Written Testimony of Marc E. Lackritz
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Financial Services Subcommittee
On Capital Markets, Insurance and Government-Sponsored Enterprises
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Chairman Baker, Chairman Oxley, and distinguished members of the Subcommittee, the Securities Industry Association ("SIA")[1] appreciates this opportunity to share our views on the implications to investors and market transparency of granting ownership rights in stock market information. As you know, for the last several years, SIA member firms, along with regulators, other market participants, and legislators, have been reconsidering the current system of providing securities market information, including the appropriate entities to collect and consolidate the information, the fees charged for the information, and the role of revenue derived from those fees. The issue is complex and the impact on market structure will be significant.

At the same time, as the database industry in the United States continues to grow, efforts are underway to grant new protections to those who collect and compile information, including securities information processors. SIA believes that legislation that would create new property rights in stock market information would seriously undermine the process of consolidating and disseminating stock market information and is contrary to the goals that Congress set out in the Securities Acts Amendments of 1975 ("1975 Act Amendments")[2] to the Securities Exchange Act of 1934 ("the Act").[3] We believe that adequate protections currently exist to address information theft, and to legislate in this area would disrupt the regulatory and contractual regimes that make real-time market information so widely available today.

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[1] The Securities Industry Association brings together the shared interests of nearly 700 securities firms to accomplish common goals. SIA member firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the accounts of nearly 80 million investors directly and indirectly through corporate, thrift, and pension plans. In the year 2000, the industry generated $314 billion of revenue directly in the U.S. economy and an additional $110 billion overseas. Securities firms employ approximately 770,000 individuals in the U.S. (More information about SIA is available on its home page: http://www.sia.com.)

[2] Pub. L. No. 94-29, 89 Stat. 97 (1975).

[3] 15 U.S.C. 78a-78mm.

Background—Importance of Market Information

Securities markets are synonymous with information. Market information, *i.e.*, the quotes at which people are willing to buy and sell stock, and the price of the last sale of a stock, is truly the lifeblood of the market. In order to make informed investment decisions, investors, regardless of whether they are large institutions or individuals, and no matter where they are located or where they are effecting their trades, must know the prevailing market price of a security and the price of the most recent sale in that security. The widespread availability of this information, also known as "transparency," ensures that buyers of securities do not pay more than the lowest price at which someone is willing to sell, or sellers do not sell for less than the highest price at which someone is willing to buy.

Transparency of market information also has facilitated the growth of an entire industry of market data vendors that add analytic information and news services to basic market information and sell it to market participants and others, thus giving individual investors access to much of the same information that previously was available only to market professionals. Unrestricted, easy access to this information has helped make the U.S. capital markets the envy of the world. Our markets are deep, our markets are liquid, and our markets are fair. Transparency is one of the reasons.

The benefits of transparency are not limited to the securities industry. Recent advances in technology and communications have spawned an explosion of information, which has benefited consumers in **all** industries. In the securities industry, retail investors have been the primary beneficiaries of this increased transparency. The advent of the Internet has provided investors with a flood of financial information and quick and easy access to the markets. Individual investors are taking personal control of their investment decisions, and many are effecting transactions without the advice of a broker. But whether they are directing their own investments or using a broker for recommendations, because of the speed and ease with which investors can monitor their investments and execute transactions, the demand for, and value of, market information has never been greater.

The "Information Age," though, has raised concerns about database piracy and the need to protect those who compile information in on-line databases. Copyright law generally will prevent the wholesale copying of an entire database, as long as there is at least a minimal amount of original expression, but does not protect the extraction and reuse of individual facts. Securities market information, *i.e.*, best bid and offer and last sale reports, is no more than a collection of facts derived from various market participants.

Database publishers, including securities information processors, also rely on contracts, common law, and technological measures to prevent the misappropriation and misuse of data that the publisher has compiled. Such measures have always been sufficient until recent actions in Europe created powerful new rights for database publishers. Under the Database Directive (the "Directive") adopted by the European

Union ("EU") in 1996, a second-generation publisher cannot extract or reuse a qualitatively or quantitatively substantial part of a first generation database, even if the second publisher did not extract or reuse any protectable expression. A non-EU publisher can receive reciprocal protection only if the publisher's country of origin affords an equivalent level of protection. Consequently, initiatives have been undertaken to strengthen database protection in the U.S.

We must be careful not to let international initiatives trigger the dismantling of a system that has grown up over the last 30 years in the U.S. securities industry. Any legislation that would create an intellectual property right in securities market information would have huge implications on the system for collecting and disseminating market information that Congress so carefully devised in the 1975 Act Amendments.

Consolidating Securities Market Information—Who Does It and What Protections Do They Need?

Individual quotes and last sale reports have little value in and of themselves. It is the aggregation of this information that produces a National Best Bid and Offer ("NBBO"), which informs investors of the best price at which market participants are willing to trade at a particular point in time. In the early 1970's, when the Securities and Exchange Commission ("SEC") first articulated its goal for a central market system, unrestricted public access to consolidated market information was a key component in that plan.

Prior to the 1975 Act Amendments, market information was not consolidated and was not widely available. In fact, the largest market did not provide public access to its quotes. This lack of transparency is precisely what Congress set out to address in creating a national market system. The primary goal was to consolidate last sale and best bid and offer information in order to facilitate efficient price discovery and best execution of customer orders.

In adopting the 1975 Act Amendments, Congress recognized that competitive forces should play a role in the achievement of the regulatory objectives of the Act and acted to remove barriers to competition. But Congress recognized that competition might not be sufficient to ensure the automated dissemination of consolidated market information and therefore gave the SEC rulemaking authority to regulate securities information systems. Using this authority, the SEC adopted rules under which market participants are required to provide basic market information, *i.e.*, best bid and offer, and last sale information in each security to an exchange or association, which in turn consolidates the information into a single stream for dissemination to market participants and the public. Under SEC rules, the self-regulatory organizations ("SROs") are required to act jointly to disseminate market information. The exchanges and Nasdaq have implemented "Plans" pursuant to these rules, under which the SROs operate facilities to consolidate and disseminate market information, set prices for the information, and share the resulting revenues among Plan participants.

Of course, when the Commission proposed rules to provide for the consolidated reporting of transactions and quotations, there were objections from those who controlled this information. The exchanges relied on a line of Supreme Court cases from the early 1900's to assert proprietary rights in their market information. These so-called "ticker cases" held that the collection of quotations by the exchanges stands like a trade secret and is entitled to the protections of the law. To address these concerns, the Commission provided that SROs and vendors could charge reasonable fees for such information.[4]

Any uncertainty surrounding the ownership of market information was settled in 1991 when the Supreme Court, in *Feist v. Rural Telephone*, 499 U.S. 340 (1991), held that under the copyright clause of the Constitution, copyright protection could extend only to expressive elements in compilations, and that effort without creativity could not convert facts into expression. That decision eliminated the "sweat of the brow doctrine," holding that expenditures of time, effort, and money do not afford copyright protection to a collection of information.

For the last 30 years, though, securities information processors under the Plans established by the SROs,[5] as **exclusive** information processors, have enjoyed broad powers. Although securities information processors are required under Section 11A of the Exchange Act to distribute market information in a fair, reasonable and non-discriminatory manner, those processors are, in effect, the existing securities markets, and these markets have relied on revenues from market information to fund other market operations. In the current debate, some market participants have maintained that market information fees are excessive, largely because they have never been subject to competitive pricing and therefore can be used to subsidize other marketplace operations, such as market regulation and surveillance. Irrespective of this debate, we do not believe that Congress or the courts have ever granted securities information processors exclusive ownership rights to market information and to do so now would be a mistake.

Conferring new property rights could impede the flow of real-time market information because, as single-source monopolies, the markets could charge excessive fees and restrict the downstream use of the information. Because they are SROs subject to SEC oversight this may not seem problematic at this point, but opportunities for abuse could occur. These risks would be exacerbated if these markets operate as for-profit enterprises that will be obligated to shareholders to maximize their earnings. While it is important to protect the markets' joint investment in data technology and infrastructure against persons who would take market information without paying for it, we do not believe the markets today are without protection under the current scheme.

Under SEC rules, broker-dealers are required to submit last sale and best bid and offer information to the market's securities information processor. Under the terms of their agreement with the processor, broker-dealers give up property rights in that

[4] Securities Exchange Act Release No. 9731 (August 14, 1972).

[5] The Consolidated Tape Association is the Plan for exchange-listed securities and Nasdaq/UTP is the Plan for Nasdaq-listed securities.

information which they are required by regulation to provide to the processor. This prevents "tape-racing," which would minimize the value of the information if the broker-dealer were to sell the information to a third party before transmitting it to the consolidator. Vendors, in turn, receive and distribute market information from the processor pursuant to various contract and licensing arrangements.

Of course, it is true that a contract only binds the parties, and databases are susceptible to theft by others who are not parties to the contract. Nevertheless, database publishers have successfully, to date, relied on misappropriation law and technological protections to guard their investment in their databases.

Creating New Property Rights in Market Information Will Harm Investors

The securities industry strongly supports broad dissemination of stock market information. Granting new property rights in market information through database protection legislation, no matter how well intentioned, will vest control of market information into the hands of single-source monopolies in the securities industry, which is the antithesis of broad access to market information that Congress intended in enacting the 1975 Act Amendments. With new proprietary rights in this information, the only constraints on pricing would be the statutory standard that requires fees to be fair, reasonable, and not discriminatory. What is considered fair and reasonable by an exchange might be very different than what is considered fair and reasonable by a market participant that conducts business off of the exchange. If costs are perceived to be excessive, the result is likely to be less information available to investors. Moreover, a whole industry that has grown around adding value to market information, re-packaging it, and selling it to market participants could be at risk. Legislation that would restrict such downstream use of market information would cripple this industry.

Conclusion

Transparency is a basic tenet that has helped make the U.S. securities markets the deepest, most liquid, fairest markets in the world. Widespread distribution of market information promotes public trust and confidence in our markets. Creating new intellectual property rights for consolidators of information would impede rather than enhance investors' access to information.

In fact, bids, offers, and last sale prices are nothing more than facts generated by investors. Alone they have no value but when they are consolidated into a single stream of information, they tell investors what the market for a particular security is at a given point in time. The value of this information is unquestioned. According to the SEC, it generates hundreds of millions of dollars each year. Today, a combination of regulation, contract, and common law ensures that market information is widely accessible to all investors and that compilers of such information are adequately compensated for their efforts. New property rights will almost certainly upset this careful balance.