Stock Market Data: A Call for Transparency to Assess Impact on U.S. Investors

The Committee on Capital Markets Regulation (the "**Committee**") is concerned that the three dominant U.S. stock exchange groups—BATS, NASDAQ and the NYSE (collectively, the "**U.S. Exchange Groups**")[1]—are charging excessive fees for market data services that are unnecessarily increasing the cost of trading stocks for U.S. investors.

In this statement, we examine the revenues that the U.S. Exchange Groups report from market data services as a proxy for the total cost of these services to broker-dealers and other market participants. We find that collective annual revenues for market data services at U.S. Exchange Groups are significant ($2.3 billion) and have substantially increased in recent years (55% since Q1 2014). Excessive fees for market data services may indeed be a problem.

However, we find that the U.S. Exchange Groups do not provide sufficient disclosures as to the underlying cost of providing market data services to determine whether the fees that they are charging are excessive. Moreover, the U.S. Exchange Groups' revenue disclosures are even more limited regarding three types of critical market data services—securities information processors ("**SIPs**"), proprietary data feeds and connectivity services—where the potential for excessive fees is particularly high as broker-dealers must pay for access to efficiently execute orders on behalf of U.S. investors.

We believe that these critical market data services are sufficiently central to the efficient functioning of U.S. trading markets that the Securities and Exchange Commission (**"SEC"**) should require the U.S. Exchange Groups to disclose their aggregate revenues from the SIPs, proprietary data feeds and connectivity services. Additionally, the SEC should require the U.S. Exchange Groups to disclose the underlying cost of these critical market data services to enable the SEC and the public to determine whether the existing fees for these services are excessive and increasing the cost of trading stocks for U.S. investors.[2]

I. Overall Exchange Revenues from Market Data Services

Our review of the quarterly disclosures by the U.S. Exchange Groups from Q1 2014 through Q1 2018 finds that their collective annual revenues from market data services[3] have

[1] NYSE is owned by Intercontinental Exchange (ICE), and BATS is owned by Chicago Board Options Exchange (CBOE).

[2] We note that SEC Commissioner Robert Jackson recently recommended a more transparent and standardized regime for revenue disclosures by U.S. stock exchanges that is generally consistent with our recommendation. *See* Commissioner Robert J. Jackson Jr., *Unfair Exchange: The State of America's Stock Markets*, George Mason University, Arlington, Virginia (Sept. 19, 2018).

[3] We determined total revenues from "market data services" by adding revenues from any segment involved in the exchanges' market data operations, as indicated in company filings. For ICE, revenues from 'data services' (divided into 'pricing and analytics,' 'exchange data,' and 'desktops and connectivity') were included. However, estimated 'pricing and analytics' revenue from Interactive Data, which ICE acquired in 2015, is excluded, as Interactive Data's business covers a range of data products and services beyond equity market data. For NASDAQ, revenues from 'trade management services' and 'information services' (divided into 'market data products' and 'index licensing and services') were included. For BATS, from 2014 to 2016, revenues from 'market data fees' and 'connectivity fees and other' were included. For CBOE, revenues from 'market data fees' and 'exchange services and other fees' were included.

increased 45% in the three years between 2014 and 2017, from $1.58 billion to $2.3 billion, respectively—and 55.2% quarter-over-quarter growth from Q1 2014 to Q1 2018.[4] **Figure 1** illustrates the relative growth in revenues from market data services for each of the U.S. Exchange Groups. The yellow line in **Figure 1** also shows the average increase in revenue from market data services across all three U.S. Exchange Groups.

Figure 1

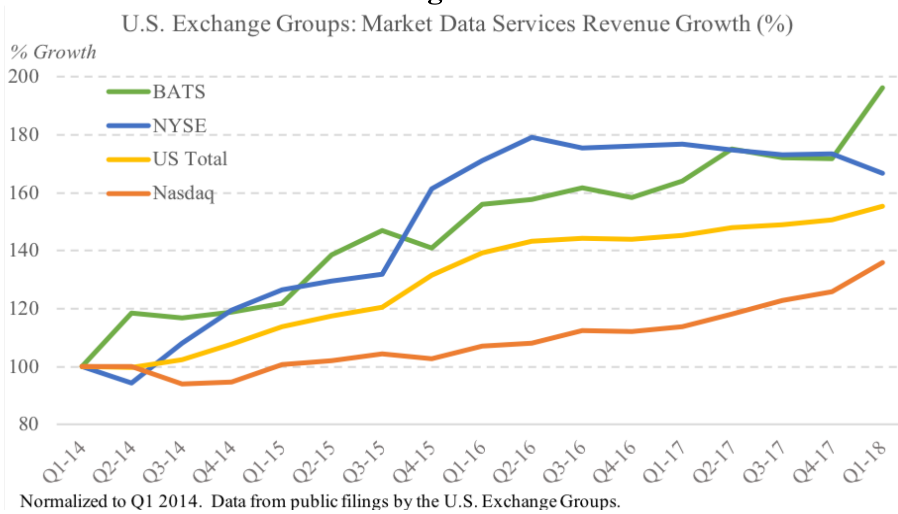
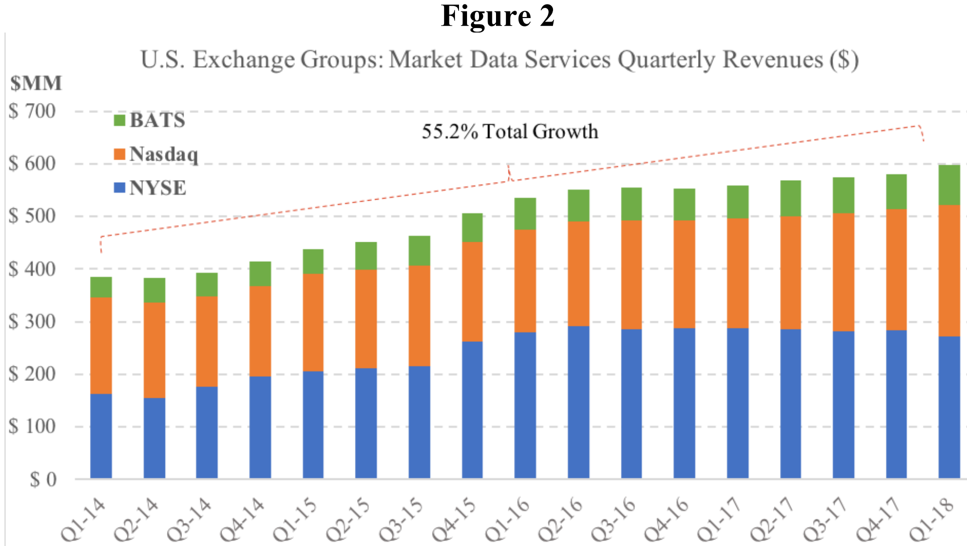


Figure 2 demonstrates the quarterly revenues that each U.S. Exchange Group derives from market data services. In Q1 2018, NYSE earned $266 million from market data services, NASDAQ earned $249 million, and BATS earned $76 million.

Figure 2



[4] ICE data sourced from filings and investor materials at http://ir.theice.com/annual-and-quarterly-reports/quarterly-results. NASDAQ data sourced from filings and materials at http://ir.nasdaq.com/annuals-proxies.cfm. CBOE data sourced from 2017 materials at http://ir.cboe.com/events-and-presentations. BATS data sourced from 10-Q filings for 2016 at https://www.sec.gov/cgi-bin/browse-edgar?action=getcompany&CIK=0001659228, joint prospectus at https://www.sec.gov/Archives/edgar/data/1659228/000104746916017129/a2230469zdefm14a.htm, and 2015 S-1 filing at https://www.sec.gov/Archives/edgar/data/1659228/000104746915009232/a2226675zs-1.htm.

II. Exchange Revenues from Critical Market Data Services

SIPs

The SIPs are governed by the Securities Act Amendments of 1975 and Regulation NMS and serve as the common reference source for equity market activity.[5] SIP data is used to determine the National Best Bid and Offer and other price-based regulations such as the limit up-limit down requirement and short sale restrictions.[6] To comply with these and other regulations, broker-dealers must pay fees to the U.S. Exchange Groups to access the SIPs.

The U.S. Exchange Groups collectively earned $311 million from the SIPs in 2017.[7] However, the U.S. Exchange Groups do not disclose their costs associated with operating the SIPs, so it is impossible to determine whether the collective fees charged by the U.S. Exchange Groups to access the SIPs are excessive.

Proprietary Data Feeds

The U.S. Exchange Groups also charge broker-dealers fees to access so-called proprietary data feeds. Both SIP data and proprietary data are consolidated from raw inputs that market participants are legally required to provide the exchanges. These proprietary data feeds can provide a direct link between an exchange and traders that allows market participants to receive market data substantially faster than through the SIPs.[8] Proprietary data feeds also provide depth of book information that is unavailable from the SIPs, such as the limit-order volume at all bid and offer prices. In practice, broker-dealers purchase access to proprietary data feeds to ensure that they are getting the best prices for investor orders.[9] Many, if not most, trades also require a broader view of liquidity that only proprietary depth-of-book data can provide.[10] However, the U.S. Exchange Groups generally do not disclose their revenues from proprietary data feeds or their costs for providing such services.[11]

[5] *See* Regulation NMS, 70 Fed. Reg. 37503, https://www.sec.gov/rules/final/34-51808.pdf; *CTA Overview*, Consolidated Tape Association, https://www.ctaplan.com/index (last visited May 22 2018).
[6] *CTA Overview*, Consolidated Tape Association, https://www.ctaplan.com/index (last visited May 22 2018).
[7] Charles M. Jones, *Understanding the Market for U.S. Equity Market Data,* (August 31, 2018) Available at: https://www0.gsb.columbia.edu/faculty/cjones/papers/2018.08.31%20US%20Equity%20Market%20Data%20Paper.pdf
[8] Examples of proprietary products include NYSE Integrated Feed, NYSE OpenBook Ultra, and Nasdaq Basic.
[9] *See NetCoalition v SEC*, 615F.3d 525,529-31 (D.C.Cir. 2010).
[10] *Id.* at 530.
[11] However, on occasion exchanges have provided limited revenue disclosures. For example, between Q3 2016 and Q3 2017, NASDAQ reported $101 million in revenue from US equity proprietary depth products. And in Q3 2017 ICE disclosed that NYSE real-time proprietary products constituted less than four per cent of its $620 million data and listings revenues (i.e. approximately $24 million); *see 3Q17 Earnings Supplement* 6, Intercontinental Exchange (Nov 2 2017), http://ir.theice.com/~/media/Files/I/Ice-IR/events-presentations/presentation/3q17-earnings-presentation-v1.pdf.

Connectivity Services

Exchanges also charge fees for faster trade execution services and faster delivery and optimal use of equity market data. So-called "co-location" services allow broker-dealers to rent space for their servers and equipment within an exchange's physical data center, which eliminates delays caused by distance. Broker-dealers must also pay high-bandwidth gate fees and session/port fees, often referred to as connectivity services, to realize the full benefits of proprietary data feeds and execute investor orders efficiently. However, the U.S. Exchange Groups do not disclose their revenues from co-location or connectivity services or their costs for providing such services.

Recommendation

Broker-dealers must pay for access to the SIPs, proprietary data feeds, and certain connectivity services to efficiently execute investor orders. However, the U.S. Exchange Groups do not provide sufficient public disclosures to determine whether the aggregate fees that they charge for these services are excessive. Without this information, neither the SEC nor the public are able to assess whether the existing equity market structure is functioning effectively for U.S. investors. The Committee therefore recommends that the SEC mandate that the U.S. Exchange Groups publicly disclose their revenues from the SIPs, proprietary data feeds, and high-speed connectivity services, as well as the underlying specific cost to the exchanges of providing these services. The SEC and the public will then be able to judge whether the aggregate fees charged for these services are excessive and determine their total impact on U.S. investors' trading costs.

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September 24, 2018