

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-53096; File No. SR-PCX-2005-141)

January 11, 2006

Self-Regulatory Organizations; Pacific Exchange, Inc.; Notice of Filing of Proposed Rule Change Relating to Modifications to Archipelago Exchange's 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 December 21, 2005, the Pacific Exchange, Inc. ("PCX" or "Exchange"), through its wholly owned subsidiary ("PCXE" or the "Corporation"), filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II and III below, which Items have been prepared by PCX. The Commission is publishing this notice to solicit comment on the proposed rule change from interested persons.

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

The Exchange proposes to amend its rules governing the Archipelago Exchange ("ArcaEx"), the equity trading facility of PCXE. With this filing, the Exchange proposes to clarify the ArcaEx's Closing Auction functionality and limit the use of the Closing Auction to primary listed securities. The text of the proposed rule change is available on the PCX Web site (<http://www.pacificex.com>), at the PCX's Office of the Secretary and at the Commission's Public Reference Room.

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. The text of these statements may

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

be examined at the places specified in Item IV below. The Exchange 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 Exchange proposes to make clarifying changes to the Closing Auction rule contained in PCXE Rule 7.35. In particular, the Exchange proposes to make conforming changes that were recently incorporated into the ArcaEx Market Order Auction rules.³ In addition, the Exchange proposes to limit the use of its Closing Auction to Exchange-listed securities, including Exchange-listed exchange traded funds, for which the Corporation is the primary market.

The conforming changes that the Exchange proposes are as follows. First, PCXE Rule 7.35(e)(2)(A) would be clarified to reflect that orders on the side of the Imbalance⁴ shall be executed as follows: (i) Market-on-Close ("MOC") Orders⁵; (ii) Limit Orders entered prior to the Closing Auction; and (iii) Limit-on-Close ("LOC") Orders.⁶ Second, the language in PCXE Rule 7.35(e)(3) would be modified to be substantively consistent with that of the Market Order Auction changes recently adopted.⁷ Specifically, when

³ See Securities Exchange Act Release No. 52361 (August 30, 2005), 70 FR 53704 (September 9, 2005)(SR-PCX-2005-58).

⁴ See PCXE Rule 1.1(q).

⁵ See PCXE Rule 1.1(dd).

⁶ See PCXE Rule 1.1(ee).

⁷ See *supra* note 3. Note that the Market Order Auction rule text can be distinguished from the Closing Auction because the Market Order Auction applies both to Nasdaq-listed and Exchange-listed securities for which the Corporation is the primary market and all Exchange-listed exchange traded funds.

there are Limited Price Orders⁸ eligible for execution in the Closing Auction, the Closing Auction price would be the Indicative Match Price.⁹ If there were no Limited Price Orders eligible for execution in the Closing Auction, MOC Orders would be rejected. In addition, MOC Orders that are eligible for, but not executed in, the Closing Auction would be cancelled immediately upon conclusion of the Closing Auction. The Exchange also proposes to delete PCXE Rule 7.35(e)(3)(C), regarding limiting the Closing Auction Price to prices within a threshold amount. In the rule filing where modifications were made to the ArcaEx Market Order Auction, the same concept as described in PCXE Rule 7.35(e)(3)(C), was incorporated into PCXE Rule 1.1(r)(A).¹⁰

Further, the Exchange proposes a few, non-substantive changes to clarify the existing language in the Closing Auction rule. First, the Exchange proposes to modify PCXE Rule 7.35(e)(1)(A) to clarify that the Total Imbalance¹¹ and Market Imbalance¹² would be published via electronic means. Second, Examples 1 and 2 of that provision would be clarified to make the reference to the last sale during normal market hours as determined by the consolidated tape to be consistent with the reference in the “Indicative Match Price” definition. Lastly, PCXE Rule 7.35(e)(2)(B) would be modified to reflect that Limited Price Orders, with the exception of LOC Orders, may be cancelled.

The Exchange also proposes to limit the use of its Closing Auction to Exchange-listed securities, including Exchange-listed exchange traded funds, for which the

⁸ See PCXE Rule 1.1(s).

⁹ See PCXE Rule 1.1(r).

¹⁰ See supra note 3.

¹¹ See PCXE Rule 1.1(q)(1)(A).

¹² See PCXE Rule 1.1(q)(1)(B).

Corporation is the primary market. Accordingly, PCXE Rule 7.31(dd) that defines MOC Orders and PCXE Rule 7.31(ee) that defines LOC Orders would be modified to reflect that such orders might be cancelled in the following circumstances: (i) in securities for which the Corporation is not the primary market; or (ii) when the auction is suspended pursuant to PCXE Rule 7.35(g). In addition, PCXE Rule 7.35(e) would be modified to reflect that the Closing Auction would be limited to Exchange-listed securities, including Exchange-listed exchange traded funds, for which the Corporation is the primary market. The Exchange proposes to limit the use of its Closing Auction to certain securities because of limited participation in the Closing Auction to date. Accordingly, with limited liquidity to participate in the Closing Auction, orders are frequently executed at prices that vary from the closing prices at other primary markets. In order to protect ETP Holders¹³ from this execution occurring, the Exchange proposes to limit its Closing Auctions to only those securities where the Corporation is the primary market.

Lastly, the Exchange proposes to clarify that in the case of unusual system problems or other malfunctions, the Exchange may suspend auctions. Accordingly, PCXE Rule 7.35(g) would be modified to reflect this. This exception would only be used on an infrequent basis when needed to maintain a fair and orderly market. In addition, the Exchange would reject MOC and LOC Orders as indicated in proposed PCXE Rules 7.31(dd) and (ee), respectively.

¹³ See PCXE Rule 1.1(n).

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b)¹⁴ of the Act, in general, and furthers the objectives of Section 6(b)(5) of the Act,¹⁵ in particular in that it is designed to facilitate transactions in securities, to promote just and equitable principles of trade, to enhance competition and to protect investors and the public interest. In particular, the Exchange believes that making such changes to the Closing Auction procedures would better protect ETP Holders from executions at the close that are substantially away from the primary market closing prices.¹⁶

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

The Exchange does not believe that the proposed rule change 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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date

¹⁴ 15 U.S.C. 78f(b).

¹⁵ 15 U.S.C. 78f(b)(5).

¹⁶ Clarified in telephone conference among Bridget Farrell, Director, Strategy, ArcaEx, Timothy Fox, Special Counsel, Division of Market Regulation (“Division”), Commission and Mitra Mehr, Special Counsel, Division, Commission on January 10, 2006.

if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve the proposed modifications, or
- (B) institute proceedings to determine whether the proposed rule change

should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change 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 email to rules-comments@sec.gov. Please include File No. SR-PCX-2005-141 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-9303.

All submissions should refer to File No. SR-PCX-2005-141. 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 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. Copies of such filing will also 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 No. SR-PCX-2005-141 and should be submitted [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁷

Nancy M. Morris
Secretary

¹⁷ 17 CFR 200.30-3(a)(12).