

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-51051; File No. SR-PCX-2004-58)

January 18, 2005

Self-Regulatory Organizations; the Pacific Exchange, Inc.; Order Approving Proposed Rule Change and Amendment No. 2 Thereto by the Pacific Exchange, Inc. Relating to the Exchange's Rules Under its Minor Rule Plan and Recommended Fine Schedule

On December 2, 2004, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission ("Commission"), 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> a proposed rule change to amend PCX Rule 10.12 to add new provisions (h)(45) and (k)(i)45. These provisions amend the PCX Minor Rule Plan ("MRP") and Recommended Fine Schedule ("RFS") to add the failure to maintain adequate procedures and controls to monitor and supervise the entry of electronic orders by Users<sup>3</sup> to prevent the prohibited practices set forth in PCX Rules 6.87(d) and 6.90(e).<sup>4</sup> The proposed rule change was published for comment in the Federal Register on December 17, 2004.<sup>5</sup> On January 3, 2005, PCX filed Amendment No. 1 to the proposal. On January 4, 2005, PCX withdrew Amendment No. 1 and filed Amendment No. 2 to the proposal.<sup>6</sup> The

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

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

<sup>3</sup> Pursuant to PCX Rule 6.87(a)(2), "User" means any person or firm that obtains electronic access to Auto-Ex (defined in PCX Rule 6.87(a)(1)) through an Order Entry Firm (defined in PCX Rule 6.87(a)(3)). Pursuant to PCX Rule 6.90(c)(1), "User" means any person or broker-dealer that obtains electronic access to PCX Plus (defined in PCX Rule 6.90(a)) through an Order Entry Firm (defined in PCX Rule 6.90(c)(2)).

<sup>4</sup> PCX Rules 6.87(c)(4) and 6.90(d)(3) require Order Entry Firms to maintain such controls and procedures.

<sup>5</sup> See Securities Exchange Act Release No. 50830 (December 9, 2004), 69 FR 75581 (December 17, 2004) ("Notice").

<sup>6</sup> In Amendment No. 2, PCX proposes to correct a typographical error in the proposed rule text by changing footnote 1 to tie to PCX Rule 10.12(k)(i) instead of to PCX Rule

Commission received no comments on the proposal. This order approves the proposed rule change, as amended.

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,<sup>7</sup> and, in particular, the requirements of Section 6(b)(5) of the Act,<sup>8</sup> in that it is designed to promote just and equitable principles of trade, facilitate transactions in securities, 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. The Commission also finds that the proposal is consistent with Section 6(b)(6) of the Act,<sup>9</sup> which requires that members and persons associated with members be appropriately disciplined for violations of Exchange rules, and Section 6(b)(7) of the Act,<sup>10</sup> which requires that members and persons associated with members are provided a fair procedures for disciplinary procedure.

In approving this proposal, the Commission in no way minimizes the importance of compliance with these rules, and all other rules subject to the imposition of fines under the MRP. The Commission believes that the violation of any self-regulatory organization's rules, as well as Commission rules, is a serious matter. However, in an effort to provide the Exchange with greater flexibility in addressing certain violations, the MRP provides a reasonable means to

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10.12(k). Amendment No. 2 is a technical amendment, and, therefore, not subject to notice and comment.

<sup>7</sup> In approving this proposed rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>8</sup> 15 U.S.C. 78f(b)(5).

<sup>9</sup> 15 U.S.C. 78f(b)(6).

<sup>10</sup> 15 U.S.C. 78f(b)(7).

address rule violations that do not rise to the level of requiring formal disciplinary proceedings. The Commission notes, however, that after the first failure by an Order Entry Firm to maintain adequate controls and procedures to monitor and supervise the entry of electronic orders pursuant to PCX Rules 6.87(c)(4) and 6.90(d)(3), the Exchange will treat subsequent violations as a formal disciplinary matter.<sup>11</sup> The Commission expects that the Exchange will continue to conduct surveillance with due diligence, and make a determination based on its findings as to whether fines of more or less than the recommended amount are appropriate for violations of rules under the MRP on a case-by-case basis, or if a violation requires formal disciplinary action.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act<sup>12</sup>, that the proposed rule change, including Amendment No.2 thereto (File No. SR-PCX-2004-58) be, and it hereby is, approved.

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

Margaret H. McFarland  
Deputy Secretary

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<sup>11</sup> See proposed PCX Rule 10.12(k)(i)45. See also Notice, *supra* note 5.

<sup>12</sup> 15 U.S.C. 78s(b)(2).

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