

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-50108; File No. SR-PCX-2004-66)

July 28, 2004

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change and Amendment No. 1 Thereto by the Pacific Exchange, Inc. to Implement Price Collars on its Archipelago Exchange Facility during the Closing Auction

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on July 13, 2004, the Pacific Exchange, Inc. (“PCX” or “Exchange”) filed with the Securities and Exchange Commission (“Commission” or “SEC”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by PCX. On July 27, 2004, the PCX filed Amendment No. 1 to the proposed rule change.³ The proposed rule change, as amended, has been filed by PCX under Rule 19b-4(f)(6) under the Act.⁴ The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Letter from Mai Shiver, Director and Senior Counsel, Regulatory Policy, PCX to Alton Harvey, Assistant Director, Division of Market Regulation, Commission, dated July 22, 2004. (“Amendment No. 1”). In Amendment No. 1, the PCX explained that in certain instances where the Closing Auction is priced at the midpoint of the NBBO, and where the price collars would otherwise be invoked, the Closing Auction would be priced at the midpoint of the NBBO.

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

The PCX, through its wholly owned subsidiary PCX Equities, Inc. (“PCXE”), proposes to amend its Closing Auction rules to implement price collars in order to improve the Closing Auction pricing mechanism on the Archipelago Exchange facility (“ArcaEx”). Under the proposed rule change, in certain instances, the Closing Auction price would be limited by pre-established thresholds.

Proposed new language is italicized; deleted language is in [brackets].

* * * * *

PCX Equities, Inc.

Rule 7

Auctions

Rule 7.35 (a) – (e)(3)(B)- (No change).

(C) If the Closing Auction Price established by subsections 7.35(e)(3)(A)-(B) is outside the benchmarks established by the Corporation by a threshold amount, the Closing Auction Price will occur at a price within the threshold amounts that best satisfies the conditions of subsections 7.35(e)(3)(A)-(B). The Corporation shall set and modify such benchmarks and thresholds from time to time upon prior notice to ETP Holders.

⁴ 17 CFR 240.19b-4(f)(6). For purposes of determining the effective date and calculating the sixty-day period within which the Commission may summarily abrogate the proposed rule change under Section 19(b)(3)(C) of the Act, the Commission considers that period to commence on July 27, 2004, the date PCX filed Amendment No. 1. See 15 U.S.C. 78s(b)(3)(C).

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

In its filing with the Commission, the Exchange 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. The 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

As part of its continuing efforts to enhance participation on ArcaEx, the PCX is proposing to improve the process associated with pricing the Closing Auction. The proposal is based on a similar standard currently in place at the Nasdaq Stock Market, Inc. ("Nasdaq") for the Nasdaq Closing Cross which was previously approved by the Commission.⁵

Currently, PCXE Rule 7.35 describes the ArcaEx Closing Auction rules. The Closing Auction price is generally determined based on the Indicative Match Price⁶ that is the price at which the maximum volume of shares is executable. To improve the pricing mechanism, ArcaEx proposes to implement price collars that would limit the

⁵ See Securities and Exchange Act Release No. 49406 (March 11, 2004), 69 FR 12879 (March 18, 2004) (SR-NASD-2003-173).

price at which the Indicative Match Price could be set. These price collars would be established by PCX and would be communicated to ETP Holders via the ArcaEx website. Initially, these price collar thresholds would be consistent with the PCXE Demonstrable Erroneous Execution Policy.⁷ That is, the Indicative Match Price would not be permitted to be greater than \$1.00 or 10% away from the consolidated last sale price. Other than utilizing the pre-established price collars to limit the Closing Auction Indicative Match Price and changing the threshold parameters with prior written notice to ETP Holders, the Corporation would not have any discretion to modify the auction process and the calculation of the Indicative Match Price.

Following is an example of how the Closing Auction price collars would function:

Consolidated last sale price: 12.00

ArcaEx Orders:

Buy 50,000 MOC

Sell 30,000 LOC @ 12.50

Sell 20,000 LOC @ 13.01

⁶ See PCXE Rule 1.1(r).

⁷ See Archipelago Exchange Web site www.arcaex.com, Orders and Trade Processing, Erroneous Execution Policy. Any changes to the thresholds of the price collars will be communicated to ETP Holders with reasonable notice prior to the closing auction.

Closing Auction results: Indicative Match Price = 12.50; Matched Volume = 30,000; Total Imbalance = 20,000. The 20,000 limit sell order at 13.01 is outside of the price collar and would not be used to determine the Indicative Match Price.

PCX believes that implementing these price collars would help ensure that the ArcaEx Closing Auction will execute at prices within range of where the stock is currently trading. Further, it would provide ETP Holders and investors with greater price certainty when entering orders into the ArcaEx Closing Auction.

In Amendment No. 1, the Exchange sought to clarify a particular scenario with respect to the collars. Specifically, in certain instances, it may not be appropriate for PCX to institute a price collar. For example, pursuant to PCXE Rule 7.35(e)(3)(B), there may be cases in which the Closing Auction is priced at the midpoint of the NBBO. The NBBO is a fair representation of then-available prices and accordingly provides for an appropriate auction pricing mechanism. In such instances, when the price collars proposed in the instant filing would otherwise be invoked (i.e. the Closing Auction price established by the midpoint of the NBBO is greater than \$1.00 or 10% away from the consolidated last sale price), it would not be appropriate for PCX to utilize such collars and as such, the Closing Auction would be priced at the midpoint of the NBBO.⁸

2. Statutory Basis

The Exchange believes that the proposal is consistent with Section 6(b) of the

⁸ See Amendment No. 1, supra note 3.

Act,⁹ in general, and Section 6(b)(5) of the Act,¹⁰ in particular, in that it will promote just and equitable principles of trade, facilitate transactions in securities, remove impediments to and perfect the mechanisms of a free and open market and national market system, and protect investors and the public interest.

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

The Exchange does not believe that the proposed rule change, as amended, will impose any burden on competition that is 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

Written comments on the proposed rule change were neither solicited nor received.

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

The foregoing rule change, as amended, has been filed by the Exchange pursuant to Section 19(b)(3)(A) of the Act¹¹ and subparagraph (f)(6) of Rule 19b-4 thereunder.¹² PCX has designated the proposed rule change as one that: (i) does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; and (iii) does not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate. Therefore, the

⁹ 15 U.S.C. 78f(b).

¹⁰ 15 U.S.C. 78f(b)(5).

¹¹ 15 U.S.C. 78s(b)(3)(A).

¹² 17 CFR 240.19b-4(f)(6).

foregoing rule change, as amended, has become effective pursuant to Section 19(b)(3)(A) of the Act¹³ and Rule 19b-4(f)(6) thereunder.¹⁴ At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate the rule change if it appears to the Commission that the action is necessary or appropriate in the public interest, for the protection of investors, or would otherwise further the purposes of the Act.

Pursuant to Rule 19b-4(f)(6)(iii) under the Act,¹⁵ the proposal may 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 the self-regulatory organization must file notice of its intent to file the proposed rule change at least five business days beforehand. PCX, through its facility, ArcaEx, provided the Commission with notice of its intent to file the proposed rule change at least five days before filing the proposal with the Commission.¹⁶ The Exchange has requested that the Commission waive the 30-day operative delay so that the proposed rule change will become immediately effective upon filing.

The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest. The Commission believes that accelerating the operative date does not raise any new regulatory issues, significantly

¹³ See supra note 11.

¹⁴ See supra note 12.

¹⁵ 17 CFR 240.19b-4(f)(6)(iii).

¹⁶ See email from Janet Angstadt, Deputy General Counsel, Archipelago Holdings L.L.C. to Alton Harvey, Assistant Director, Commission, dated June 30, 2004.

affect the protection of investors or the public interest, or impose any significant burden on competition. The Commission notes that it recently approved a similar proposal by Nasdaq on which the Exchange's proposal is based.¹⁷ For these reasons, the Commission designates the proposed rule change as effective and operative immediately.

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. Please include File Number SR-PCX-2004-66 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-2004-66. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your 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

¹⁷ See supra note 5.

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 Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of the 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-2004-66 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.¹⁸

Margaret H. McFarland
Deputy Secretary

¹⁸ 17 CFR 200.30-3(a)(12).