

SR-PCX-2002-28 and should be submitted by July 11, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>23</sup>

Jill M. Peterson,

Assistant Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46071; File No. SR-PCX-2002-27]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the Pacific Exchange, Inc. To Adopt a New Order Modifier Called "Timed Order" and To Adopt a New Interpretation Under PCXE Rules 1.1(r) and 7.37

July 12, 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> notice is hereby given that on May 20, 2002, the Pacific Exchange, Inc. ("PCX") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II and III below, which the PCX has prepared. On June 7, 2002, the PCX filed an amendment to the proposed rule change. The Commission is publishing this notice to solicit comments from interested persons on the proposed rule change, as amended.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The PCX, through its wholly owned subsidiary PCX Equities, Inc. ("PCXE"), proposes to amend its rules governing the Archipelago Exchange ("ArcaEx"), the equities trading facility of PCXE, by: (1) Adopting a new order modifier called a "Timed Order" for use by ETP Holders and Sponsored Participants;<sup>3</sup> (2) amending its interpretation of PCXE Rule 7.37 to clarify the manner in which NOW Orders and Primary Only Orders will be treated on the ArcaEx facility when the routing of such orders to other market centers or market participants is required; (3) clarifying its definition of "Indicative Match Price" as it relates to

the opening auctions; and (4) making several minor technical rule changes to correct grammatical or typographical errors. The text of the proposed rule change is as follows:

#### Text of the Proposed Rule Change<sup>4</sup>

##### Rule 1—Definitions

##### Rules 1.1(a)–(q)—No change.

##### Indicative Match Price

(r) For the purposes of the Opening Auction, the Market Order Auction and the Trading Halt Auction, as the case may be, the term "Indicative Match Price" shall mean for each security (1) the 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 Trading Halt Auction, the last sale during normal market hours*), as determined by the Consolidated Tape *will establish the opening price, 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.*

(s)–(aaa)—No change.

##### Rule 7—Equities Trading

##### Cancellation of [Revisions in] Transactions

Rule 7.10—No change.

##### Short Sales

Rule 7.16(a)–(c)—No change.

(d) Exceptions. The provisions of subsection (a) hereof shall not apply to: (1)–(8)—No change.

(9) Any sale by an underwriter, or any member of a syndicate or group participating in the distribution of a security, in connection with an over-allotment of securities, or any lay-off sale by such a person in connection with a distribution of securities through rights or a standby underwriting commitment[.]; or

(10)—No change.

(e)–(f)—No change.

##### Orders and Modifiers

Rule 7.31(a)–(p)—No change.

(q) *Timed Order. A limit order to buy or sell that is to remain in effect until a specified time, after which such order*

*or the portion thereof not executed is to be treated as cancelled. The specified time interval of such order may remain in effect for one or more consecutive trading sessions for that particular day only.* [Reserved.]

(r)–(x)—No change.

##### Opening Session Auctions

Rule 7.35(a)–(d)—No change.

##### (e) Transition to Core Trading Session.

(1)—No change.

(2) Market orders entered after 6:28 am (Pacific Time) and before 6:30 am (Pacific Time), which are eligible for either the Market Order Auction or the Core Trading Session, shall become eligible for execution at 6:30 am (Pacific Time) or at the conclusion of the Market Order Auction, whichever is later, unless otherwise provided in Rule 7.35 [7.30](c)(2)(C).

(3)—No change.

(f)—No change.

##### Order Execution

Rule 7.37. Subject to the restrictions on short sales under Rule 10a-1 under the Exchange Act, like-priced orders, bids and offers shall be matched for execution by following Steps 1 through 5 in this Rule; provided, however, for an execution to occur in any Order Process, the price must be equal to or better than the NBBO, unless the Archipelago Exchange has routed orders to [all] away markets at the NBBO, *where applicable (however, a User may submit a NOW Order or Primary Only Order that may be routed to an away market without consideration of the NBBO).*

(a)–(e)—No change.

#### 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 had 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

On October 25, 2001, the Commission approved the PCX's proposal to

<sup>23</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> A "Sponsored Participant" means "a person which has entered into a sponsorship arrangement with a Sponsored ETP Holder pursuant to [PCXE] Rule 7.29." See PCXE Rule 1.1(tt).

<sup>4</sup> New text is italicized and deleted text is in brackets.

establish ArcaEx as a new electronic trading facility of PCXE.<sup>5</sup> ArcaEx is a fully electronic securities trading facility for use by ETP Holders and their customers. PCX and PCXE are responsible for all regulatory functions related to the facility, and Archipelago Exchange, L.L.C., a subsidiary of Archipelago Holdings, L.L.C., is responsible for the business of the facility to the extent that these activities are not inconsistent with the regulatory and oversight functions of PCX and PCXE. ArcaEx commenced operations on March 22, 2002, replacing the PCXE's traditional trading floor facilities.

### 1. Timed Order Modifier

As part of its continuing effort to enhance participation in its electronic auction market, the PCX proposes to adopt a new order modifier, called a "Timed Order," for use by ETP Holders and Sponsored Participants (collectively "Users") on ArcaEx. The PCX proposes to add PCXE Rule 7.31(q) to define a Timed Order. A Timed Order is a limit order to buy or sell that is to remain in effect until a specified time, after which the order or the portion thereof not executed is to be treated as cancelled. The specified time interval of the order may remain in effect for one or more consecutive trading sessions for that particular day only.<sup>6</sup>

The PCX believes that the Timed Order modifier would enable a User to implement its own customized means for accomplishing the order execution. This modifier would be an enhanced alternative to a traditional day order in that a shorter time interval could be specified for the order to remain in effect, and Users would be able to specify in advance when to cancel their outstanding orders. In the PCX's view, this would afford Users more flexibility in applying their trading strategies. Accordingly, the PCX believes that the proposed rule would promote a more efficient and effective market operation, and would enhance the investment choices available to investors over a broad range of trading scenarios.

### 2. NOW and Primary Only Orders

The PCX's current rules governing the order execution processes for orders in the ArcaEx Book<sup>7</sup> are set forth in PCXE

Rule 7.37. The proposed rule change provides a clarification of PCXE Rule 7.37 as to the manner in which NOW Orders and Primary Only Orders ("PO Orders") would be treated through ArcaEx's trading system when the routing of those orders to other market centers or market participants is required. The first paragraph of PCXE Rule 7.37 states that "[s]ubject to the restrictions on short sales under Rule 10a-1 under the Exchange Act, like-priced orders, bids, and offers shall be matched for execution by following Steps 1 through 5 in this Rule; provided, however, for an execution to occur in any Order Process, the price must be equal to or better than the NBBO, unless the Archipelago Exchange has routed orders to all away markets at the NBBO." With this filing, the PCX is proposing to add interpretive language to make it clear that a User may submit a NOW Order or PO Order that may be routed away to other markets without consideration of the NBBO. The PCX believes that this interpretation is fairly implied in its rules that define these order types and the terms of the ArcaEx Approval Order.

ArcaEx has been designed to provide its Users with a choice as to how they wish to route their orders to away markets. This includes NOW Orders and PO Orders, as discussed below. Under PCXE Rule 7.31(v), a NOW Order is a Limited Price Order<sup>8</sup> that is executed in whole or in part on the ArcaEx, and the portion not so executed is routed pursuant to Rule 7.37(d)<sup>9</sup> to one or more NOW Recipients for immediate execution when received. If a NOW Order is not marketable when submitted to ArcaEx, it is cancelled. Similarly, any portion of the order that the NOW Recipient does not immediately execute is cancelled. NOW Orders may not be Directed Orders.<sup>10</sup> For purposes of a NOW Order, a NOW Recipient means any exchange, ECN or other broker-dealer (i) with which ArcaEx maintains an electronic linkage, including ITS,

divided into four components, called processes—the directed order process, the display order process, the working order process, and the tracking order process. See PCXE Rule 7.37 for a detailed description of these order execution processes.

<sup>8</sup> See PCXE Rule 1.1(s) ("Limited Price Order" is defined as any order with a specified price or prices (e.g., limit orders and working orders, other than stop orders).

<sup>9</sup> The routing order process is the fifth step of the ArcaEx execution algorithm, which involves routing orders away to other market centers or market participants and is available only to those ETP Holders who have entered into a Routing Agreement. See PCXE Rule 7.37(d) (description of "routing order process").

<sup>10</sup> See PCXE Rule 7.31(i) (definition of "directed order"). See also PCXE Rule 7.37(a) (description of "directed order process").

and (ii) which provides instantaneous responses to NOW Orders routed from ArcaEx. The PCXE designates from time to time those exchanges, ECNs, or other broker-dealers that qualify as NOW Recipients.<sup>11</sup>

Similarly, a PO Order modifier enables Users to implement their own customized means for accomplishing the order execution. As defined in Rule 7.31(x), a PO Order is a market order, for exchange-listed securities only, that is to be routed as a market-on-open order to the designated primary market for participation in the primary market opening or re-opening process. A PO Order bypasses the order-execution processes of the ArcaEx Book and is routed directly to the designated primary market.

The PCX believes that the NOW and PO order types involve a routing element unique to ArcaEx. These specific orders types allow a User's instructions to take precedence over the general requirement that orders will be routed to away markets at the NBBO. The PCX believes that it is implicit in the current definitions of these alternative order types that they will be processed in a manner consistent with the User's instructions and, therefore, the order may have to be routed to away markets that are not quoting at the NBBO.

### 3. Indicative Match Price

ArcaEx operates two auctions during its Opening Session—the Opening Auction and the Market Order Auction. Also, to facilitate the re-opening of a security following a trading halt in that security, ArcaEx will conduct a Trading Halt Auction.<sup>12</sup> The term "Indicative Match Price" is applicable to these auctions and is defined in Rule 1.1(r) to mean "for each security (1) the 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, as determined by the Consolidated Tape." The PCX proposes to amend the definition of the term "Indicative Match Price" to clarify the process that establishes a single price opening when there are two or more prices at which the maximum volume of shares are executable.

Currently, PCXE Rule 1.1(r) provides that if there are two or more prices at which the maximum volume of shares

<sup>11</sup> See PCXE Rule 1.1(ff) (definition of "NOW Recipient").

<sup>12</sup> See PCXE Rule 7.35 for a discussion of the Opening Session Auctions and the Trading Halt Auction.

<sup>5</sup> See Securities Exchange Act Release No. 44983 (October 25, 2001), 66 FR 55225 (November 1, 2001) (SR-PCX-00-25) (hereinafter "ArcaEx Approval Order").

<sup>6</sup> See PCXE Rule 7.34(a) for a description of ArcaEx's trading sessions.

<sup>7</sup> ArcaEx maintains an electronic file of orders, called the ArcaEx Book, through which orders are displayed and matched. The ArcaEx Book is

are executable, the price that is closest to the closing price of the previous day's normal trading hours will be used to establish the opening price. Since this language may be interpreted to mean that the opening trade for the subject auction may occur at a price that trades through eligible limited price orders residing in the ArcaEx Book, and since such an interpretation would be inconsistent with the PCX's priority rules as set forth in PCXE Rule 7.36(a), the PCX proposes to add interpretive language to its definition of Indicative Match Price. The proposed language would make it explicit that when 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 day's normal trading hours would be used to establish the opening price, provided that if the price would trade through an eligible limited price order designated for that auction, then the opening price would occur at the best price level available where no trade through occurs. The PCX is also proposing to modify PCXE Rule 1.1(r) by adding a parenthetical statement to clarify that, in the case of a Trading Halt Auction, the last sale during normal market hours will be used for purposes of determining the opening price.

The PCX believes that the proposed rule change will more accurately reflect ArcaEx's current opening price methodology, and that it is consistent with PCXE's price-time priority rules. Accordingly, the ArcaEx system is designed to ensure that limited price orders residing in the Arca Book will be executed in strict price-time priority, and that those orders will be afforded trade-through protection.

#### 4. Technical Changes

The PCX proposes to make the following minor technical rule changes to correct grammatical or typographical errors:

(a) *Rule 7.10*—"Cancellation of Transactions" is replacing the heading entitled "Cancellation of Revisions in Transactions."

(b) *Rule 7.16(c)(9)*—A semi-colon and the word "or" will be inserted after the first sentence.

(c) *Rule 7.35(e)*—The rule cross-referenced in the text will be changed from *Rule 7.30(c)(2)(C)* to *7.35(c)(2)(C)*.

The PCX believes that the proposed rule change is consistent with Section 6(b)<sup>13</sup> of the Act, in general, and furthers the objectives of Section 6(b)(5),<sup>14</sup> in particular, because it is

designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and 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 provided the Commission with written notice of its intention to file the proposed rule change at least five business days before its filing. Moreover, the PCX has designated the proposed rule change as one that: (i) Does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; and (iii) does not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate. Therefore, the foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>15</sup> and Rule 19b-4(f)(6) thereunder.<sup>16</sup> At any time within 60 days of the filing of Amendment No. 1 to the proposed rule change, the Commission may summarily abrogate the rule change if it appears to the Commission that the action is necessary or appropriate in the public interest, for the protection of investors, or would otherwise further the purposes of the Act.

Under Rule 19b-4(f)(6)(iii) under the Act,<sup>17</sup> the proposal does not become operative for 30 days after the date of its filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest. The PCX has requested that the Commission waive the 30-day operative date so that the PCX can implement the proposed rule change as

quickly as possible. The Commission, consistent with the protection of investors and the public interest, has determined to waive the 30-day operative period.<sup>18</sup>

#### **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. 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 the 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-2002-27 and should be submitted by July 11, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>19</sup>

**Jill M. Peterson,**

*Assistant Secretary.*

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#### **SMALL BUSINESS ADMINISTRATION**

##### **[Declaration of Disaster #3421]**

##### **State of California**

Los Angeles County and the contiguous counties of Kern, Orange, San Bernardino, and Ventura in the State of California constitute a disaster area as a result of damages caused by an explosion and fire that occurred May 24, 2002 at the Park Encino apartment complex in Encino. Applications for loans for physical damage as a result of this disaster may be filed until the close of business on August 12, 2002 and for economic injury until the close of business on March 13, 2003 at the

<sup>18</sup> For purposes of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>19</sup> 17 CFR 200.30-3(a)(12).

<sup>13</sup> 15 U.S.C. 78f(b).

<sup>14</sup> 15 U.S.C. 78f(b)(5).

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

<sup>16</sup> 17 CFR 240.19b-4(f)(6).

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