



RULE
ADOPTION
NOTICE

RAN-05-62
September 7, 2005

**TO: All OTP Holders and OTP Firms
ETP Holders and Sponsored Participants**

FROM: Department of Regulatory Policy

**SUBJECT: ArcaEx Modifications to Market Order Auction
(File No. SR-PCX-2005-58)**

On April 22, 2005, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission a proposed rule change to amend PCXE Rules governing the Market Order Auction of the Archipelago Exchange ("ArcaEx"), the equities trading facility of PCXE. On June 27, 2005, the Exchange amended the proposed rule change and on July 8, 2005, the Exchange further amended the proposed rule change. The Commission approved the proposed rule change on August 30, 2005.

The following is the text of the rule change. Questions regarding this bulletin may be directed to Alden Adkins at (415) 393-4037.

EXHIBIT 5
Text of the Proposed Rule Change¹

PCX Equities, Inc.

Rule 1
Definitions

Definitions

Rule 1.1(a) – (q) – No change.

Indicative Match Price

¹ New text is underscored; deleted text is in brackets.

(r) For the purposes of the Opening Auction, the Market Order Auction, the Closing Auction and the Trading Halt Auction, as the case may be, the term "Indicative Match Price" shall mean for each security (1) the best price at which the maximum volume of shares are executable; or (2) if there are two or more prices at which the maximum volume of shares are executable, the price that is closest to the closing price of the previous trading day's normal market hours (or, in the case of a Closing Auction or a Trading Halt Auction, the last sale during normal market hours), as determined by the consolidated tape will establish the opening price (or the closing price in the case of a Closing Auction), provided that if such price would trade through an eligible Limited Price Order designated for such auction, then the opening price will occur at the best price level available where no trade through occurs.

(A) When the Market Order Auction Price or Closing Auction Price is established by PCXE Rule 7.35(c)(3)(A)(1) or 7.35 (e)(3), the Limit Orders eligible for determining the Indicative Match Price shall be limited by the price collar thresholds established by the Corporation. The Corporation shall set and modify such thresholds from time to time upon prior notice to ETP Holders.

Rule 1.1(s) – (aaa) – No change.

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Rule 7 Equities Trading

Auctions

Rule 7.35 (a)- (b)- No change.

(c) Market Order Auction.

For exchange-listed securities, excluding: (i) exchange-listed securities for which the Corporation is the primary market; and (ii) all exchange-listed exchange traded funds, the Corporation will not conduct a Market Order Auction. Rather, the Corporation will route all Market Orders to the primary market until the first opening print on the primary market. After the first opening print on the primary market, all Market Orders will be processed pursuant to PCXE Rule 7.37. Limit Orders will be processed pursuant to PCXE Rule 7.37.

(1) Publication of Indicative Match Price and Imbalances

(A) For exchange-listed securities for which the Corporation is the primary market and all exchange-listed exchange traded funds

[(A)] (1) Beginning at 5:00 am (Pacific Time), and updated real-time thereafter, the Indicative Match Price of the Market Order Auction and the volume of Market Orders and Limit [o]Orders available to trade at such price, and the Market Imbalance and Total Imbalance [associated with the Market Order Auction], if any, shall be published via electronic means. Market [o]Orders shall be included for purposes of calculating the Total Imbalance and Market Imbalance. [Limit orders shall only be included in the Total Imbalance calculations.]

Example 1:

- (1) Market [o]Order to buy 5000 shares;
- (2) Auction-Only Limit Order to sell 1000 at 50;
- (3) Limit [o]Order to sell 1000 at 50.50; and
- (4) Limit [o]Order to sell 500 at 50.75.

The Archipelago Exchange will publish an Indicative Match Price of 50.75, a volume of [2500] 5000 shares, a buy Market Imbalance of 2500 shares, and a Total Imbalance of 2500 Shares.

Example 2:

- (1) Market [o]Order to buy 3000 shares;
- (2) Market [o]Order to sell 1000;
- (3) Limit [o]Order to sell 1000 at 41.00; and
- (4) Limit [o]Order to sell 1000 at 41.25.

The Archipelago Exchange will publish an Indicative Match Price of 41.25 and a match volume of 3000 shares and will not publish an Imbalance.

[(B) If an Indicative Match Price does not exist, the Archipelago Exchange shall indicate via electronic means that an Indicative Match Price does not exist.

(C) If the difference between the Indicative Match Price and the closing price of the previous trading day's normal market hours, as determined by the Consolidated Tape, is equal to or greater than a pre-determined amount, as determined from time to time by the Corporation, the Archipelago Exchange will assign a "SIG" designator to such Indicative Match Price and publish such designator via electronic means as determined from time to time by the Corporation.]

(B) For Nasdaq-Listed securities

Beginning at 5:00 am (Pacific Time), and updated real-time thereafter, the Market Imbalance associated with the Nasdaq-Listed Market Order Auction, if any, shall be published via electronic means. The Corporation will not publish an Indicative Match Price.

(2) Reduction of Imbalances

(A) For exchange-listed securities for which the Corporation is the primary market and all exchange-listed exchange traded funds

[(A)] (1) Any Imbalance in the Market Order Auction may be reduced by new orders, entered on the side of the market opposite the Imbalance[,]. Orders on the side of the Imbalance shall be executed pursuant to the following priority:

(i) Market [o]Orders;

(ii) Limited Price Orders eligible for the Opening Session;

(iii) Limited Price Orders designated for the Core Trading Session and entered before 6:28 am (Pacific Time);

(iv) Auction-Only Limit Orders; and

(v) Cleanup Orders.

[(B)] (2) Between 6:28 am (Pacific Time) and the conclusion of the Market Order Auction, Limited Price Orders eligible for the Opening Session [or the Core Trading Session] may be cancelled, but Limited Price Orders not eligible for the Opening Session, [m]Market [o]Orders, Auction-Only Limit Orders and Cleanup Orders may not be cancelled.

[(C)] (3) Between 6:28 am (Pacific Time) and the conclusion of the Market Order Auction, [m]Market [o]Orders and Auction-Only Limit Orders may not be entered on the same side as the Imbalance. Market [o]Orders and Auction-Only Limit Orders may be entered on the opposite side of the Imbalance, however, any time before the conclusion of the Market Order Auction.

(B) For Nasdaq-Listed securities

Any Market Imbalance in the Nasdaq-listed Market Order Auction may be reduced by new Market Orders entered on the side of the market opposite the Market Imbalance.

(3) Determination of Market Order Auction Price

(A) For exchange-listed securities for which the Corporation is the primary market and all exchange-listed exchange traded funds, the Market Order Auction Price shall be determined as follows:

[(A)] (1) [If there is no Imbalance,]If there are Limit Orders in the Market Order Auction eligible for execution, all orders eligible for execution in the Market Order Auction pursuant to PCXE Rule 7.34(d) will be executed [in the Market Order Auction] at the Indicative Match Price as of 6:30 am (Pacific Time).

[(B)] (2) [If an Imbalance exists, or if an equilibrium exists between buy market orders and sell market orders,] If there are no Limit Orders eligible for execution in the Market Order Auction:

- (i) in the case of exchange-listed exchange traded funds for which the Corporation is not the primary market, as many buy [m]Market [o]Orders and sell [m]Market [o]Orders as possible shall be matched and executed [, on a time priority basis,] once an NBBO is available, [(i)] at the midpoint of the first uncrossed NBBO [at] after 6:30 am (Pacific Time), [in the case of exchange-listed securities for which the Corporation is not the primary market] ; or
- (ii) in the case of exchange-listed securities, including exchange-listed exchange traded funds, for which the Corporation is the primary market, Market Orders shall be rejected and shall not be eligible for paragraph 7.35(c)(3)(A)(3) below.

(3) The Market Orders that are eligible for, but not executed in the Market Order Auction, shall become eligible for execution in the Core Trading Session immediately upon conclusion of the Market Order Auction.

[(ii)] at the midpoint of the NBBO at 6:30 am (Pacific Time), in the case of Nasdaq-listed securities, provided that the NBBO is not crossed; or

[(iii)] at the midpoint of the first uncrossed NBBO after 6:30 am (Pacific Time), in the case of Nasdaq securities in which the NBBO is crossed but one side of the BBO is not crossed by the NBBO; or

[(iv)] at the midpoint of the first uncrossed NBBO after 6:30 a.m. (Pacific Time), in the case of Nasdaq securities in which the NBBO is crossed and where both sides of the BBO are crossed by the NBBO; or

[(v)] at the bid (offer) of the BBO that was crossed prior to 6:30 am (Pacific Time), in the case of Nasdaq securities in which the BBO is crossed by a market participant; or

[(vi)] at the Indicative Match Price as of 6:30 am (Pacific Time) in the case of those issues for which the Corporation is the primary market. If equilibrium exists between buy and sell market orders, the match price shall be at the last Corporation sale price in the security regardless of the trading session; however, if the last Corporation sale price is lower than the BBO, the match price shall be the displayed bid in the security, or if the last Corporation sale price is higher than the BBO, the match price will be the displayed

offer in the security.]

(4) [Such] Market Order Auction executions shall be designated with a modifier to identify them as Market Order Auction trades. [The market orders that are eligible for, but not executed in the Market Order Auction, shall become eligible for execution in the Core Trading Session immediately upon conclusion of the Market Order Auction.]

(B) For Nasdaq-Listed securities

(1) As many buy Market Orders and sell Market Orders as possible shall be matched and executed at the midpoint of the first uncrossed NBBO after 6:30 am (Pacific Time);

(2) Limit Orders and any remaining Market Imbalance Market Order interest [will] shall be ranked in price/time priority as described in PCXE Rule 7.36 and processed pursuant to PCXE Rule 7.37.

7.35 (d) - (g)- No change.

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