



RULE
ADOPTION
NOTICE

RAN-04-47
October 21, 2004

TO: All PCX OTP Holders and OTP Firms

FROM: Department of Regulatory Policy

**SUBJECT: Facilitation Crossing Rule
(File No. SR-PCX-2003-64)**

The SEC has approved the following rule change regarding the facilitation crossing rule and the Exchange will make it operative on Friday, October 29, 2004.

The following is the text of the rule change. Questions regarding this bulletin may be directed to Mai Shiver at (415) 393-4266.

Overview:

A Facilitation Procedure is a defined term under PCX Rule 6.47 and provides that, when a Floor Broker who holds a Customer Order and an order for the propriety account of an OTP Holder or OTP Firm or an organization under common control with an OTP Firm Market Maker (collectively, Facilitation Firm), for 50 contracts or more, the Floor Broker may cross the order by following the Facilitation Procedure outlined in the rule.

1. Facilitation Procedure in Summary:

- The Floor Broker receives an order/interest from a Facilitating Firm holding a Customer Order that the Facilitating Firm seeks to cross.
- The Floor Broker may enter the crowd and make an informal query to determine whether the facilitation cross might be achieved on the floor.
- Either following an informal query, or without one, the Floor Broker may make a formal request for a market by requesting all bids and offers for all components of the Customer Order including size. The Floor Broker need not request a facilitation market.

- The trading crowd will be given a reasonable period of time to provide a quote. For the purposes of this rule, the Exchange interprets reasonable as 3 seconds for simple crosses and 60 seconds for complex crosses. The trading crowd's quote remains in effect for such time as necessary for the Floor Broker to respond/vocalize the Customer Order, but in no event remains in effect if the Floor Broker leaves the crowd.
- If the trading crowd's bid or offer is outside that of the Facilitation Price, the Floor Broker will announce the bid (offer) of the Customer Order and offer (bid) of the Facilitating Firm. At that time, the Customer Order is deemed executed.
- The trading crowd may then, within a reasonable period of time determined generally to be no longer than 3 seconds, bid (offer) at the Facilitation Price in order to execute up to 60% of the trade against the Customer Order. After the trading crowd has provided its bid (offer) within the prescribed period, the Floor Broker may execute up to 40% of the trade against the Customer Order.
- The remainder of the order will be allocated equally to those members of the trading crowd who bid (offered) at the Facilitation Price.
- If the trading crowd does not provide a bid (offer) at the Facilitation Price, or if it chooses to collectively execute less than 60% of the total trade against the Customer Order, the Floor Broker, on behalf of the Facilitation Firm, will fill the remainder of the Customer Order.
- If the trading crowd provides a bid or offer that is superior to that of the Facilitation Price, then the trading crowd may satisfy the Customer Order at that improved price and the Floor Broker will be given an opportunity to improve its price to join the crowd for up to 40% of the order. The allocation of the trade will be made on a size pro rata basis to those individuals in the trading crowd whose bid (offer) improved the Facilitation Price.
- Consistent with the above, the allocation of the trading crowd's percentage will be based upon certain factors. If the trading crowd joins in at the Facilitation Price, then all members of the trading crowd bidding and offering at the Facilitation Price will have an equal allocation of the order. If the trading crowd improves the price, then the allocation of the trading crowd's share of the order will be made on a size pro rata basis depending upon the size that each member of the trading crowd bidding or offering at the improved price provided in response for a market.

2. General Considerations Pursuant to the Facilitation Procedure:

- Customer Orders will always be filled if they are priced at or between the quoted bid or offer.

- The Facilitating Firm (through the Floor Broker) will always get at least 40% of the trade that is at or between the quoted bid or offer.
- Customer Orders may never get filled outside of the Exchange’s disseminated market at the time of a request for a market.
- The trading crowd may get as much as 60% by quoting at the Facilitation Price or may get more than 60% if improves the market and the Facilitation Firm, through the Floor Broker, does not join in the improved market.
- A trading crowd bid or offer for a size collectively less than the size of the facilitation order will be treated as though the trading crowd did not provide a bid or offer at all.
- The Floor Broker must first satisfy the orders for the account of persons who are not OTP Holders or OTP Firms of the Exchange pending at the facilitation price. The remaining part of the order (net) is subject to the allocation analysis (below).
- For the purpose of the Facilitation Procedure, the LMM will be treated as any member of the crowd except under the following circumstance: if the Facilitating Firm (acting through the Floor Broker) chooses to take less than the 40% of the order to which it is entitled, then the LMM who is bidding or offering at the Facilitation Price may choose to take either (i) its share of the trading crowd’s allocation as described below, or (ii) the difference between 40% of the order minus the amount of the order that the Facilitation Firm (acting through the Floor Broker) chooses to take.
- It will be a violation of the Floor broker’s duty to use due diligence in representing its Customer Order if a Floor Broker does not employ the Facilitation Procedure on the PCX immediately upon receipt on the PCX of the order that the OTP Holder or OTP firm wishes to have executed as a facilitations cross. It will also be a violation of the OTP Holder or OTP Firm’s duty of best execution to its customer if it were to cancel a facilitation order in order to avoid execution of the order at a better price.

3. Examples

Exchange Disseminated Market	Trading Crowd bid or offer with collective size equal or greater than the size of the facilitation order	Facilitation Price	Allocation net of the component of the order
1.00 – 1.20	1.00 – 1.20	1.10 customer order to buy 500 facilitated by facilitation firm offering to sell at 1.10	Customer order filled; Facilitating firm gets 40% minimum; Crowd may participate at 1.10 and get an equal allocation of the remaining 60% of the order.

1.00 – 1.20	1.05 – 1.15	1.10 customer order to buy 500 facilitated by facilitation firm offering to sell at 1.10	Customer order filled; Facilitating firm gets 40% minimum; Crowd may participate at 1.10 and get an equal allocation of the remaining 60% of the order.
1.00 – 1.20	1.05 buy at 1.10 sell	1.10 customer order to buy 500 facilitated by facilitation firm offering to sell at 1.10	Customer order filled; Facilitating firm gets 40% minimum. Crowd may participate at 1.10 and get a pro rata allocation depending upon initial quote with size order
1.00 – 1.20	1.00 – 1.05	1.10 customer order to buy 500 facilitated by facilitation firm offering to sell at 1.10	Customer Order filled at 1.05; facilitating firm, via floor broker, could agree to accept 40% at 1.05. Otherwise, the trading crowd gets 100% of the trade at 1.05.
1.00 – 1.20		1.10 customer order to buy 500 facilitated by facilitation firm offering to sell at 1.10	Customer order filled; Facilitating firm gets 40% minimum; Crowd may participate at 1.10 and get an equal allocation of the remaining 60% of the order.

Exhibit A
Text of the Rule Change:

**Rules of the Board of Governors
of the
Pacific Exchange, Inc.**

Rule 6
Options Trading

"Crossing" Orders and Stock/Option Orders

Rule 6.47.

(a) – No change.

(b) *Facilitation Procedure.* The Facilitation Procedure is a process by which a Floor Broker who holds an order for a customer (“Customer Order”) and an order for the proprietary account of an OTP Holder or OTP Firm or an organization under common control with a Market Maker that is representing that customer (the “Facilitation Order”) may cross those orders. The Floor Broker may do so by following the Facilitation Procedure outlined in this subsection (b) of this Rule. The Floor Broker must be willing to facilitate the entire size of the Customer Order entered via the Facilitation Procedure.

(1) The size of the Customer Order subject to facilitation must be at least fifty contracts. Orders for less than fifty contracts may be facilitated pursuant to this rule but are not subject to the firm guarantees of subsections (4) through (6) of this Rule and therefore a Floor Broker must satisfy all orders in the book and orders represented in the trading crowd (affording the trading crowd a reasonable period of time to respond) before the Floor Broker may cross the order.

(2) The option order tickets for both the Facilitation Order and the Customer Order must display all of the terms of such orders, including any contingencies involving, and all related transactions in, either options or underlying or related securities. The Floor Broker must disclose all securities that are components of the Customer Order.

(3) The Floor Broker must request bids and offers for all components of the Customer Order, including the size of the order, but does not have to specifically request a “facilitation market.” Once the trading crowd has been afforded a reasonable time to provide a quote, the quote will remain in effect only for such time as is necessary for the Floor Broker to immediately vocalize the Customer Order.

(4) In response to the trading crowd’s quoted market, the Floor Broker may immediately consummate the facilitation cross if: (i) he or she immediately bids (offers) a

price on the Customer Order that is on or inside the quoted market (“Facilitation Price”) provided by the trading crowd in response to the Floor Broker’s request for a market and (ii) satisfies all other contingencies associated with the Customer Order. After satisfying any orders for the account of persons who are not OTP Holders or OTP Firms of the Exchange pending at the Facilitation Price, the Floor Broker may facilitate up to forty percent (40%) of the remaining Customer Order against the Facilitation Order at the Facilitation Price and must allow any other members of the trading crowd interested in trading at the facilitation price to execute the remaining sixty percent (60%) or more of the Customer Order. The allocation of the remaining Customer Order will be made on a (i) size pro-rata basis (the percentage of the orders that is the ratio of the size of the offers (bids) to the total size of the offers (bids) as described in 6.75(f)(6)); or (ii) equal basis (in the case of identical offers (bids)) as described in PCX Rule 6.75(c) where the floor broker’s bid (offer) improved the crowd’s price in response to the request for a market. If after providing the crowd reasonable time to execute the remaining 60% of the Customer Order any amount of the Customer Order remains, the Floor Broker must fill the remainder of the Customer Order by executing it against the Facilitation Order at the Facilitation Price.

(5) If the trading crowd does not provide a bid and offer for all components of the Customer Order in response to the Floor Broker’s request within a reasonable period of time, for the purposes of this rule, either: (i) the quoted market disseminated by the Exchange prior to the commencement of the Facilitation Procedure will constitute the market quoted by the trading crowd in response to the Floor Broker’s request; or (ii) for orders for which there is no disseminated market (such as complex orders), the market for the order will be determined by the disseminated quote for each leg of the transaction prior to the commencement of the Facilitation Procedure. Once the Floor Broker provides a Facilitation Price and can satisfy all of the contingencies associated with the Customer Order, the Customer Order is deemed consummated at the Facilitation Price. After satisfying the orders of any persons who are not OTP Holders or OTP Firms of the Exchange pending at the Facilitation Price, the Floor Broker may facilitate up to forty percent (40%) of the remaining Customer Order against the Facilitation Order at the Facilitation Price and must allow any other member of the trading crowd interested in trading at the facilitation price to execute the remaining sixty percent (60%) or more of the Customer Order. After providing the crowd reasonable time to execute the remaining 60% of the Customer Order on an equal basis as described in PCX Rule 6.75(c), the Floor Broker must fill the remainder of the Customer Order by executing it against the Facilitation Order at the Facilitation Price.

(6) If the facilitation trade occurs at the Lead Market Maker’s (“LMM’s”) quoted bid or offer in their allocated issue and the Floor Broker takes less than forty percent (40%) of the trade, then the LMM may elect to accept either: (i) a guaranteed participation level of forty percent (40%) minus the Floor Broker’s allocation percentage, or (ii) to participate in the pro-rata allocation on a non-guarantee participation level. If the trade occurs at a price other than the LMM’s quoted bid or offer, the LMM is entitled to no “guaranteed” participation. Nothing in this rule is intended to prohibit a Floor

Broker or LMM from trading more than their percentage entitlements if the other members of the trading crowd do not choose to trade the remaining portion of the order.

(c) – No change.

(d) – Trading Crowd Opportunity to Respond. Except as provided in subparagraph (b) of this rule relating to the Facilitation Procedure for Customer Orders of at least 50 contracts, Floor Brokers are cautioned that they must allow OTP Holders in the trading crowd a reasonable period in which to respond to the bid and/or offer prior to consummating the cross transaction. A reasonable period will not be defined in terms of specific time limit. However, an obvious attempt to execute a cross in an uninterrupted sequence with the announcement of the bid and offer is deemed to be a violation of Rule 6.47 and Rule 6.73, and grounds for objection to the cross transaction.

(e) –(f) – No change.

Commentary:

.01 The term "customer of an OTP Holder or OTP Firm" shall mean, in connection with Rule 6.62(i) and 6.47, a customer that is neither an OTP Holder or OTP Firm nor a broker/dealer.

.02 When accepting a bid or offer made on behalf of a customer, all contingencies of the Customer Order must be satisfied by the accepting OTP Holder or OTP Firm.

.03 – No change.

.04 Where a related transaction must be effected in another market, that transaction must be effected prior to the options transaction.

.05 – No change.

.06 It will be a violation of a Floor Broker's duty to use due diligence in representing its Customer Order if a Floor Broker does not employ the Facilitation Procedure on the PCX immediately upon receipt on the PCX of the order that the OTP Holder or OTP Firm wishes to have executed as a facilitation cross.

.07 It will be a violation of an OTP Holder or OTP Firm's duty of best execution to its customer if it were to cancel a Facilitation Order to avoid execution of the order at a better price. The availability of the Facilitation Procedure does not alter an OTP Holder or OTP Firm's best execution duty to get the best price for its customer. Accordingly, while facilitation orders can be cancelled prior to a trading crowd providing quotes in response to a request for a market, if an OTP Holder or OTP Firm were to cancel a Facilitation Order when there was a superior price available on the Exchange and subsequently re-enter the Facilitation Order at the same Facilitation Price after the better price was no longer available without attempting to obtain that better price for its customer, there would be a presumption that the OTP Holder or OTP Firm did

so to avoid execution of its Customer Order in whole or in part by other brokers at the better price.