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FINANCIAL REGULATION

# SEC Commissioner Calls for Regulators to Bolster Market Oversight

In a policy speech, Robert Jackson, a Democratic commissioner at the SEC, alleges the agency "stood on the sidelines" amid investor harm

In a policy speech to be delivered Wednesday, Robert Jackson, shown here on Oct. 24, 2017, will call on the SEC to ensure "that the exchanges' actions do not unduly burden competition and are fair and reasonable."

PHOTO: JOSHUA ROBERTS/REUTERS

*By Gretchen Morgenson*
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A top securities regulator is calling for his agency to beef up its oversight of the nation's stock exchanges to root out conflicts and curb rising fees that he says are harming investors.

In a policy speech to be delivered Wednesday, Robert J. Jackson Jr., a Democratic commissioner at the Securities and Exchange Commission, will allege that the SEC has "stood on the sidelines" as the New York Stock Exchange, Nasdaq Inc. and other market operators have significantly boosted their profits while raising investors' costs, according to a copy of his remarks.

Mr. Jackson will call on the SEC to ensure "that the exchanges' actions do not unduly burden competition and are fair and reasonable."

All of the currently active U.S. stock exchanges are for-profit enterprises, a reversal of the way the stock market operated for nearly two centuries. The NYSE, for instance, was a member-owned nonprofit until 2006 and was later acquired by Intercontinental Exchange Inc., an Atlanta-based global exchange operator. Critics charge that for-profit exchanges exploit their central position in the markets to extract greater fees from traders.

To gain access to the richest and fastest stock-price and trading information, banks and brokerage firms must pay the exchanges to connect to their data feeds. These costs have jumped in recent years, said Mr. Jackson, one of two Democrats on the five-person SEC.

Between 2013 and 2018, for example, connectivity fees more than tripled on the Bats Global Markets exchanges, he said. A spokeswoman for the Cboe Global Markets Inc., which acquired Bats in 2017, said, “Our connectivity offering has been significantly enhanced since the beginning of 2013. Then, a connection, which was offered free, covered two equity markets, and one new options exchange. Today, that same connection provides access to four equity exchanges and three options exchanges, which represent a major share of daily trading activity in those markets.”

Mike Williams, executive director of the Equity Markets Association, which represents both the NYSE and Nasdaq, said, “U.S. exchanges are the most heavily regulated, transparent and trusted participants in our national equity trading infrastructure, and today provide more valuable, efficient and resilient trading and data services, at the lowest relative cost to investors, than at any time in history.”

As a single minority commissioner, Mr. Jackson doesn’t hold great sway on SEC policy at the moment. But his view echoes criticism from some market participants and others about market-data sales.

“It is very important that [stock exchanges] be regulated effectively,” said Ken Bertsch, executive director of the Council of Institutional Investors.

Since technological advances have pushed down the prices of connectivity in other arenas, Mr. Jackson questioned why costs are rising for stock investors. Still, the SEC has approved every fee increase for connectivity to the nation’s exchanges, Mr. Jackson said. In the future, he said, the agency should approve the increases only if the exchanges can justify them.

Mr. Jackson's speech is to be delivered at an event co-sponsored by George Mason University Law & Economics Center in Arlington, Va., and the Healthy Markets Association, an investor-oriented nonprofit.

In it, he also will highlight problems with the current two-tiered system for stock-price data—a slow, relatively cheap public feed and lightning-fast private feeds that traders can access for a steeper fee. Those who pay up for the private feed can trade ahead of investors using the public data, he said, receiving better prices on their trades.

"What does it say to mom-and-pop investors," Mr. Jackson said in an email, "that our stock markets are full of abuses like these?"

A remedy, Mr. Jackson wrote, is to bar exchanges from controlling the public feed while they sell access to private price data. The current setup has incentivized the exchanges to invest heavily in their private—and highly profitable—data feeds while letting the public system languish, he said.

The exchanges say they have invested in the public-data system in the past few years and significantly improved its speed, making it tougher for high-speed traders to exploit differences between the private and public data feeds.

Understanding how for-profit exchanges' practices are affecting investors is crucial for the SEC, Mr. Jackson said.

It is difficult to pinpoint how much the exchanges earn in connectivity and data fees because the companies' financial filings provide varying levels of detail on these revenue sources.

But Eric Budish, professor at the University of Chicago's Booth School of Business, estimates that in 2015 the three major exchange families—Bats, Nasdaq and NYSE—generated at least $675 million from sales of proprietary data products, connectivity and "co-location," which allows traders to co-locate equipment within exchange data centers, giving them faster access to stock trading.

Without the revenues from proprietary data products and connectivity, the exchanges wouldn't be profitable, Mr. Budish said.

"They have market power in the sale of data and connectivity specific to their exchanges," Mr. Budish said in an interview. "This helps explain why the exchanges might be hesitant to innovate in ways that would be good for the market as a whole."

Mr. Jackson also will argue that stock exchanges should no longer have immunity from investors' lawsuits because they also conduct regulatory activities. In 2012, when Nasdaq bungled the Facebook Inc. initial public offering, for example, it fought investor lawsuits by claiming regulatory immunity; Nasdaq later settled the case.

Even when exchanges are held liable for investor mistreatment, Mr. Jackson said, most enjoy an SEC-approved modest cap on liability each year.

**Write to** Gretchen Morgenson at gretchen.morgenson@wsj.com

**Corrections & Amplifications**
An earlier version of this article incorrectly stated Robert Jackson's middle initial and omitted Jr. from his name.