April 7, 2004

TO: Secretary, The Securities and Exchange Commission
450 Fifth Street N.W.
Washington, D.C. 20549-0609

FILE NUMBER: SR-PCX-2004-08

FROM: John A. Brown
Pacific Exchange Member

SUBJECT: Pacific Exchange "Demutualization" Plan

Dear Commission,

This is a response to a filing of the Pacific Exchange's regarding a plan to convert the ownership of the Exchange from a membership organization to eventually a publicly traded common stock. My request is for the Exchange to do several things before giving Commission approval.

First, the Exchange must hold another vote on the plan because the first vote was tainted by the use of financial coercion. The Exchange is currently assessing seat owners $750 per seat, per month, even if the seat is inactive. The management of the Exchange created this charge with the express purpose of pushing seat prices down. (See attached letter of 10/29/02, page 2, paragraph 2). They did this to do economic harm to a group of dissident seat holders in Chicago. The assessment in fact forced that group to sell approximately 50 seats for approximately $18,500 each.

Even though the Exchange continued to operate at near breakeven in the 2000-2002 bear market, the assessment stayed in tack. While the Chairman was receiving a $450,000 bonus in 2002, seats settled at $14,000-$16,000 down dramatically from their $500,000 high. While many market forces are reflected in seat prices, even the most naïve would admit that a $9000 charge on a $14,000 investment has a disastrous effect on the value of that asset.

Of course, this has played nicely into the hands of the current management. Note that the current Chairman is to receive approximately 10% of the stock in the demutualized Exchange. His Compensation Committee will grant him options with a striking price of $20,000 per seat. Of course, they picked the low on seats ($14M) then added a premium to reach the $20,000 figure suggesting this was fair. What a joke! As soon as the plan passed with 90% to 10% favorable vote, the seats jumped to the $40,000 level. What a surprise!

The Exchange points with pride that their plan received 90% approval. Sounds like the results of a Cuban election? The fact that the Exchange stated; vote for the plan and the $750 monthly assessment will stop, vote against it and the Exchange will continue the assessment. That is economic blackmail!

Couple economic blackmail to the option plan for the Chairman of the Exchange and you see the plan for what it is, an asset grab by the management.

Not since Joe Grasso has a Chairman smiled so graciously and spoke with such sincerity while reaching into each Exchange member's pocket.

Please stop this injustice. I request as a remedy:

1. Stop the assessment in order for the vote to be untainted.
2. Require the Exchange to rewrite the option plan both as to the amount of shares and the striking price for the Chairman.
3. Schedule a new vote on the demutualization plan after the remedies are in place.

The Commission must at some point stand up and protect the many individuals who have suffered greatly at the hands of the current Pacific Exchange senior management. If not the Commission, then who?

Sincerely,

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John A. Brown
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October 29, 2002

Mr. Phil DeFeo, Chairman
The Pacific Exchange
301 Pine St.
San Francisco, CA 94104

Dear Phil,

For over thirty years I have had an interest in the future and well being of the Pacific Exchange. From member/chairman to the current arrangement I've seen seven chairmen come and go. Perhaps none have faced greater challenges than you. And in today's environment, where all CEO's will be examined under a microscope, none of the past chairmen have faced the same scrutiny as you.

It is my desire to better understand your mind-set and in return for you to understand mine. That is what motivates me to write this letter.

I would like you to explain your perspective or correct my misconceptions in several areas.

My first question surrounds what seems to me as an accounting anomaly. When we voted to spin off the equity business it was generally believed we had about $20-25 million in cash. The exit from equities would create approximately $32 million after tax dollars or about $50-55 million in total cash assets to the Exchange. For a year and half I tried unsuccessfully to get current financials. The excuse was given that there were "accounting issues" that were delaying the financials due to the Archipelago deal. Then one day, on the quarterly conference call to seat owners/members, you stated we had about $18-19 million in cash after the $32 million from Archipelago. I was stunned. What happened?

The second question surrounds credibility! For years, we as an Exchange argued for "Best Market" executions. All of a sudden we are involved in the business of facilitating the practice of buying order flow. You excused our about face saying we had no choice since the competition was doing it. Yet when the competition abandoned the practice, we stayed involved. The excuse was that the Exchange was only collecting the money, not actually doing the paying out. Is a pimp any less a whore?

The third area of concern is basic. For whom do you work? Most Chairmen believe that they are responsible to their Boards. That works as long as the Board represents the ownership. At the Pacific Exchange one would be deeply confused to believe the Board represents the broad ownership versus the interests of their individual firms. The public governors are always good people but often unschooled in the inter-workings of the securities industry. All too often, as is human nature, public governors "go along – to get along."

The Exchange's master plan of demutualization seemed to me just a thinly veiled plan to give ownership of the Exchange away to a few New York-based security firms. The roaring 90's provided a venue to dangle a carrot of riches to the seat holders when the demutualized company was taken public. With the dot com bubble destroyed the Board has taken a different direction.

That new direction seemed to be – destroy the value of the seats. Then it would be much easier to dispose of the old ownership. The imposition of a monthly $750 fee on unleased seats quickly reduced the seats to under $20,000 and accomplished what I believe was the goal. It had to be the Board's objective because of the mere $1,500,000 a year this monthly charge generates, it sacrificed 2/3 of the market value of the Pacific Exchange in just a few short weeks. The staff and the Board knew what the results would be and still proceeded.

My bottom line is this; the public customer is the only salvation for any Exchange outside of New York City. The equity option business was started in Chicago by commodity people because they wanted to reach the New York firm dominated equity customer. Nothing has changed. Whomsoever controls the customer order flow wins. You will **never** buy that order flow. Not cheaper rates, under the table kickbacks, nor new technology will keep a New York based firm from doing everything they can to drive business to the East Coast. Someone will always do it cheaper, spend more on technology, or buy the integrity of an order flow provider with a bigger check.

The only hope we have is to go directly to public customers. Why should e-Trade, Ameritrade, etc., etc., stand between the Pacific Exchange and the customer? To heck with Goldman Sachs and Solomon Brothers, they could care less about the Pacific. The NY firms use the West Coast when it suits them as a lever to keep other Exchanges in line.

Every vote that has come up since you became Chairman, I've supported. My letter may sound adversarial, but I am confused as just what is the game plan. The ECN's continue to steal order flow and they are backed by the very people you seem to court. How can that make any sense?

Please don't blow me off with a letter from some "legal advisor." I'm in your corner but I'm not stupid and I ask questions in a direct manner. Perhaps we could spend some time together on one of my trips to see my son and his family and you could enlighten me.

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In closing, these must be very stressful times and I pray for your health and good judgment that you may lead us through this difficult period.

Sincerely,

John A. Brown