectives that could help make the CAT user-friendly.

CONCLUSION

We hope the Commission finds our comments helpful. In our view, the Commission has proposed critically important reforms that must be enacted quickly. The Commission must do so to better protect investors, promote market integrity through fair play, transparency, and investor empowerment. We urge the Commission to approve the Proposal with the modifications offered above.

Sincerely,

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