



RULE  
ADOPTION  
NOTICE

**RAN-03-30**  
**November 6, 2003**

**TO: All PCX Members and Member Organizations**

**FROM: Department of Regulatory Policy**

**SUBJECT: PCX Plus Housekeeping Changes to Options Trading Rules  
(File No. SR-PCX-2003-31)**

On July 8, 2003, the Exchange filed with the Securities and Exchange Commission a proposed rule change to clarify existing provisions, eliminate superfluous provisions, re-number rules where appropriate, and to otherwise update the rules to conform with PCX Plus. The Exchange filed Amendment Nos. 1 and 2 to the proposed rule change on September 10, 2003 and September 24, 2003, respectively. The Commission approved the rule proposal on October 31, 2003, as amended.

The following is the text of the rule changes. Questions regarding this bulletin may be directed to Tania Cho at (415) 393-4107.

## **EXHIBIT A**

### **PACIFIC EXCHANGE, INC.**

#### **RULES OF THE BOARD OF GOVERNORS**

##### **Text of the Proposed Rule Change:<sup>1</sup>**

###### **Rule 6 Options Trading**

\* \* \*

###### **¶ 4889 Fast Markets and Unusual Market Conditions**

Rule 6.28(a) – No change.

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<sup>1</sup> New text is underscored; deleted text is in brackets.

(b)(1) – (4) – No change.

(5) Market Makers will be required to trade a minimum of one contract based on quoted markets, pursuant to Rule 6.37[(f)], Commentary .05.

(6) – No change.

(c) – (d) – No change.

**¶ 4905 Market Maker Defined**

Rule 6.32(a) – (d) – No change.

(e) With regard to orders of Market Makers entered from off the floor that are not entitled to special margin treatment pursuant to subsections (c) and (d), above, Market Maker clearing firms are directed to instruct their respective trading desks to identify such [their] orders [as entered from off the floor] by placing a "C" after the Market Maker's number in the "firm" box on the ticket. Floor Brokers, when accepting an order by phone from a Market Maker, are similarly directed to identify such [that] orders in the same manner.

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**¶ 4923 Appointment of Market Makers**

Rule 6.35(a). On a form or forms prescribed by the Exchange, a registered Market Maker must [shall] apply for a Primary Appointment, having the obligations hereunder, and of Rule 6.37[(b)], in one or more classes of option contracts.

[(b) – (f) – Reserved.]

(b) The Options Allocation Committee will [shall] ordinarily appoint a minimum of one or up to a maximum of six posts on the Options Trading Floor to each registered Market Maker, [as his Primary Appointment.] In making such Primary Appointments, the Committee may consider: [shall give attention to]

(1)[(a)] the preference of the applicant;

(2)[(b)] the maintenance and enhancement of competition among Market Makers in each class of option contracts;

(3)[(c)] assuring that the financial resources available to the applicant are sufficient for satisfying [enable him to satisfy] the obligations set forth in Rule 6.37 with respect to each class of option contracts to which the applicant [he] is appointed; and

(4)[(d)] the applicant's prior performance as a Market Maker.

(c) A Market Maker may request [select] a minimum of one post or up to a maximum of six contiguous posts to comprise his Primary Appointment Zone. The Committee may appoint more than six posts or non-contiguous posts in the existence of special circumstances.

(d) Newly registered Market Makers [shall] have a grace period (60 days from the commencement of trading[,]) during which time they may have, but are not required to have, [he shall not have] a Primary Appointment Zone[)]. Prior to [At] the completion of the grace period, the Market Maker must select a Primary Appointment Zone. Market Makers who fail to select a Primary Appointment Zone prior to the expiration of their grace periods will be subject to disciplinary action pursuant to Rule 10.13. [Committee shall provide the Market Maker with a list of Primary Appointments Zones from which to choose. The new Market Maker shall trade in that Primary Appointment Zone for a period of 90 calendar days. At the completion of the 90 days period, the Market Maker may apply for the Primary Appointment Zone of his choice.]

(e) Requests for new or changes in Primary Appointment Zones will [shall] be reviewed by the Committee. The Committee may suspend, terminate or change any Primary Appointment of a Market Maker under this Rule, and may appoint a Market Maker to additional classes of option contracts whenever, in the Committee's judgment, the interests of a fair and orderly market are best served by such action.

No Primary Appointment of a Market Maker shall be made without the Market Maker's consent to such appointment, however, refusal to accept a Primary Appointment may be deemed a sufficient cause for termination or suspension of a Market Maker's registration.

A member or prospective member adversely affected by a determination of the Committee under this Rule may obtain a review by the Board of Governors of such determination.

(f) Primary Appointment Trading Requirement.<sup>2</sup> Except in unusual circumstances, at least 75% of the trading activity of a Market Maker (measured in terms of contract volume per quarter) must be in classes of option contracts to which that Market Maker's Primary Appointment extends. In computing the percentage specified herein, a weighting factor may be assigned based upon relative inactivity of one or more classes or series of option contracts.

(g) – (i) – No change.

*Commentary:*

.01 – .02 – No change.

.03 Reserved. [Except in unusual circumstances, at least 75% of the trading activity of a Market Maker (measured in terms of contract volume per quarter) shall be in classes of option contracts to which his Primary Appointment extends. In computing the percentage specified

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<sup>2</sup> Former Rule 6.35, Commentary .03 is being renumbered as new Rule 6.35(f).

herein, a weighting factor may be assigned based upon relative inactivity of one or more classes or series of option contracts.]

.04 – .05 – No change.

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#### ¶4929

#### Letters of Guarantee

Rule 6.36(a) – (c) – No change.

(d) FLEX Options. Market Makers may not effect transactions in FLEX Options unless one or more Letter(s) of Guarantee on behalf of such Market Makers has been issued by a Clearing Member in accordance with Rule 8.115(a).

*Commentary:*

.01 When a M[m]arket M[m]aker is subject to a written interim notice of revocation and open positions remain in a Market Maker Account, held by such M[m]arket M[m]aker, closing transactions only may be effected for such account for the period between the effective date of the written interim notice of revocation and the effective date of the final notice of revocation required by subsection [paragraph] (c) of this Rule. [section.]

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#### ¶4935

#### Obligations of Market Makers

Rule 6.37(a) – (b) – No change.

*(c) In Classes of Option Contracts Other Than Those to Which Appointed.* With respect to classes of option contracts other than those to which their [his] Primary Appointments extend[s], pursuant to Rule 6.35 [a] Market Makers should not engage in transactions for an account in which they have [he has] an interest that [which] are disproportionate in relation to, or in derogation of, the performance of their [his] obligations as specified in paragraph (b) of this Rule [section] with respect to those classes of option contracts to which their [his] appointments do [does] extend. Whenever [a] Market Makers enter[s] the trading crowd for a class of options in which they do [he does] not hold a Primary Appointment in other than a floor brokerage capacity, they must [he shall] fulfill the obligations established by paragraph (b) of this Rule [section]. In addition, when present anywhere on the Options Trading Floor, with regard to all securities traded on the Trading Floor, [a] Market Makers are [is] expected to undertake the obligations specified in paragraph (b) of this Rule [Section] in response to a demand therefore [therefore] from the Order Book Official that the performance of such obligations by other Market Makers requires [required] supplementation. Furthermore, Market Makers should not:

(1) – (4) – No change.

(d) – (g) – No change.

(h) Obligations of Remote Market Makers

(1) All PCX Rules applicable to Market Makers will also apply to Remote Market Makers unless otherwise provided or unless the context clearly indicates otherwise. The following Rules do not apply to Remote Market Makers who are not present on the Trading Floor: Rule 6.2(b) – (f) and (h) (Admission to and Conduct on the Options Trading Floor); Rule 6.35(a) – (e) (Appointment of Market Makers); Rule 6.37(d) and Commentaries .03 and .05 (Obligations of Market Makers); Rule 6.53, Commentary .01 (Issuing a Call for Market Makers); Rule 6.66 (Order Identification); Rule 6.73 (Manner of Bidding and Offering); Rule 6.74 (Bid and Offers in Relation to Units of Trading); and Rule 6.100 (Evaluation of Options Trading Crowd Performance).

(2) – No change.

(3) Each Remote Market Maker must meet its quoting obligations as set forth in Rules 6.35(h)(2) and 6.37(g). A failure to comply with the 60% quoting requirement may result in a fine pursuant to Rule 10.13; however, if aggravating circumstances are present, formal disciplinary action may be taken pursuant to Rule 10.4. The Exchange may consider exceptions to this quoting requirement based on demonstrated legal or regulatory requirements or other mitigating circumstances (e.g., excused leaves of absence, personal emergencies, or equipment problems).

(4) – No change.

(5) Remote Market Makers must trade at least 75% of their average daily trading volume per quarter in issues included in their primary appointments pursuant to Rules 6.35(g) and 6.35(h)(2). Remote Market Makers may trade up to 25% of their quarterly contract volume in option issues that are not included within their primary appointments. Remote Market Makers may not enter two-sided quotations in option issues that are not included within their primary appointments.

(6) – (7) – No change.

*Commentary:*

.01 The limitations of [paragraph] Rule 6.37(b)(2) [of this Section] should not be carried over from one day to the next, and therefore are not applicable to the Exchange's opening.

.02 The bid-ask differentials as stated in paragraph (b)(1) of Rule 6.37 shall apply to all option series open for trading in each option class.

.03 – .08 – No change.

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**¶4941                      Restriction on Acting as Market Maker and Floor Broker**

Rule 6.38(a) Application

(1) – (2) – No change.

(b) Restrictions

(1)-(3) – No change.

(4) Members who wish to apply for the privilege of acting in the capacity of both a Market Maker and Floor Broker must apply for and receive approval from [through] the Options Allocation [Appointments] Committee.

(5) – No change.

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**ORDER BOOK OFFICIALS**

**¶5003                      Order Book Official Defined**

**Obligations for Orders**

Rule 6.52(a) – (d) – No change.

*Commentary:*

.01 – .02 – No change.

.03 For purposes of this Rule, an order shall be deemed to be from a member if the order is placed with an Order Book Official by a person associated with a member (e.g., a clerk or a runner), provided that the order is either (i) an order to buy at a price equal to or below the highest bid in the Order Book Official's book or (ii) an order to sell at a price equal to or above the lowest offer in the Order Book Official's book. These conditions will not be applicable when a person associated with a member is placing a cancel/replace (CFO) with the Book.

[It is the purpose of this interpretation to clarify that an Order Book Official may accept orders from persons associated with members, i.e. clerks, runners or other associated persons, except when the order is one which improves the existing best bid or offer in the book, in which case, unless the order is a CFO, the direct involvement of a member will be required.]

.04 – .05 – No change.

¶ 5181

**Lead Market Makers**

Rule 6.82(a) – No change.

(b) Qualification of Lead Market Makers

(1) – (2) – No change.

(3) *Resignation of LMMs.* An LMM, interim LMM or back-up LMM [or alternate LMM] who fails to give a ten-day written notice of resignation to the Exchange may be subject to formal disciplinary action pursuant to Article XI, Section 2(a) of the Exchange Constitution.

(4) – No change.

(c) Obligations of Lead Market Makers.

Each LMM must meet the following obligations:

(1) – (2) – No change.

(3) [Determine any formula for generating the] Generate and automatically update two-sided [updated] market quotations with size in all appointed series either through the Exchange's auto-quoting system or through the LMM's own proprietary autoquoting system;

(4) – No change.

(5) Be present at the trading post throughout every business day and, in addition, designate an approved LMM to act as a back-up [substitute] LMM and notify Book Staff of such designation;

(6) – (14) – No change.

(d) – (h) – No change.

*Commentary:*

.01 - .03 – No change.

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**Joint Accounts**

Rule 6.84(a) – (c) – No change.

(d) Each participant in a joint account must file with the Exchange [Member Services Department] and thereafter keep current a completed application on a form prescribed by the Exchange.

(e) – No change.

(f) Joint [A]account[s] participants may not [shall not be permitted to] enter: (1) opening option transactions from off the Floor for the joint account in option contracts listed on the Exchange (unless otherwise permitted by Exchange Rules); (2) [any] transactions for option contracts not listed on the Exchange; and (3) transactions for any other security. This prohibition does [shall]not apply to transactions entered for securities underlying Exchange option contracts in the joint account.

(g) [A joint account which acts in the capacity of a] Individual Market Makers trading for a joint account must [shall not be required to] have a primary appointment, but the joint account itself is not required to have a primary appointment.

(h) – No change.

*Commentary:*

.01 – .03 – No change.

.04 Any order of a joint account participant[,] that [which] is executed by a Floor Broker[,] must [shall] be in accordance with the procedures set forth in Rule 6.85, except that the joint account trading number with its alpha identification must [should] appear in the “executing firm” area. Additionally, a joint account may not bid, offer, purchase, sell, or enter orders in an option series in which a Floor Broker holds an order on behalf of the joint account or for the proprietary account of another participant in the joint account. Orders of joint account participants in a particular option series may not be concurrently represented[,] by one or more Floor Brokers.

.05 – .07 – No change.

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## **Intermarket Linkage**

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### **Definitions**

Rule 6.92(a)(1) – (6) – No change.

(7) “Eligible Market Maker,” with respect to an Eligible Option Class, means a market maker that:

(i) is assigned to, and is providing two-sided quotations in, the Eligible Option Class;

(ii) is logged on to participate in Auto-Ex or PCX Plus in such Eligible Option Class; and

(iii) is in compliance with the requirements of Rule 6.95 (relating to limitation or principal order access).

(8) – (21) – No change.

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### **Options Floor Procedure Advices**

#### **Conduct of Market Makers**

**[B-4**

#### **Subject: Market Maker Trading on the PCX Equity Floors**

Rule 6.36 provides that no Market Maker shall make any transaction on the Floor of the Exchange unless there is in effect a Letter of Guarantee which has been issued for each member by a Clearing Member. Moreover, Rule 6.66 provides that for each transaction in which he participates, the member must immediately give up the name of the Clearing Member through whom the transaction will be cleared.

Market Makers are reminded that analogous requirements must be met when executing principal trades on the Equity Trading Floors and that a Market Maker not associated with a Clearing Member of Pacific Clearing Corporation must give up the symbol of a Clearing Member in each such transaction. Accordingly, prior to granting such Market Maker member access to the Equity Trading Floors, they will be required to have on file with the Exchange a Clearing Letter of Guarantee and Authorization issued by a Clearing Member of PCX who undertakes to authorize and guarantee such equity trades. Such Letter of Guarantee will be in the following form:

The undersigned corporation, a clearing participant in Pacific Clearing Corporation (“PCC”) and a member of the Pacific Stock Exchange Incorporated (“PCX”) hereby authorizes \_\_\_\_\_, a member organization of PCX, and any members of PCX associated with such member organization to give up the undersigned’s name as the party responsible for clearance and settlement in connection with all trades executed as principal or as agent by such member organization, any officer or employee thereof, or any member of PCX affiliated therewith on the Equity Trading Floors of PCX. The undersigned assumes full financial responsibility for clearance and settlement of all trades executed by such member organization, any officer or employee thereof, or any member of PCX affiliated herewith on the Equity Trading Floors of PCX if the undersigned’s name was given up in connection with such trade. This commitment

by the undersigned is for the specific benefit of the Pacific Clearing Corporation and any member or member organization with which \_\_\_\_\_ effects a trade on the Equity Trading Floors of PCX.

This Clearing Letter of Authorization and Guarantee shall remain in effect until a written notice of revocation has been filed with the Exchange and posted on the bulletin board of the Equity Trading Floors of PCX in both Los Angeles and San Francisco.

If such written Notice has not been posted for at least one hour prior to the opening of trading on a particular business day, such revocation shall not become effective until the close of trading on such day. A revocation shall in no way relieve the undersigned from responsibility for transactions guaranteed prior to the effective date of such revocation.

Dated: \_\_\_\_\_

\_\_\_\_\_  
A Clearing Participant

Accepted:  
PACIFIC CLEARING CORPORATION

By: \_\_\_\_\_  
Its: \_\_\_\_\_ ]

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