

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-73399; File No. SR-NASDAQ-2014-081)

October 21, 2014

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Order Approving a Proposed Rule Change Related to Proposed Changes to NASDAQ Rule 4120(c) to Modify the Parameters for Releasing Securities for Trading upon the Termination of a Trading Halt in a Security That Is the Subject of an Initial Public Offering

I. Introduction

On August 20, 2014, The NASDAQ Stock Market LLC (“NASDAQ” or the “Exchange”) filed with the Securities and Exchange Commission (the “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change relating to its initial public offering (“IPO”) process. The proposed rule change was published for comment in the Federal Register on September 9, 2014.³ The Commission received no comments on the proposal. This order approves the proposed rule change.

II. Description of the Proposal

The Exchange proposes to amend NASDAQ Rule 4120(c) to modify the parameters for releasing securities for trading upon the termination of a trading halt in a security that is the subject of an IPO (the “IPO Halt Cross” or the “Cross”).⁴ Currently, NASDAQ Rule 4120(c)(7)(B) governs the launch of trading of IPO securities approved for listing on the Exchange.⁵ NASDAQ Rule 4120(c)(7)(B) provides a two-phase process in which there is a 15

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 72961 (September 3, 2014), 79 FR 53500 (“Notice”).

⁴ See id.

⁵ See Securities Exchange Act Release No. 69897 (July 1, 2013), 78 FR 40782, 40783 (July 8, 2013).

minute Display Only Period in which market participants may enter quotes and orders in that IPO security in the NASDAQ systems, which is then followed by a “Pre-Launch Period” that is not of a fixed duration.⁶ According to the Exchange, the Pre-Launch Period continues until: (1) NASDAQ receives notice from the underwriter of the IPO that the security is ready to trade and there is no “order imbalance”⁷ in the security, in which case the security is released for trading; or (2) the underwriter, with concurrence of NASDAQ, determines to postpone and reschedule the IPO. The Exchange states that it disseminates the “Current Reference Price,” which is an indication of the price at which the IPO Halt Cross would execute if it occurred at that time, every five seconds during the Display Only Period and the Pre-Launch Period.⁸

The Exchange proposes to replace its current process with a procedure under which the “Expected Price”⁹ of the IPO Halt Cross will be displayed to the underwriter, who will then select price bands to ensure that the actual calculated price at which the IPO Halt Cross would occur does not deviate from the Expected Price by more than the selected amounts.¹⁰ According

⁶ See Notice, supra note 3, at 53501.

⁷ See id.

⁸ See id. According to the Exchange, under the current rule, an “order imbalance” in an IPO security exists if: (1) the Current Reference Price disseminated immediately prior to commencing the release of the IPO for trading during the Pre-Launch Period and any of the three preceding Current Reference Prices differ by more than the greater of 5 percent or 50 cents; (2) upon completion of the Cross calculation, the calculated price at which the security would be released for trading and any of the three preceding Current Reference Prices disseminated immediately prior to the initiation of the Cross calculation differ by more than the greater of 5 percent or 50 cents; or (3) all market orders will not be executed in the Cross. See id.; and NASDAQ Rule 4120(c)(7)(C).

⁹ The “Expected Price,” according to the Exchange, is the Current Reference Price displayed to the underwriter after the Exchange receives notice from the underwriter that the security is ready to trade. See Notice, supra note 3, at 53501, and Proposed NASDAQ Rule 4120(c)(8)(A)(i).

¹⁰ See Notice, supra note 3, at 53501. The Exchange is also proposing to reorganize certain provisions of NASDAQ Rule 4120 relating to the process for ending a trading halt of

to the Exchange, price deviations between the Expected Price and the actual calculated price of the Cross can occur because market participants may continue to enter and cancel orders during the period between the display of the Expected Price to the underwriter and the commencement of the Cross calculation, a period of up to five seconds in duration.¹¹

Under the proposal, the process for determining the end of the Pre-Launch Period and when the IPO security will be released for trading will be as follows: (1) NASDAQ receives notice from the underwriter of the IPO that the security is ready to trade; (2) the NASDAQ system will then calculate the Current Reference Price and display it to the underwriter (i.e., the Expected Price); (3) the underwriter agrees to go forward; (4) the NASDAQ system determines that all market orders will be executed in the cross; and (5) the NASDAQ system determines that the security satisfies a “price validation test,” as described below.¹²

Under the proposal, prior to the conclusion of the Pre-Launch Period,¹³ the underwriter will select price bands¹⁴ and, as noted above, the system will then compare the Expected Price with the actual price calculated by the Cross.¹⁵ If the actual price calculated by the Cross differs from the Expected Price by an amount in excess of the price band selected by the underwriter,

securities other than IPO securities, but is not making substantive modifications to these rules. See id.

¹¹ See id.

¹² See id.

¹³ The underwriter can select the price bands at any time during the Display Only Period or the Pre-Launch Period, and may modify them at any time prior to the Pre-Launch Period. See id. at n.6.

¹⁴ Specifically, the underwriter will select an upper price band (i.e., an amount by which the actual price may not exceed the Expected Price) and a lower price band (i.e., an amount by which the actual price may not be lower than the Expected Price). The Exchange notes that the underwriter may select different price bands above and below the Expected Price. See id.

¹⁵ See Notice, supra note 3, at 53501.

the security will not be released for trading and the Pre-Launch Period will continue.¹⁶ Under the proposal, if a security does not satisfy the price validation test, the underwriter may, but is not required to, select different price bands before recommencing the process to release the security for trading.¹⁷

According to the proposal, the available price bands the underwriter may select for the price validation test will include increments and price points established by the Exchange, which may be modified by the Exchange from time to time.¹⁸ Under the proposal, the initial available price bands will range from \$0 to \$0.50, with increments of \$0.01.¹⁹ Under the proposal, the Exchange reserves the right to stipulate wider increments (such as \$0.05) or price bands that include certain price points, but exclude others (for example, increments of \$0.01 up to \$0.10, and increments of \$0.05 thereafter).²⁰

III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.²¹ In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,²² which requires, among other things, that the rules of

¹⁶ See id.

¹⁷ See id. at 53502.

¹⁸ See id.

¹⁹ See id. Under the proposal, an underwriter may select a price band of \$0.00 (i.e., no change from the Expected Price would be permitted). See id.

²⁰ See Notice, supra note 3, at 53502. The Exchange states that it will notify member organizations and the public of changes in available price band or increments through a notice that is widely disseminated at least one week in advance of the change. See id.

²¹ In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

²² 15 U.S.C. 78f(b)(5).

a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

As noted above, the proposal is designed to offer an additional safeguard against an unexpected deviation between the Expected Price and the actual price of the Cross by providing the underwriter with the authority to set price bands based on the characteristics of and expectations for each IPO. The Exchange represents that such price deviations can occur because market participants may continue to enter and cancel orders during the period of up to five seconds between the display of the Expected Price to the underwriter and the commencement of the Cross calculation.²³ The Commission notes that, if the actual price calculated by the Cross differs from the Expected Price by an amount in excess of the price band selected by the underwriter, the security will not be released for trading and the Pre-Launch Period will continue.²⁴ The Commission believes that the proposed rule change is designed to protect investors and the public interest by limiting unexpected volatility in the pricing of an IPO security at the conclusion of the Pre-Launch Period.

²³ See supra note 11 and accompanying text.

²⁴ See supra note 16 and accompanying text.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,²⁵ that the proposed rule change (SR-NASDAQ-2014-081) is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁶

Kevin M. O'Neill
Deputy Secretary

²⁵ 15 U.S.C. 78s(b)(2).

²⁶ 17 CFR 200.30-3(a)(12).