

result, Nasdaq would append the .M modifier and publish it with a trade size of zero to signal to the ESIP and vendors not to include it in the Consolidated Close calculation. The NOCP would, on the other hand, be used to populate the Nasdaq Individual Market Close field that the ESIP currently disseminates. The Predicate Trade would be reported to the ESIP according to Nasdaq's existing trade reporting rules and it would be eligible to set the Consolidated Close, as it would be today.

Nasdaq recognizes that it must educate investors and vendors about its new NOCP and the .M modifier to avoid creating confusion. Currently, the Nasdaq ESIP disseminates a Closing Trade Summary Report that includes the Consolidated Close as well as the Individual Market Closes for Nasdaq and for each UTP Exchange that trades Nasdaq securities. If this proposal is approved, the Individual Market Close field for Nasdaq in the Closing Trade Summary Report would contain the NOCP in place of its last sale price. Neither the Consolidated Close nor any of the Individual Market Closes for any UTP Exchange would be affected by this proposal.

The Nasdaq ESIP is engaged in a development effort to accommodate the new trade modifier and its treatment in the consolidated data streams. Nasdaq has also discussed the addition of the new .M trade modifier with the UTP Operating Committee, and has made it clear that any UTP participant can use the new trade modifier if it chooses.

### III. Summary of Comments and Nasdaq's Responses

As noted above, the Commission received seven comment letters regarding the original proposal.<sup>10</sup> Nasdaq filed Amendment No. 1 to the proposal<sup>11</sup> to respond to the positive comments received by four of the commenters<sup>12</sup> and also filed the Second Response Letter<sup>13</sup> to address further concerns raised by three of the commenters.<sup>14</sup>

#### A. Amendment No. 1

Three of the commenters addressed in Amendment No. 1 fully supported Nasdaq's proposed rule change.<sup>15</sup> One commenter believed that the institution

of an official closing price for the Nasdaq market would greatly enhance the overall integrity of the market and that the proposed methodology for calculating the NOCP appeared sensible and reasonably impervious to manipulation.<sup>16</sup> Another commenter stated that the implementation of Nasdaq's proposal would result in the determination of closing values that accurately and consistently reflect market conditions at the close and is an improvement that would provide greater financial market transparency.<sup>17</sup> The third commenter believed that the proposal would provide tremendous benefits to the marketplace and improve stability and predictability across the Nasdaq market and enthusiastically supported each of the three components of the proposal: (1) Reducing the consideration time for inclusion in the closing price from 4:01:30 to 4:00:02 p.m.; (2) restricting the closing price to trades effected on Nasdaq; and (3) "normalizing" closing prices based upon the closing inside market.<sup>18</sup>

Furthermore, under the proposal, Nasdaq would adjust the NOCP only if the Predicate Trade is cancelled or corrected by 4:30:00 p.m., even though Nasdaq would continue to accept trade cancel and correction messages via its ACT until 5:15:00 p.m. Although supporting the proposed rule change, one commenter questioned Nasdaq's willingness to accept trade cancel and correction messages via ACT until 5:15:00 p.m., inasmuch as this would result in a disconnect between the NOCP and ACT.<sup>19</sup> While Nasdaq asserted that it receives over 99 percent of cancel or corrections before 4:30:00 p.m., this commenter believed that material changes consistently occur after 4:30:00 p.m. The commenter also believed that a failure to synchronize these two events would very likely result in mutual funds being compelled to disregard the NOCP at 4:30:00 p.m.<sup>20</sup> Similarly, another commenter indicated that the 4:30:00 p.m. deadline would be 45 minutes prior to the time that other markets continue to accept

adjustments.<sup>21</sup> In response to comments, Nasdaq revised its proposal in Amendment No. 1 to extend the calculation of the NOCP to 5:15:00 p.m.<sup>22</sup> Nasdaq believed that the 5:15:00 p.m. cut-off would permit flexibility to review and correct trades that occur during the busiest trading of the day, while fulfilling the equally important need for finality in the closing price calculation.

#### B. Second Response Letter

As noted above, the Commission received three comment letters that raised procedural, competitive, and methodological concerns with respect to the proposed rule change.<sup>23</sup> Nasdaq filed the Second Response Letter to specifically address these comments.<sup>24</sup>

##### 1. Procedural Issues

Because Nasdaq would be replacing the Nasdaq UTP Plan's methodology in calculating its close with the NOCP methodology, proposing that the Predicate Trade be "normalized," and introducing new cut off times for calculating its individual close and disseminating that info through the ESIP facilities and thus changing the closing reports disseminated by the ESIP to display the NOCP instead of the Nasdaq UTP Plan's standard calculation, three of the commenters believed that Nasdaq should not be permitted to bypass the UTP Operating Committee or the terms of the Nasdaq UTP Plan, but instead should seek UTP Operating Committee interpretation or Nasdaq UTP Plan amendment to accommodate the NOCP.<sup>25</sup> The commenters also criticized Nasdaq for not involving other interested Nasdaq UTP Plan participants in developing the specifications for the SIP system changes before starting development work<sup>26</sup> and that Nasdaq designed the .M modifier accommodated by the ESIP in a fashion that is suited to its own particular system needs.<sup>27</sup> Furthermore, one of the commenters questioned Nasdaq's stated purpose for proposing the rule change, stating that if Nasdaq had a legitimate concern about the methodology specified in the Nasdaq UTP Plan for calculating the consolidated close, the appropriate forum to address that issue would be the UTP Operating

<sup>10</sup> See UBSW Letter, *supra* note 4.

<sup>11</sup> See S&P Letter, *supra* note 4.

<sup>12</sup> See SSB Letter, *supra* note 4.

<sup>13</sup> See Institute Letter, *supra* note 4.

<sup>20</sup> This commenter also suggested that the deadline for cancel and correction messages for both the NOCP and for ACT be set at 5:00:00 p.m. rather than 5:15:00 to provide mutual funds an additional 15 minutes to calculate daily closing prices. See Institute Letter, *supra* note 4. In response, Nasdaq stated that, while it cannot implement that recommendation via this proposal, it understands the logic of the commenter's recommendation and commits to continue discussions on this proposal with the commenter and with Nasdaq's membership. See Amendment No. 1, *supra* note 5.

<sup>21</sup> See CSE Letter, *supra* note 4.

<sup>22</sup> See Amendment No. 1, *supra* note 5.

<sup>23</sup> See Amex Letter, CSE Letter and Instinet Letter, *supra* note 4.

<sup>24</sup> See Second Response Letter, *supra* note 6.

<sup>25</sup> See Amex Letter, CSE Letter and Instinet Letter, *supra* note 4.

<sup>26</sup> See Amex Letter and CSE Letter, *supra* note 4.

<sup>27</sup> See CSE Letter and Instinet Letter, *supra* note 4.

<sup>10</sup> See *supra* note 4.

<sup>11</sup> See Amendment No. 1, *supra* note 5.

<sup>12</sup> See Institute Letter, SSB Letter, S&P Letter and UBSW Letter, *supra* note 4.

<sup>13</sup> See Second Response Letter, *supra* note 6.

<sup>14</sup> See Amex Letter, CSE Letter and Instinet Letter, *supra* note 4.

<sup>15</sup> See SSB Letter, S&P Letter and UBSW Letter, *supra* note 4.