

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-49818; File No. SR-PCX-2004-39)

June 4, 2004

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the Pacific Exchange, Inc. to Extend a Pilot Program under Which it Lists Options on Selected Stocks Trading Below \$20 at One-Point Intervals until August 4, 2004

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on June 3, 2004, the Pacific Exchange, Inc. (“PCX” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by PCX. PCX filed Amendment No. 1 the proposal on June 4, 2004.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

PCX proposes to extend its pilot program under which it lists options on selected stocks trading below \$20 at \$1 strike price intervals (“\$1 Pilot Program”) until August 4, 2004. The text of the proposed rule change is available at the Office of the Secretary, PCX, and the Commission.

---

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, PCX included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. PCX has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of this proposal is to extend PCX's \$1 Pilot Program until August 4, 2004. The current \$1 Pilot Program expires on June 5, 2004. PCX states that its member firms have expressed a continued interest in listing additional strike prices on low priced stocks so that they can provide their customers with greater flexibility in their investment choices. For this reason, PCX proposes to extend the \$1 Pilot Program. PCX notes that all of the issues eligible to be included in the \$1 Pilot Program the procedures for adding \$1 strike intervals, the procedures for phasing out \$2.50 strike price intervals, the prohibition against listing long-term options (also known as "LEAPS") in equity option classes at \$1 strike price intervals, the procedures for

---

<sup>3</sup> See letter from Steven B. Matlin, Senior Attorney, Regulatory Policy, PCX, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission, dated June 3, 2004 ("Amendment No. 1"). In Amendment No. 1, PCX replaced in its entirety the proposed rule text it attached as Exhibit A to its initial Form 19b-4.

adding expiration months and the procedures for deleting \$1 strike intervals will all remain the same.<sup>4</sup>

## 2. Statutory Basis

PCX believes that the continuation of \$1 strike prices will stimulate customer interest in options overlying lower-priced stocks by creating greater trading opportunities and flexibility. The Exchange further believes that continuation \$1 strike prices will provide customers with the ability to more closely tailor investment strategies to the precise movement of the underlying security. For these reasons, PCX believes the proposed rule change is consistent with the Act and the rules and regulations thereunder and, in particular, the requirements of section 6(b) of the Act.<sup>5</sup> Specifically, PCX believes the proposed rule change is consistent with the requirements under Section 6(b)(5)<sup>6</sup> that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts, to remove impediments to and

---

<sup>4</sup> The Commission approved the \$1 Pilot Program on June 17, 2003. See Securities Exchange Act Release No. 48045 (June 17, 2003); 68 FR 37549 (June 24, 2003) (“Pilot Program Approval Order”). Consistent with the Pilot Program Approval Order, PCX represents that it will file a report with the Commission which shall include: (1) data and written analysis on the open interest and trading volume for options (at all strike intervals) selected for the \$1 Pilot Program; (2) delisted option series (for all strike price intervals) selected for the \$1 Pilot Program; (3) an assessment of the appropriateness of the \$1 strike price intervals for the options the PCX selected for the Pilot Program; (4) an assessment of the impact of the Pilot Program on the capacity of the PCX’s, OPRA’s, and vendors’ automated systems; (5) any capacity problems or other problems that arose during the operation of the Pilot Program and how the PCX addressed them; (6) any complaints that the PCX received during the operation of the \$1 Pilot Program and how the PCX addressed them; and (7) any additional information that would help assess the operation of the \$1 Pilot Program.

<sup>5</sup> 15 U.S.C. 78f(b).

<sup>6</sup> 15 U.S.C. 78(f)(b)(5).

perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

B. Self-Regulatory Organization's Statement on Burden on Competition

PCX does not believe that the proposed rule change, as amended, will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

PCX has not solicited, and does not intend to solicit, comments on this proposed rule change. PCX has not received any unsolicited written comments from its members or other interested persons.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>7</sup> and subparagraph (f)(6) of Rule 19b-4<sup>8</sup> thereunder because it does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate; and PCX has given the Commission written notice of its intention to file the proposed rule change at least five business days prior to filing. At any time within 60 days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in

---

<sup>7</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>8</sup> 17 CFR 240.19b-4(f)(6).

furtherance of the purposes of the Act.<sup>9</sup>

Under Rule 19b-4(f)(6)(iii) of the Act,<sup>10</sup> the proposal does not become operative for 30 days after the date of its filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest and PCX is required to give the Commission written notice of its intention to file the proposed rule change at least five business days prior to filing. PCX has requested that the Commission waive 30-day operative delay so that the \$1 Pilot Program may continue without interruption after it would have otherwise expired on June 5, 2004. For this reason, the Commission, consistent with the protection of investors and the public interest, has determined to waive the 30-day operative delay,<sup>11</sup> and, therefore, the proposal is effective and operative upon filing with the Commission.<sup>12</sup>

---

<sup>9</sup> For purposes of calculating the 60-day abrogation date, the Commission considers the 60-day period to have commenced on June 4, 2004, the date PCX filed Amendment No. 1.

<sup>10</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>11</sup> For purposes only of waiving the 30-day operative delay for this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>12</sup> In its Pilot Program Approval Order, the Commission stated that if PCX proposed to (1) extend the \$1 Pilot Program beyond June 5, 2004; (2) expand the number of options eligible for inclusion in the \$1 Pilot Program; or (3) seek permanent approval of the \$1 Pilot Program, the PCX would be required to submit a Pilot Program Report to the Commission along with the filing of such proposal. The Pilot Program Approval Order required the PCX to submit a proposed rule change with the Pilot Program Report at least 60 days prior to the expiration of the \$1 Pilot Program. Because PCX has failed to provide a Pilot Program Report to the Commission containing the analysis and assessment required by the Pilot Program Approval Order, the Commission is extending PCX \$1 Pilot Program only until August 4, 2004.

If PCX proposes to (1) extend the \$1 Pilot Program beyond August 4, 2004; (2) expand the number of options eligible for inclusion in the \$1 Pilot Program; or (3) seek

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-PCX-2004-39 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

All submissions should refer to File Number SR-PCX-2004-39. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your

---

permanent approval of the \$1 Pilot Program, it must submit a Pilot Program Report to the Commission along with the filing of such proposal by July 6, 2005. The Pilot Program Report must cover the entire time the \$1 Pilot Program was in effect, and must include: (1) data and written analysis on the open interest and trading volume for options (at all strike price intervals) selected for the \$1 Pilot Program; (2) delisted options series (for all strike price intervals) for all options selected for the Pilot Program; (3) an assessment of the appropriateness of \$1 strike price intervals for the options the PCX selected for the \$1 Pilot Program; (4) an assessment of the impact of the \$1 Pilot Program on the capacity of the PCX's, OPRA's, and vendors' automated systems; (5) any capacity problems or other problems that arose during the operation of the \$1 Pilot Program and how the PCX addressed them; (6) any complaints that the PCX received during the operation of the \$1 Pilot Program and how the PCX addressed them; and (7) any additional information that would help to assess the operation of the \$1 Pilot Program. The Commission notes that the submission of a satisfactory Pilot Program Report along with a proposed rule change to extend, expand, or permanently approve the \$1 Pilot Program by July 6, 2004 is a condition precedent to the future operation of PCX's \$1 Pilot Program.

comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of PCX. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-PCX-2004-39 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

Margaret H. McFarland  
Deputy Secretary

---

<sup>13</sup> 17 CFR 200.30-3(a)(12).