



RULE
ADOPTION
NOTICE

RAN-05-69
October 31, 2005

TO: All OTP Holders and OTP Firms

FROM: Department of Regulatory Policy

SUBJECT: Offers of Settlement
(File No. SR-PCX-2005-75)

On June 13, 2005, the Pacific Exchange, Inc. (“PCX” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) an amendment to PCX Rule 10.6 and subsequently filed Amendment No. 1 on September 21, 2005. The amended PCX Rule 10.6 revises the procedures for offers of settlement submitted in Exchange enforcement actions against Options Trading Permit (“OTP”) Holders and OTP Firms in order to make the disciplinary process more efficient and effective while maintaining appropriate OTP Holder and OTP Firm involvement in the oversight of the settlement process. The SEC approved the proposed rule change on October 28, 2005.

The following is the text of the rule change. Questions regarding this bulletin may be directed to Melanie Grace at (415) 393-4135.

EXHIBIT 5

Text of the Proposed Rule Change:¹

Rules of the Pacific Exchange, Inc.

Rule 10 **Offers of Settlement**

Rule 10.6 (a)[. At any time prior to decision by the Conduct Panel the Respondent may submit to the Ethics and Business Conduct Committee a written offer of settlement which shall contain a proposed stipulation of facts and shall consent to a specified penalty. Where the Ethics and Business Conduct Committee accepts an offer of settlement, it shall issue a decision, including findings and conclusions and impose a penalty, consistent with the terms of such offer. Where the Ethics and Business Conduct Committee rejects an offer of settlement, it shall notify the Respondent and the matter shall proceed as if such offer had not been made, and the offer and all documents relating thereto shall not become part of the record. A decision of the Ethics and Business

¹ New text is underlined, Deleted text is in brackets.

Conduct Committee issued upon acceptance of an offer of settlement as well as the determination of the Ethics and Business Conduct Committee whether to accept or reject such an offer shall be final, and the Respondent may not seek review thereof.

(b) If there is more than one Respondent in a proceeding and one or more of said Respondents submits an offer of settlement, the Ethics and Business Conduct Committee may accept or reject such offers from any one or all of the Respondents submitting such offers. The proceedings shall be dismissed as to those Respondents whose offers have been accepted, and the proceedings shall continue as scheduled for the remaining Respondents.]

When Offer Allowed; No Stay of Proceeding

(1) A Respondent, as defined in PCX Rule 10.4, who is notified that a matter has been referred to the Department of Enforcement of the Exchange against him or her may propose in writing to the Department of Enforcement of the Exchange an offer of settlement at any time.

(2) If a Respondent proposes an offer of settlement after a hearing on the merits has begun, the making of an offer of settlement shall not stay the proceeding, unless otherwise decided by the Conduct Panel as defined in PCX Rule 10.5(a).

(b) Settlement Offer Shall Conform to Rule

A Respondent who makes an offer of settlement shall do so in conformity with the provisions of this Rule 10.6 and shall not make such an offer of settlement frivolously or propose a sanction inconsistent with the seriousness of the violations to be found.

(c) Contents and Signature Requirements

An offer of settlement shall be in writing and signed by the person making the offer, and, if the person is represented by counsel or a representative, signed also by the counsel or representative. The offer of settlement shall contain in reasonable detail:

(1) the specific statutory or rule provisions that the OTP Holder, OTP Firm or associated person is alleged to have violated;

(2) a statement containing the acts or practices that the OTP Holder, OTP Firm or associated person is alleged to have engaged in or omitted;

(3) a statement consenting to findings of fact and violations consistent with the statements contained in the offer of settlement required by subparagraphs (c)(1) and (c)(2);

(4) a proposed sanction to be imposed that is consistent with the Exchange's then current sanction guidelines or, if inconsistent with the sanction guidelines, a detailed statement supporting the proposed sanction(s); and

(5) the effective date of any sanction(s) imposed, or a statement that the effective date of the sanction(s) will be determined by the General Counsel of the Exchange.

(d) Waiver

If a Respondent submits an offer of settlement, by the submission thereof, such Respondent expressly waives:

(1) any right of such Respondent to appeal or otherwise challenge the acceptance or the rejection of the offer or the related decision before a Conduct Panel, the EBCC, any other Board committee, the Board, the Securities and Exchange Commission, the courts, or any other relevant authority;

(2) any right of such Respondent to claim bias or prejudice of the Chief Regulatory Officer, EBCC, Chairman of the EBCC, the Conduct Panel, the Chairman of the Conduct Panel, a panelist of the Conduct Panel, the General Counsel, the Board, or any member of the Board, in connection with such person's or body's participation in discussions regarding the terms and conditions of the offer of settlement and the decision, or other consideration of the offer of settlement and decision, including acceptance, or rejection of such offer of settlement and decision; and

(3) any right of such Respondent to claim that a person or body violated the ex parte prohibitions of PCX Rule 10.3, in connection with such person's or body's participation in discussions regarding the terms and conditions of the offer of settlement and the decision, or other consideration of the offer of settlement and decision, including acceptance or rejection of such offer of settlement and decision.

(e) Uncontested Offers of Settlement

(1) If a Respondent makes an offer of settlement and the Department of Enforcement of the Exchange does not oppose it, the offer of settlement is uncontested.

(2) If an offer of settlement is uncontested by the Department of Enforcement prior to the issuance of a Complaint pursuant to Rule 10.4, the Department of Enforcement shall transmit the uncontested offer and a proposed decision to the General Counsel of the Exchange with its recommendation.

(A) A proposed decision accepting an offer of settlement shall (i) recite the facts and findings to which Respondent has stipulated in the offer of settlement; (ii) impose sanctions consistent with those to which Respondent has consented in the offer of settlement; and (iii) recite the rule(s), regulation(s), or statutory provision(s) related to such sanctions to which Respondent has consented.

(B) The General Counsel of the Exchange shall accept or reject the offer of settlement and proposed decision.

(C) If the offer of settlement and decision are accepted by the General Counsel of the Exchange, they shall become final and the

Department of Enforcement shall issue the decision and notify the Respondent.

(3) If an offer of settlement is uncontested by the Department of Enforcement after the issuance of a Complaint pursuant to Rule 10.4 but prior to the commencement of a hearing on the merits has begun, the Department of Enforcement shall transmit the uncontested offer and a proposed decision to the General Counsel of the Exchange with its recommendation.

(A) A proposed decision accepting an offer of settlement shall (i) recite the facts and findings to which Respondent has stipulated in the offer of settlement; (ii) impose sanctions consistent with those to which Respondent has consented in the offer of settlement; and (iii) recite the rule(s), regulation(s), or statutory provision(s) related to such sanctions to which Respondent has consented.

(B) The General Counsel of the Exchange shall accept or reject the offer of settlement and proposed decision.

(C) If the offer of settlement and decision are accepted by the General Counsel of the Exchange, they shall become final and the General Counsel of the Exchange shall issue the decision and notify the Department of Enforcement and Respondent.

(4) If an offer of settlement is uncontested by the Department of Enforcement after the issuance of a Complaint pursuant to Rule 10.4 and after a hearing on the merits has begun, the Department of Enforcement shall transmit the uncontested offer of settlement and a proposed decision to the Conduct Panel with its recommendation.

(A) A proposed decision accepting an offer of settlement shall (i) recite the facts and findings to which Respondent has stipulated in the offer of settlement; (ii) impose sanctions consistent with those to which Respondent has consented in the offer of settlement; and (iii) recite the rule(s), regulation(s), or statutory provision(s) related to such sanctions to which Respondent has consented.

(B) The Conduct Panel shall accept or reject the uncontested offer of settlement and the proposed decision.

(C) If the uncontested offer of settlement and decision are accepted by the Conduct Panel, they shall become final and the General Counsel of the Exchange shall issue the decision and notify the Department of Enforcement and Respondent.

(f) Contested Offers of Settlement

(1) If a Respondent makes an offer of settlement and the Department of Enforcement of the Exchange opposes it, the offer of settlement is contested.

(2) A Respondent may not submit a contested offer of settlement for consideration to the EBCC or the Conduct Panel prior to the issuance of a Complaint pursuant to Rule 10.4.

(3) If an offer of settlement is contested by the Department of Enforcement after the issuance of a Complaint pursuant to Rule 10.4 but prior to the commencement of a hearing on the merits has begun, the Department of Enforcement shall transmit the contested offer and a proposed decision to the EBCC with its recommendation.

(A) A proposed decision accepting an offer of settlement shall (i) recite the facts and findings to which Respondent has stipulated in the offer of settlement; (ii) impose sanctions consistent with those to which Respondent has consented in the offer of settlement; and (iii) recite the rule(s), regulation(s), or statutory provision(s) related to such sanctions to which Respondent has consented.

(B) The EBCC shall accept or reject the contested offer of settlement and proposed decision.

(C) If the contested offer of settlement and decision are accepted by the EBCC, they shall become final and the General Counsel of the Exchange shall issue the decision and notify the Department of Enforcement and Respondent.

(4) If an offer of settlement is contested by the Department of Enforcement after the issuance of a Complaint pursuant to Rule 10.4 and after a hearing on the merits has begun, the Department of Enforcement shall transmit the contested offer of settlement and a proposed decision to the Conduct Panel with its recommendation.

(A) A proposed decision accepting an offer of settlement shall (i) recite the facts and findings to which Respondent has stipulated in the offer of settlement; (ii) impose sanctions consistent with those to which Respondent has consented in the offer of settlement; and (iii) recite the rule(s), regulation(s), or statutory provision(s) related to such sanctions to which Respondent has consented.

(B) The Conduct Panel shall accept or reject the contested offer of settlement and the proposed decision.

(C) If the contested offer of settlement and decision are accepted by the Conduct Panel, they shall become final and the General Counsel of the Exchange shall issue the decision and notify the Department of Enforcement and Respondent.

(g) Final Disciplinary Action

(1) A proceeding pursuant to Rule 10.6(e)(2) shall conclude as of the date the decision is issued by the Department of Enforcement. The decision shall constitute final disciplinary action of the Exchange. The sanction(s) shall take effect as set forth in the decision.

(2) A proceeding pursuant to Rule 10.6(e)(3), (e)(4), (f)(3) or (f)(4) shall conclude as of the date the decision is issued by the General Counsel of the Exchange. The decision shall constitute final disciplinary action of the Exchange.

The sanction(s) shall take effect as set forth in the decision.

(h) Rejection of Offer of Settlement

(1) If an uncontested offer of settlement or a decision is rejected by the General Counsel of the Exchange or the Conduct Panel, the Respondent shall be notified in writing and the offer of settlement and proposed decision shall be deemed withdrawn.

(2) If a contested offer of settlement or a decision is rejected by the EBCC or the Conduct Panel, the Respondent shall be notified in writing and the offer of settlement and proposed decision shall be deemed withdrawn.

(3) A rejected offer of settlement or a rejected proposed decision shall not constitute a part of the record in any proceeding against the Respondent making the offer.

(4) As set forth in subsection (d)(1) above, if an offer of settlement or a decision is rejected by the General Counsel of the Exchange, EBCC or the Conduct Panel, the Respondent shall have no right to challenge or contest the rejection of the offer of settlement or the decision before a Conduct Panel, the EBCC, any Board Committee, the Board, the Securities and Exchange Commission, the courts, or any other relevant authority.

(i) Disciplinary Proceeding with Multiple Respondents

When a disciplinary proceeding names multiple Respondents, settlement offers may be accepted or rejected as to any one or all of the Respondents submitting offers. The proceedings shall thereafter be terminated as to those Respondents whose offer of settlements are accepted, but such Respondents may be required to participate in any hearing conducted as to those Respondents that did not submit offers of settlement or whose offers of settlement were rejected.

(j) No Prejudice from Rejected Offer of Settlement

If an offer of settlement is rejected by the General Counsel of the Exchange, EBCC or the Conduct Panel, the Respondent shall not be prejudiced by the offer, which shall not be introduced into evidence in connection with the determination of the issues involved in the pending complaint or in any other proceeding.

(k) Review of Final Disciplinary Actions

(1) The EBCC and the Board Appeals Committee, as defined in PCX Rule 3.3(a)(1), shall review each quarter final disciplinary actions pursuant to Rule 10.6(g) in order to provide the Department of Enforcement and the General Counsel of the Exchange with guidance related to future settlement practices and sanction amounts.

(2) The Board Appeals Committee and the Board shall not have the ability to reject final disciplinary actions pursuant to Rule 10.6.

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