

commencement of the Core Trading Session. The Opening Session is comprised of the Opening Auction and, thereafter, the Market Order Auction.<sup>7</sup> Limited Price Orders are matched in the Opening Auction or the Market Order Auction and executed at the Indicative Match Price.

ArcaEx currently permits a Timed Order designated as good from 5 a.m. (Pacific Time) and designated for the Opening Session to participate in the Opening Auction. Conversely, a Timed Order designated as good from 6:30 a.m. (Pacific Time) and designated for the Opening Session does not participate in the Market Order Auction. The proposed rule change is intended to reconcile the treatment of Timed Orders during the Opening Session. Accordingly, Timed Orders designated as good from 5 a.m. (Pacific Time) or 6:30 a.m. (Pacific Time) and designated for the Opening Session will not be eligible for inclusion in the Opening Auction or the Market Order Auction and, therefore, will not be reported for purposes of the Indicative Match Price and Imbalance. The PCX believes that the proposed change will facilitate ArcaEx's dissemination of consistent information.

## 2. Basis

The PCX believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>8</sup> and furthers the objectives of Section 6(b)(5) of the Act<sup>9</sup> because it is designed to promote just and equitable principals of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, to remove impediments and perfect the mechanisms of a free and open market, and to protect investors and the public interest.

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

The PCX 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*

The PCX neither solicited nor received written comments on the proposed rule change.

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

The PCX submitted a draft of this filing, including the proposed new rule text, to the Commission in fulfillment of the five-day draft notice period of Rule 19b-4(f)(6).<sup>10</sup> The PCX has further designated that the proposed rule change: (1) Does not significantly affect the protection of investors or the public interest; (2) does not impose any significant burden on competition; and (3) does not become operative for 30 days from the date of filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest. Therefore, the proposed rule change has become effective immediately upon filing with the Commission pursuant to Section 19(b)(3)(A) of the Act<sup>11</sup> and Rule 19b-4(f)(6) thereunder.<sup>12</sup>

A proposed rule change filed under Rule 19b-4(f)(6)<sup>13</sup> does not become operative until 30 days after the date of filing or such shorter time as the Commission may designate if such action is consistent with the protection of investors and the public interest. The PCX believes that the proposed rule change will reconcile the treatment of Timed Orders during the Opening Session and will eliminate any potential confusion with respect to the use of this order modifier. The PCX also believes that the rule change is necessary and appropriate in order to promote a fair, orderly, and competitive market. Therefore, the PCX has requested that the Commission accelerate the implementation of the proposed rule changes so that it may become operative immediately, before the 30-day period specified in Rule 19b-4(f)(6)(iii).<sup>14</sup>

The Commission believes that it is consistent with the protection of investors and the public interest to waive the 30-day period and to designate that the proposed rule change has become operative as of March 3, 2003, the date the PCX filed the proposal with the Commission.<sup>15</sup> At any time within 60 days after the filing of the proposed rule change, the Commission may summarily abrogate the 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 furtherance of the purposes of the Act.

### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposal is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. 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 submissions should refer to File No. SR-PCX-2003-10 and should be submitted by April 3, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>16</sup>

**Margaret H. McFarland,**  
*Deputy Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-47467; File No. SR-PCX-2002-75]

### **Self-Regulatory Organizations; Order Approving Proposed Rule Change by the Pacific Exchange, Inc., as Amended, and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 2 Relating to New Order Types and To Amend PCXE Rule 7.37**

March 7, 2003.

#### **I. Introduction**

On December 9, 2002, 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> the Pacific Exchange, Inc. ("PCX" or "Exchange"),

<sup>16</sup> 17 CFR 200.30-3(a)(12).

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

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

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

<sup>11</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>12</sup> 17 CFR 240.19b-4(f)(6).

<sup>13</sup> *Id.*

<sup>14</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>15</sup> The Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation for the sole purpose of accelerating the operative date of the proposed rule change. 15 U.S.C. 78c(f).

<sup>7</sup> See PCXE Rule 7.35(b) and PCXE Rule 7.35(c), respectively, for a detailed discussion of the Opening Auction and Market Order Auction.

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

<sup>9</sup> 15 U.S.C. 78f(b)(5).

through its subsidiary, PCX Equities, Inc. ("PCXE"), filed with the Securities and Exchange Commission ("Commission") a proposed rule change to establish new order types on the Archipelago Exchange ("ArcaEx"), the equity facility of the PCXE, and to amend the ArcaEx Working Order Process to enable the execution of such order types. The PCX filed Amendment No. 1 to the proposal on January 15, 2003.<sup>3</sup> The PCX filed Amendment No. 2 on March 7, 2003.<sup>4</sup> The proposed rule change, as amended by Amendment No. 1, was published for comment and appeared in the **Federal Register** on January 29, 2003.<sup>5</sup> The Commission received no comment letters in response to the proposed rule change. This order approves the PCX's proposed rule change, as amended, and notices and grants accelerated approval to Amendment No. 2 to the proposed rule change.

## II. Description of the Proposal

The proposal would amend PCXE rules to: (1) Adopt several new order types to accommodate the trading of securities listed on the Nasdaq Stock Market, Inc. ("Nasdaq"), on an unlisted trading privileges ("UTP") basis; (2) amend PCXE Rule 7.37 to provide for a limited exemption from the ArcaEx guarantee of executions at the NBBO or

<sup>3</sup> In Amendment No. 1, the Exchange submitted a new Form 19b-4, which replaced the original filing in its entirety.

<sup>4</sup> See Letter from Peter Bloom, Acting Managing Director, Regulatory Policy, PCX, to Marc McKayle, Special Counsel, Division of Market Regulation, Commission, dated March 7, 2003 ("Amendment No. 2"). In Amendment No. 2, the Exchange made various clarifying and technical amendments to the proposed rule text to: (1) Reference the "Joint Self-Regulatory Organization Plan Governing the Collection, Consolidation and Dissemination of Quotation and Transaction Information for Nasdaq-Listed Securities Traded on Exchanges ("Nasdaq Unlisted Trading Privileges Plan") in proposed PCXE Rule 1.1(aa), (2) clarify that the term "OTC/UTP Listing Market" shall have a meaning consistent with the Nasdaq Unlisted Trading Privileges Plan, (3) clarify the definition of "Sweep Reserve Order" by replacing the word "price" with the word "size," (4) clarify the definition of "Random Reserve Order" by indicating that the random reserve value is expressed in round-lot increments and by correcting a grammatical error, (5) amend the definition of "Pegged Order" to reflect that the display price will track the relevant Consolidated Quote information for such orders on a real-time basis and that the displayed price of a Pegged Order designated as a Discretionary Order will track the National Best Bid or Offer ("NBBO"), and that the discretionary price of such order would re-price in correlation to any changes to the displayed price, and (6) clarify that Immediate or Cancel ("IOC"), NOW, Post No Preference ("PNP"), Passive Discretionary, Discretion Limit, IOC Cross and PNP Cross orders in Nasdaq securities would receive executions no worse than the ArcaEx Best Bid or Offer ("BBO").

<sup>5</sup> Securities Exchange Act Release No. 47223 (January 21, 2003), 68 FR 4527 (January 29, 2003) (SR-PCX-2002-75).

better for certain order types trading Nasdaq securities; (3) reflect the operational requirements of two proposed order types in the Working Order Process; and (4) make various minor technical rule changes to conform to the Nasdaq UTP Plan, which extends UTP to Nasdaq SmallCap securities.

### A. Proposed New Order Types

As part of its ongoing preparation for the trading of Nasdaq securities on the ArcaEx pursuant to UTP,<sup>6</sup> PCX proposes to make several new order types available to Electronic Trading Permit ("ETP") Holders<sup>7</sup> and Sponsored Participants<sup>8</sup> (collectively "Users"), which are currently in use on the Archipelago electronic communication network ("ECN").<sup>9</sup> The proposed new order types are discussed below.

#### 1. Inside Limit Order

An Inside Limit Order is a limit order that is to be executed in whole or in part on ArcaEx. If the order were not executed in its entirety, the remaining portion of the order would be routed pursuant to PCXE Rule 7.37(d) to the market participant<sup>10</sup> with the best displayed price. Any unfilled portion of the order would not be routed to the next best price level until all quotes at the current best bid or offer are exhausted. If the Inside Limit Order were no longer marketable, it would be ranked in the Arca Book pursuant to PCXE Rule 7.36.

#### 2. Discretionary Orders

Currently, a User can submit a Discretionary Order, which is an order to buy or sell a stated amount of a security at a specified, undisplayed price (the "discretionary price"), as well as at a specified, displayed price. The undisplayed prices of a Discretionary Order are represented in the Working

<sup>6</sup> The Nasdaq UTP Plan was initially approved in 1990. See Securities Exchange Act Release No. 28146 (June 26, 1990), 55 FR 27919 (July 6, 1990) (S7-24-89). It has subsequently been amended on several occasions to, among other things, admit new Participants. See also Securities Exchange Act Release No. 46381 (August 19, 2002), 67 FR 54687 (August 23, 2002) (S7-24-89) (Order approving most recent amendments to Nasdaq UTP Plan, the 13th Amendment).

<sup>7</sup> See PCXE Rule 1.1(n).

<sup>8</sup> A "Sponsored Participant" means "a person which has entered into a sponsorship arrangement with a Sponsoring ETP Holder pursuant to [PCXE] Rule 7.29." See PCXE Rule 1.1(tt).

<sup>9</sup> The broker-dealer commonly referred to as the Archipelago ECN is Archipelago Securities, a wholly owned subsidiary of Archipelago Holdings LLC and a member of the NASD. The ECN function will cease to operate as such once all the Nasdaq securities have been transferred to ArcaEx.

<sup>10</sup> See PCXE Rule 1.1(w) (definition of "market participant").

Order Process<sup>11</sup> and can be matched with orders on the other side of the market under prescribed conditions. The Exchange proposes to adopt two new variations of the Discretionary Order called a "Passive Discretionary Order" and a "Discretion Limit Order." A summary of these proposed order types is discussed below.

a. *Passive Discretionary.* The Exchange proposes to add PCXE Rule 7.31(h)(2)(A) to define a Passive Discretionary Order. A Discretionary Order may be designated as a Passive Discretionary Order and such order would be routed pursuant to PCXE Rule 7.37(d) only if the displayed price is marketable against an away market participant. If the discretionary price of a Passive Discretionary Order were marketable, such order would only interact with trading interest in the ArcaEx Book pursuant to PCXE Rule 7.37(b)(2) and would not be routed away. Under the proposal, the Passive Discretionary order type will be available for exchange-listed and Nasdaq securities. For Passive Discretionary Orders in exchange-listed securities, if the discretionary price is marketable, such order will only interact with trading interest in the ArcaEx Book pursuant to PCXE Rule 7.37(b)(2) and will not be routed away. A Passive Discretionary Order for ITS Trade-Through Exempt Securities (as defined in PCXE Rule 7.37) will be permitted to trade at a price no more than three cents (\$0.03) away from the NBBO displayed in the Consolidated Quote. For Passive Discretionary Orders in Nasdaq securities, if the discretionary price can be matched against orders in the ArcaEx Book, then such order will interact with trading interest in the ArcaEx Book pursuant to 7.37(b)(2). The NBBO or better execution guarantee set forth in PCXE Rule 7.37 will not apply to Passive Discretionary Orders in Nasdaq securities. Instead, Passive Discretionary Orders in Nasdaq securities would trade at no worse than the ArcaEx BBO.<sup>12</sup>

In the event that a Passive Discretionary Order routed from ArcaEx to another market participant is not executed in its entirety at the other market participant's quote, ArcaEx would attempt to execute the residual trading interest in the ArcaEx Book pursuant to PCXE Rule 7.37. Finally,

<sup>11</sup> The Working Order Process is the third step in the ArcaEx execution algorithm. Working Orders are defined to include any order with a conditional or undisplayed price and/or size, including All-or-None, Discretionary, and Reserve Orders. See PCXE Rule 7.37(b)(2) (description of "Working Order Process").

<sup>12</sup> See Amendment No. 2, *supra* note 4.

Passive Discretionary Orders that are not marketable would be ranked in the ArcaEx Book pursuant to PCXE Rule 7.36.

*b. Discretion Limit.* The Exchange also proposes to add PCXE Rule 7.31(h)(2)(B) to define a Discretion Limit Order. A Discretionary Order may be designated as a Discretion Limit Order for Nasdaq securities only. If the discretionary price of a Discretion Limit Order could be matched against trading interest in the ArcaEx Book, then such order would be executed at the discretionary price or better against the displayed share size of available trading interest in the ArcaEx Book, regardless of size. If the discretionary price of a Discretion Limit Order could be matched against an away market participant, then such order would be routed pursuant to PCXE Rule 7.37(d) but only if the displayed share size of the Discretion Limit Order is equal to or less than the displayed share size of the away market participant. The NBBO or better execution guarantee set forth in PCXE Rule 7.37 would not apply to Discretion Limit Orders. Instead, Discretion Limit Orders, which will only be available for the trading of Nasdaq Securities, will not trade at a price inferior to the ArcaEx BBO.<sup>13</sup>

### 3. Reserve Orders

Under current PCXE Rule 7.31(h)(3), a Reserve Order is a limit order with a portion of the size displayed and with a reserve portion of the size ("reserve size") that is not displayed on the ArcaEx Book. With this filing, the Exchange proposes to adopt two new variations of the Reserve Order, a "Sweep Reserve Order" and a "Random Reserve Order." These proposed order types would be ranked and maintained in the Display Order Process<sup>14</sup> and/or Working Order Process of the ArcaEx Book according to price-time priority and would be processed for internal matches in the same manner as standard Reserve Orders pursuant to PCXE Rule 7.37(b)(2). The proposed rule change regarding Sweep Reserve Orders should clarify how ArcaEx treats such orders when routing to other market participants is required. In the case of a Random Reserve Order, the proposed rule change would allow a User to define the original display quantity and a random reserve value in a share

<sup>13</sup> See Amendment No. 2, *supra* note 4.

<sup>14</sup> The Display Order Process is the second step in the ArcaEx execution algorithm. In this process, the ArcaEx system matches an incoming marketable order against orders in the Display Order Process at the display price of the resident order for the total size available at the that price or for the size of the incoming order. See PCXE Rule 7.37(b)(1) description of "Display Order Process".

amount that would be used to determine the displayed quantity within a defined range each time it is replenished. These proposed order types are discussed separately below.

*a. Sweep Reserve Order.* Under proposed PCXE Rule 7.31(h)(3)(A), a Reserve Order may be designated as a Sweep Reserve Order. Based upon a User's instruction, if the displayed price of a Sweep Reserve Order is marketable against an away market participant(s), then such order will be routed (i) serially as component orders, such that each component corresponds to the displayed size, or (ii) only once in its entirety, including both the displayed and reserve portions. The Exchange believes that this rule change codifies current order routing methodology, and believes that the proposed Sweep Reserve Order type is clearly implied in current PCXE Rule 7.37(d)(2)(A)(ii).

*b. Random Reserve Order.* The Exchange proposes to add PCXE Rule 7.31(h)(3)(B) to define a Random Reserve Order. Under the rule proposal, a User could determine a display and reserve quantity for a Reserve Order. In addition, a User could also define a random reserve delta (expressed in a share amount) to determine the number of shares to display when the quote is refreshed from reserve.<sup>15</sup> Users are required to display at least 100 shares for all Reserve Orders including Random Reserve Orders. If the User does not specify the random reserve delta or the random reserve delta is set to zero, the ArcaEx system would assign the displayed size of the Reserve Order to vary to within 20% of the original specified displayed size. Should a User enter a Random Reserve Order with a display amount of 500 shares or less and a random reserve delta that is unspecified or set to zero, the order would be handled as a regular Reserve Order. The ArcaEx system would refresh the display quantity to the original displayed size, and would not vary the display quantity.

### 4. Pegged Orders

The Exchange proposes to modify the ArcaEx trading system to accept Pegged Orders. A Pegged Order is a limit order to buy or sell a stated amount of a security at a display price set to track the current bid or ask of the NBBO in an amount specified by the User.<sup>16</sup> The tracking of the relevant Consolidated Quote information for Pegged Orders would occur dynamically on a real-time basis. The associated price of each

<sup>15</sup> See Amendment No. 2, *supra* note 4.

<sup>16</sup> See proposed PCXE Rule 7.31(cc) (definition of "Pegged Order").

Pegged Order that is updated would be assigned a new entry time with priority in accordance with PCXE Rule 7.36(a). A Pegged Order may be designated as a Reserve Order or Discretionary Order and would be subject to the applicable order execution rules. The displayed price of a Pegged Order designated as a Discretionary Order would track the NBBO, and discretionary price of such order would re-price in correlation to any changes to the displayed price.<sup>17</sup> Finally, Pegged Orders are only eligible during the Core Session.

### B. Changes to PCXE Rule 7.37

The Exchange's current rules governing the order execution processes for orders in the ArcaEx Book are set forth in PCXE Rule 7.37. Presently, PCXE Rule 7.37 provides, in part, that for an execution to occur in any Order Process, the price must be equal to or better than the NBBO. The requirements of this rule do not apply to orders designated as IOC, NOW and PNP in certain exchange-traded funds ("ETFs") that are subject to the Commission's order granting a *de minimis* exemption from the trade-through restrictions of the Intermarket Trading System ("ITS") Plan; provided, however, that any resulting executions will be at a price no more than three cents (\$0.03) away from the NBBO displayed in the Consolidated Quote.<sup>18</sup> The Exchange proposes that the requirements of PCXE Rule 7.37 would not apply to existing order types (IOC, NOW and PNP orders) and proposed new order types (Passive Discretionary, Discretion Limit, IOC Cross and PNP Cross)<sup>19</sup> in Nasdaq securities, provided however that such orders in Nasdaq securities would not result in an execution at a price less than the ArcaEx BBO.<sup>20</sup>

### C. Working Order Process

The Exchange proposes the following conforming changes to certain provisions of the Working Order Process set forth in PCXE Rule 7.37(b)(2):

Under the proposal PCXE Rule 7.37(b)(2) will be amended to clarify the

<sup>17</sup> See Amendment No. 2, *supra* note 4.

<sup>18</sup> See Securities Exchange Act Release No. 46428 (August 28, 2002), 67 FR 56607 (September 4, 2002) (Order Pursuant to Section 11A of the Act and Rule 11Aa3-2(f) thereunder Granting a De Minimis Exemption for Transactions in Certain ETFs from the ITS Trade-Through Provisions. See also Securities Exchange Act Release No. 46684 (October 17, 2002), 67 FR 65618 (October 25, 2002) (SR-PCX-2002-69).

<sup>19</sup> See Securities Exchange Act Release No. 47178 (January 13, 2003), 68 FR 3076 (January 22, 2003) (Order approving File No. SR-PCX-2002-74). The Commission recently approved a separate proposed rule change establishing IOC Cross and PNP Cross Orders.

<sup>20</sup> See Amendment No. 2, *supra* note 4.

conditions in which a Passive Discretionary Order and Discretion Limit Order would be routed to an away market participant's quote. Passive Discretionary Orders would be routed away only if the displayed price is marketable against an away market participant. Discretion Limit Orders would be routed away only if the displayed share size of such order is equal to or less than the displayed share size of the away market participant.

Several pricing scenarios have been added to the Working Order Process regarding incoming marketable orders that could be matched against a Passive Discretionary Order. First, for Nasdaq securities, if the ArcaEx BBO is outside the NBBO and a Passive Discretionary Order(s) within the Working Order Process has a discretionary price worse than the NBBO, then the incoming order would execute against such Passive Discretionary Order(s) at the price of the incoming order or the displayed price of the Discretionary Order(s), whichever is better. Second, for Nasdaq securities, if the ArcaEx BBO is outside the NBBO and a Passive Discretionary Order(s) within the Working Order Process has a discretionary price equal to or better than the NBBO, then the incoming order would execute against such Passive Discretionary Order(s) pursuant to current PCXE Rule 7.37(b)(2)(A)(ii). Finally, for ITS Trade-Through Exempt Securities (as defined in PCXE Rule 7.37), if the ArcaEx BBO is outside the NBBO and a Passive Discretionary Order(s) within the Working Order Process has a discretionary price worse than the NBBO by three cents (\$0.03) or less, the incoming order would execute against such Passive Discretionary Order(s) at the price of the incoming order or the displayed price of the Discretionary Order(s), whichever is better.

#### D. Technical Changes

The Exchange has proposed to adopt several minor technical changes throughout PCXE Rules 1.1 and 7.18 to conform to the Nasdaq UTP Plan, which extends UTP to Nasdaq SmallCap securities. Accordingly, the Exchange is proposing to delete references to the term "Nasdaq/NM Security" and replacing it with "Nasdaq Security." In addition, several definitions contained in PCXE Rule 1.1 are being amended to reflect the change in name of the Nasdaq UTP Plan. Finally, current PCXE Rule 1.1(jj), which defines the term "OTC/UTP Primary Market," is being amended to reflect that the Listing Market, rather than the Primary Market, would have the authority to call a Regulatory Halt pursuant to PCXE Rule 7.18(c). A

definition of "OTC/UTP Listing Market" is being adopted from the Nasdaq UTP Plan.<sup>21</sup>

### III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning Amendment No. 2, including whether Amendment No. 2 is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. 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 submissions should refer to Amendment No. 2 of File No. SR-PCX-2002-75 and should be submitted by April 3, 2003.

### IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change

After careful review, the Commission finds, for the reasons discussed below, that the proposal is consistent with the requirements of the Act and the rules and regulations thereunder applicable to the PCX.<sup>22</sup> The Commission finds that the proposed rule change is consistent requirements of section 6(b)(5) of the Act<sup>23</sup> and the objectives of section 11A(a)(2) of the Act.<sup>24</sup> Section 6(b)(5) requires, among other things, that the rules of a national securities exchange be designed to facilitate transactions in securities and to remove impediments to and perfect the mechanism of a free and open market and a national market system. Section 11A(a)(2) of the Act authorizes the Commission to establish a national market system for securities, which should include the establishment of new data processing and communications techniques.<sup>25</sup>

In proposing to establish new order types on ArcaEx, PCX seeks to provide

market participants with more choices that will permit a more accurate representation of their trading interest on its electronic auction trading facility. In the Commission's view, the proposed order types could provide a new and advanced way for sophisticated trading interests and strategies to be represented and executed on ArcaEx. Further, the Commission believes that by amending the rules to include pricing and execution scenarios for the new order types in the Working Order Process the proposed rule change should assist Users in effectuating such trading interests and strategies. The Commission believes that the implementation of the new order types may enhance the ability of investors to represent their trading interest more completely than is currently possible on ArcaEx. In addition, the new order types may facilitate enhanced order interaction and foster price competition. The depth and liquidity of the market on ArcaEx could increase as a result of the enhanced interest and competition on ArcaEx. The Commission believes that, such order types could assist ArcaEx in attracting new market participants and to increase order flow to the PCXE, which in turn could promote greater competition among market centers.

Pursuant to PCXE Rule 7.37 quotes and orders on the ArcaEx, except those in ITS Trade-Through Exempt Securities, must be executed at a price equal to or better than the NBBO, unless ArcaEx has routed the order to an away market at the NBBO. Under the proposal, executions in IOC, NOW, PNP, Passive Discretionary, Discretion Limit, IOC Cross, and PNP Cross orders for Nasdaq securities would also be included in the ArcaEx exception to the PCXE Rule 7.37 price protection provision. Specifically, executions in such orders in Nasdaq securities could be effected at a price no worse than the ArcaEx BBO. The Commission notes that currently there is no trade-through prohibition for Nasdaq securities because the Nasdaq UTP Plan does not provide for intermarket linkages between its participants like the listed securities market.<sup>26</sup> The Commission believes that without the presence of an intermarket linkage for Nasdaq UTP Plan participants it would be impracticable for PCXE to attempt to provide intermarket price protection for the above-mentioned orders in Nasdaq securities. Nonetheless, the Commission emphasizes that this approval order does not diminish investor protections, and that such orders in Nasdaq

<sup>21</sup> See *supra* note 6.

<sup>22</sup> In approving this rule, the Commission notes that it has considered the proposal's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>23</sup> 15 U.S.C. 78f(b)(5).

<sup>24</sup> 15 U.S.C. 78k-1(a)(2).

<sup>25</sup> 15 U.S.C. 78k-1(a)(2).

<sup>26</sup> See *supra* note 6.

securities on ArcaEx are still subject to a broker's duty of best execution for its customer.

The Commission finds good cause for approving Amendment No. 2 to the proposed rule change prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. In Amendment No. 2, the Exchange made various clarifying and technical amendments to the proposed rule text to: (1) Reference the "Joint Self-Regulatory Organization Plan Governing the Collection, Consolidation and Dissemination of Quotation and Transaction Information for Nasdaq-Listed Securities Traded on Exchanges" in proposed PCXE Rule 1.1(aa), (2) clarify that the term "OTC/UTP Listing Market" shall have a meaning consistent with the Nasdaq Unlisted Trading Privileges Plan, (3) clarify the definition of "Sweep Reserve Order" by replacing the word "price" with the word "size," (4) clarify the definition of "Random Reserve Order" by indicating that the random reserve value is expressed in share amounts and by correcting a grammatical error, (5) amend the definition of "Pegged Order" to reflect that the display price will track the relevant Consolidated Quote information for such orders on a real-time basis and that the displayed price of a Pegged Order designated as a Discretionary Order will track the NBBO, and that the discretionary price of such order would re-price in correlation to any change in the displayed price, and (6) clarify that IOC, NOW, PNP, Passive Discretionary, Discretion Limit, IOC Cross and PNP Cross orders in Nasdaq securities will received executions at a price no worse than the ArcaEx BBO. Because Amendment No. 2 is of a technical, clarifying, non-substantive nature, and does not raise any novel regulatory issues or issues that were not considered by the Commission prior to its submission, the Commission finds good cause for accelerating approval of the proposed rule change, as amended by Amendment No. 2.

## V. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,<sup>27</sup> that the proposed rule change, (File No. SR-PCX-2002-75) as amended, be, and it hereby is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>28</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 03-6072 Filed 3-12-03; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-47456; File No. SR-Phlx-2002-77]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the Philadelphia Stock Exchange, Inc. To Adopt a Specialist Revenue Sharing Plan for Trades in the Nasdaq-100 Index Tracking Stock

March 6, 2003.

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 December 16, 2002, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange"), 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 Phlx. The Exchange amended the proposal on February 28, 2003.<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

The Phlx proposes to amend its schedule of dues, fees and charges to adopt a Specialist Revenue Sharing Plan for trades in the Nasdaq-100 Index Tracking Stock ("QQQ").<sup>SM</sup> <sup>4</sup> Under this

<sup>28</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> On February 28, 2003, the Exchange filed a Form 19b-4, which replaced the original filing in its entirety ("Amendment No. 1"). In Amendment No. 1, the Exchange made technical corrections to the proposed rule text.

<sup>4</sup> The Nasdaq-100®, Nasdaq-100 Index®, Nasdaq®, The Nasdaq Stock Market®, Nasdaq-100 Shares<sup>SM</sup>, Nasdaq-100 Trust<sup>SM</sup>, Nasdaq-100 Index Tracking Stock<sup>SM</sup>, and QQQ<sup>SM</sup> are trademarks or service marks of The Nasdaq Stock Market, Inc. ("Nasdaq") and have been licensed for use for certain purposes by the Phlx pursuant to a License Agreement with Nasdaq. The Nasdaq-100 Index® (the "Index") is determined, composed, and calculated by Nasdaq without regard to the Licensee, the Nasdaq-100 Trust<sup>SM</sup>, or the beneficial owners of Nasdaq-100 Shares<sup>SM</sup>. Nasdaq has complete control and sole discretion in determining, comprising, or calculating the Index or in modifying in any way its method for determining, comprising, or calculating the Index in the future.

program, the Exchange is proposing to share with the QQQ specialist unit a portion of the revenues that the Exchange receives under the Consolidated Tape Association ("CTA") Plan<sup>5</sup> attributable to the QQQ (which is reportable on Tape B).<sup>6</sup> The Exchange proposes to begin its program on November 1, 2002.

The text of the proposed rule change is set forth below. Additions are in italics.

*Specialist Revenue Sharing Program for Nasdaq-100 Index Tracking Stock ("QQQ")*

*The Exchange will share a portion of net revenues that it receives for Tape B under the Consolidated Tape Association ("CTA") Plan attributable to the Nasdaq-100 Index Trading Stock ("QQQ") with the specialist unit for the QQQ. The Specialist Revenue Sharing Program operates as follows:*

- *Revenues under the CTA Plan are distributed to Plan Participants on a quarterly basis. Each quarter, the Phlx will start its calculation with the quarterly revenues actually received for Tape B.*
- *First, Phlx will determine the portion of such quarterly revenues attributable to the trading of QQQ for each calendar month in the quarter to which the revenue is attributed.*
- *Then, Phlx will subtract the amount it owes Nasdaq under its license agreement for each such calendar month, to arrive at the "Monthly Residual QQQ Tape Revenue" for that month.*

- *The Monthly Residual QQQ Tape Revenue will be shared between Phlx and the QQQ specialist unit in the following order of priority, in each case to the extent that Monthly Residual QQQ Tape Revenues are available:*

- (i) *Phlx will receive the first \$15,000 per month of the Monthly Residual QQQ Tape Revenue to cover, at a minimum, its estimated monthly costs for operating and regulating trading of the QQQ on the Exchange;*

- (ii) *the specialist unit will receive the next \$15,000 per month; and*

<sup>5</sup> The CTA Plan is a national market system plan approved by the Commission pursuant to section 11A of the Act, (15 U.S.C. 78k-1, and Rule 11Aa3-2 thereunder, 17 CFR 240.11Aa3-2); CTA Plan: Second Restatement of Plan Submitted to the Securities and Exchange Commission Pursuant to Rule 11Aa3-1 under the Act, May 1974 as restated March 1980 and December 1995. The CTA Plan governs, among other things, the collection, consolidation and dissemination of transaction reports in certain securities and the distribution of the revenues derived therefrom among parties to the CTA Plan, which are known as the Plan Participants.

<sup>6</sup> This proposal applies only to QQQ and to no other Tape B security nor any Tape A security.

<sup>27</sup> 15 U.S.C. 78s(b)(2).