INVESTMENT INDUSTRY ASSOCIATION OF CANADA

Letter from the President

The Rising Cost of Equity Market Data and What Can Be Done About It?

The Rising Cost of Data

The price of equity market data has been soaring in recent years – with much of the cost ultimately being borne by investors. What specific factors are responsible for the price hikes – and what can be done to ensure fair pricing? The Investment Industry Association has set up an industry working group to address the issue. The working group is composed of representative large and small firms from across the country to review the significant price escalation in equity market data costs in recent years, determine if excessive pricing is at play and bring forward recommendations to the regulators for a fair pricing model.

The working group has engaged Securities Litigation Consulting Group (SLCG) to undertake the needed research and analysis, and propose recommendations for market data pricing. SLCG carried out a similar study on market data pricing for SIFMA in 2008. This study contributed significantly to a U.S. District of Columbia Court ruling that NYSE data pricing for Level 2 (depth of book) data was not subject to competitive forces, with instructions to the SEC to intervene with regulatory oversight (as is the case with Level 1, or "top of book" data in the U.S. today).

Market Share: Bigger or Smaller, the Price Moves in the Same Direction – Up

In the past five years, TSX market data costs alone have risen 27%, with the percentage increase even higher when ATS data costs are included. The Canadian securities industry pays out about $150 million a year for market data. A large share of these costs is passed on to investors. Moreover, information vendors such as Bloomberg and Belzberg that provide market information directly to investors have found similar high and escalating prices for market data.

A further concern is that as the six ATSs build market share, data fees charged by these other marketplaces will continue to escalate. For example, Alpha Trading Systems recently began to charge for data once trading reached a 20% market share. Omega and Pure Trading, with less than a one percent market share, also charge for market data. But while the price escalator moves up as a marketplace builds market share, it doesn't seem to move down that much when a marketplace loses share. Overall TSX data costs have not come down proportionate to the decline in stock exchange market share. While the TSX did recently reduce prices for small market participants (with less than 100 terminals), those reductions have been limited in scope and prices remain high in historical terms.

What's Behind the Data Price Increases?

Secondary equity market trading is concentrated in several equity marketplaces, with the TSX having a dominant market share. This concentration gives the marketplaces considerable leverage, with pricing determined by revenue and rate of return targets rather than market forces. The TSX has the majority trading share of roughly 68%, down from 99% as recently as two years ago. In addition, the individual marketplaces leverage data pricing from regulations that require dealers to obtain real time pricing from all marketplaces to meet best price obligations for their clients. Dealers must purchase data at whatever the cost and execute trades at whatever the transaction fee to meet these regulatory requirements.

What the IIAC is Doing

The objective of the IIAC study is to measure the concentration of trading in secondary equity markets, review and assess marketplace pricing strategies, measure historical pricing trends – particularly relative to the cost of producing the data – draw international comparisons of data pricing, particularly in U.S. markets, and advance remedial solutions. The study will examine specific mechanisms to achieve fair and transparent pricing of market data. The working group will in the course of its work be monitoring the initiatives undertaken by the SEC to regulate market data pricing of the stock exchanges in response to the Court's instructions.

It is anticipated the IIAC study will be completed by the end of October. The IIAC Working Group will keep securities regulators well-briefed on ongoing work. Once this study is completed, the Working Group will discuss its recommendations and proposals with the securities regulators and move forward to achieve its objectives.

Yours sincerely,

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