

regulations thereunder, Gerald J. Laporte, Designated Federal Officer of the Committee, has ordered publication of this notice.

Dated: October 7, 2005.

**Jonathan G. Katz,**

*Committee Management Officer.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-52566; File No. SR-PCX-2005-56]

### Self-Regulatory Organizations; Pacific Exchange, Inc.; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto Relating to the Directed Order Process

October 5, 2005.

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 April 21, 2005, the Pacific Exchange, Inc. (“PCX” 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 the PCX. On October 4, 2005, the PCX filed Amendment No. 1 to the proposed rule change.<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 PCX proposes to modify its Directed Order Process as part of its continuing efforts to enhance participation on the Archipelago Exchange (“ArcaEx”) facility. In conjunction with these modifications, the Exchange proposes two new classifications of Market Makers, Designated Market Makers (“DMMs”) and Lead Market Makers (“LMMs”). Only DMMs and LMMs will be eligible to participate in the Directed Order Process as Market Makers.

The text of the proposed rule change, as amended, appears below. Additions are in italics. Deleted items are in brackets.

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

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

<sup>3</sup> Amendment No. 1, which replaced and superceded the original filing in its entirety, is incorporated in this notice.

#### Rule 1

##### Definitions

Definitions

Rule 1.1 (a)–(aaa)—No change.

(bbb) *The term “Designated Market Maker” shall mean a registered Market Maker that participates in the Directed Order Process.*

(ccc) *The term “Lead Market Maker” shall mean a registered Market Maker that is the exclusive Designated Market Maker in listings for which the Corporation is the primary market.*

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#### Rule 7

##### Equities Trading

Registration of Market Makers in a Security

Rule 7.22 (a)–(b)—No change.

(c) *The Corporation may limit the number of Designated Market Makers in a security upon prior written notice to ETP Holders.*

(d) *Designated Market Makers and Lead Market Makers shall be selected by the Corporation. Such selection shall be based on, but is not limited to, the following: experience with making markets in equities; adequacy of capital; willingness to promote the Exchange as a marketplace; issuer preference; operational capacity; support personnel; and history of adherence to Exchange rules and securities laws.*

[(c)] (e) *Voluntary Termination of Security Registration. A Market Maker may voluntarily terminate its registration in a security by providing the Corporation with a one-day written notice of such termination. A Market Maker that fails to give advanced written notice of termination to the Corporation may be subject to formal disciplinary action pursuant to Rule 10.*

[(d)] (f) *The Corporation may suspend or terminate any registration of a Market Maker in a security or securities under this Rule whenever, in the Corporation’s judgment, the interests of a fair and orderly market are best served by such action.*

[(e)] (g) *An ETP Holder may seek review of any action taken by the Corporation pursuant to this Rule, including the denial of the application for, or the termination or suspension of, a Market Maker’s registration in a security or securities, in accordance with Rule 10.13.*

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#### Rule 7

##### Equities Trading

*Designated Market Maker Performance Standards*

Rule 7.24 [Reserved].

(a) *Designated Market Makers will be required to maintain minimum performance standards the levels of which may be determined from time to time by the Corporation. Such levels will vary depending on the price, liquidity, and volatility of the security in which the Designated Market Maker is registered. The performance measurements will include (i) percent of time at the NBBO; (ii) percent of executions better than the NBBO; (iii) average displayed size; (iv) average quoted spread; and (v) in the event the security is a derivative security, the ability of the Designated Market Maker to transact in underlying markets.*

(b) *Designated Market Makers that are Lead Market Makers will be held to higher performance standards in the securities in which they are registered as Lead Market Maker than Designated Market Makers that are not Lead Market Makers.*

(c) *Market Makers that are not Designated Market Makers will not be required to maintain the minimum performance standards as described in paragraph (a) above.*

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#### Rule 7

##### Equities Trading

Registration of Odd Lot Dealers

Rule 7.25 (a)—No change.

(b) *Market Makers Registered in a Security. For each security in which a Market Maker is registered, the Market Maker may become an Odd Lot Dealer in that security. For each security in which a Market Maker is registered as Lead Market Maker, the Lead Market Maker must also register as an Odd Lot Dealer in that security.*

Rule 7.25 (c)–(e)—No change.

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#### Rule 7

##### Equities Trading

Orders and Modifiers

Rule 7.31 (a)–(h)—No change.

(i) *Directed Order.*

(1) *Any market or limit order to buy or sell which has been directed to a particular Designated Market Maker by the User. Users must be permissioned by Designated Market Makers to send a Directed Order to that Designated Market Maker.*

[(2)] *The Corporation shall suspend the Directed Order Process for a security*

when a locked or crossed market exists in that security. The Directed Order Process for that security shall resume when the locked or crossed market in that security no longer exists.]

(j) Directed Fill. Any *Designated Market Maker* [with the appropriate technology, as determined from time to time by the Corporation.] may submit a standing instruction to the Archipelago Exchange for the parameters of a Directed Fill, including, but not limited to, the size and price of the order. [the Users that may send such Market Maker a Directed Order, the price improvement algorithm and the period of time the instruction is effective.] The Market Maker's Directed Fill described in the instruction will only be generated in response to a Directed Order directed to such Market Maker. [The Directed Fill is a limit order with (1) a size that is equal to or less than the size of the Directed Order and (2) a price that improves the BBO by an automatically preset amount, which, except as provided in Rule 7.6(a), Commentary .06, must be equal to or greater than the MPII, pursuant to a price improvement algorithm; provided, however, the Directed Fill will not be generated if the price is not equal to or better than the NBBO.] A Market Maker may modify the parameters of the instruction for a Directed Fill at any time [from time to time], as the Corporation permits.

Rule 7.31 (k)-(hh)—No change.

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## Rule 7

### Equities Trading

#### Order Execution

##### Rule 7.37

(a) Step 1: Directed Order Process. [During Core Trading Hours only,] [o]Orders may be matched and executed in the Directed Order Process as follows:

(1) If a User submits a marketable Directed Order to the Archipelago Exchange and the User's [d]Designated Market Maker has a standing instruction for a Directed Fill to the Archipelago Exchange, the Directed Order shall be [executed] *matched* against the Directed Fill of the [d]Designated Market Maker.

(2) If a User submits a marketable Directed Order to the Archipelago Exchange and the User's [d]Designated Market Maker has not submitted an instruction for a Directed Fill, the Directed Order shall enter the Display Order Process, as described in subsection (b) of this Rule.

(3) *Directed Orders that are matched for execution against Directed Fills may be broken up by orders on the Arca Book if there is a displayed order on the Arca Book priced at or better than the*

*matched order. In the event that the matched order is broken up, it will be handled as follows:*

(i) *If the remaining balance of the matched order results in the Designated Market Maker side of the order being unexecuted, the remaining balance of the order shall be returned to the Directed Process to be eligible as a Directed Fill instruction.*

(ii) *If the remaining balance of the matched order results in the User being unexecuted, the remaining balance of the order will be posted in the Arca Book.*

[[3]4] If a User submits any order other than a marketable Directed Order to the Archipelago Exchange, the User's order immediately shall enter the Display Order Process, as described in subsection (b) of this Rule, without interacting with any Directed Fills.

[(4) No Directed Order to buy (sell) shall be executed at a price equal to or better than the national best bid (offer) within the Directed Order Process. Such Directed Orders immediately shall enter the Display Order Process, as described in subsection (b) of this Rule, without interacting with any Directed Fills.]

Rule 7.37 (b)-(d)—No change.

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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 PCX 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

Currently, PCXE Rule 7.37 describes ArcaEx's order execution processes.<sup>4</sup> This proposal seeks to modify the first of those processes, the Directed Order Process. In particular, the Exchange seeks to make the following modifications. First, the Exchange proposes to add a provision that

<sup>4</sup> PCXE Rule 7.37 includes the following ArcaEx order execution processes: Directed Order Process, Display Order Process, Tracking Order Process, and Routing Away. This rule proposal seeks to modify the Directed Order Process.

requires Users<sup>5</sup> to be permissioned by DMMs to send a Directed Order to that DMM. Second, the Exchange proposes to eliminate a provision of PCXE Rule 7.31 that suspends the Directed Order Process when a locked or crossed market exists in a security. This section would be eliminated because the Exchange believes that it is not relevant to suspend the Directed Order Process during a locked or crossed market. Third, the Exchange proposes to simplify the "Directed Fill" definition to make clear that a Directed Fill specifies the size and price of the Directed Fill.

The modifications to PCXE Rule 7.37 and the Directed Order Process are described below. First, the Exchange proposes that the Directed Order Process be available during Opening, Core, and Late trading sessions and that PCXE Rule 7.37's language that limits the Directed Process to Core Trading Hours be eliminated. Second, the Exchange proposes to simplify language in PCXE Rule 7.31(j) related to the definition of a Directed Fill to make clear that the parameters of a Directed Fill are price and size, and to delete obsolete language no longer necessary. Third, the Exchange proposes that marketable Directed Orders first attempt to match against the DMM to which the order has been directed. Directed Orders that are matched against DMMs pursuant to their Directed Fill instructions would be exposed to the Arca Book before execution.<sup>6</sup> Such matched orders would be broken up if there is an order displayed on the Arca Book at a price that is at or better than the matched order. In the event that a matched order is broken up, the remaining portion of the Directed Order would be posted in the Arca Book. Further, because the displayed orders in the book take priority over Directed Orders, the Exchange proposes deleting the existing reference in PCXE Rule 7.37(a)(4).<sup>7</sup>

In addition, the Exchange proposes creating a definition of "Designated Market Maker." The definition would be added to PCXE Rule 1.1 to clarify that a DMM is a registered Market Maker that participates in the Directed Order

<sup>5</sup> See PCXE Rule 1.1(yy).

<sup>6</sup> Directed Fills that are matched against Directed Orders would not be eligible for post trade anonymity and, as such, the Exchange is not seeking a limited exemption from Paragraph (a)(2)(i)(A) of Rule 10b-10 under the Act.

<sup>7</sup> PCXE Rule 7.37(a)(4) states that "[n]o Directed Order to buy (sell) shall be executed at a price equal to or better than the national best bid (offer) within the Directed Order Process. Such Directed Orders immediately shall enter the Display Order Process, as described in subsection (b) of this Rule, without interacting with any Directed Fills."

Process. The Exchange also proposes adding a definition to PCXE Rule 1.1 to describe a LMM as an exclusive DMM for primary listings. Further, the Exchange proposes adding language to PCXE Rule 7.22 regarding the Registration of Market Makers to provide the Corporation with the ability to limit the number of DMMs with prior written notice to ETP Holders.<sup>8</sup> PCXE Rule 7.22 already provides that the Corporation may consider certain performance and capability guidelines in selecting Market Makers. The Exchange also proposes adding DMM and LMM selection criteria that is consistent with the criteria described in PCX Rule 6.82 for options LMMs.<sup>9</sup> In addition, the Exchange seeks to clarify in PCXE Rule 7.24 that DMMs would be required to maintain certain performance standards which may vary depending on the price, liquidity, and volatility of the security. In particular, such standards would include (i) Percent of time at the NBBO; (ii) percent of executions better than the NBBO; (iii) average displayed size; (iv) average quoted spread; and (v) in the event the security is a derivative security, the ability of the DMM to transact in the underlying markets. The Exchange would have the ability to modify the specific levels to be used in defining the performance standards, however, the Exchange would not modify the types of standards to be used. Lastly, PCXE Rule 7.25 would be modified to require LMMs to register as Odd Lot Dealers in the securities in which they are registered as LMM. This modification would ensure that odd lot executions are facilitated for primary listings that could not otherwise be routed away to another market center for execution.

## 2. Statutory Basis

The Exchange believes that the proposed rule change, as amended, is consistent with Section 6(b) of the Act,<sup>10</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act,<sup>11</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and

equitable principals of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system.

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

- (A) by order approve such proposed rule change, as amended, or
- (B) institute proceedings to determine whether the proposed rule change, as amended, 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, 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](mailto:rule-comments@sec.gov). Please include File Number SR-PCX-2005-56 on the subject line.

### Paper Comments

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE., Washington, DC 20549-9303.

All submissions should refer to File Number SR-PCX-2005-56. 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 Section, Station Place, 100 F Street, NE., 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-2005-56 and should be submitted on or before November 3, 2005.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

**J. Lynn Taylor,**

*Assistant Secretary.*

[FR Doc. E5-5594 Filed 10-12-05; 8:45 am]

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## SMALL BUSINESS ADMINISTRATION

[License No. 06/76-0329]

### Pharos Capital Partners II, L.P.; Notice Seeking Exemption Under Section 312 of the Small Business Investment Act, Conflicts of Interest

Notice is hereby given that Pharos Capital Partners II, L.P., One Burton Hills Blvd., Suite 180, Nashville, TN 37215, a Federal Licensee under the Small Business Investment Act of 1958, as amended ("the Act"), in connection with the financing of a small concern, has sought an exemption under section 312 of the Act and § 107.730, Financings which Constitute Conflicts of Interest of the Small Business Administration ("SBA") Rules and Regulations (13 CFR 107.730). Pharos Capital Partners II, L.P. proposes to provide equity/debt security financing to Alereon, Inc. The financing

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

<sup>8</sup> See PCXE Rule 1.1(n).

<sup>9</sup> See PCX Rule 6.82(e) which states "The Exchange will select that candidate who appears best able to perform the functions of an LMM in the designated option issue. Factors to be considered for selection include, but are not limited to, the following: experience with trading the option issue; adequacy of capital; willingness to promote the Exchange as a marketplace; operational capacity; support personnel; history of adherence to Exchange rules and securities laws; trading crowd evaluations made pursuant to Rule 6.100; and any other criteria specified in this Rule."

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

<sup>11</sup> 15 U.S.C. 78f(b)(5).