PACIFIC EXCHANGE
STOCK & OPTIONS

RULE
ADOPTION
NOTICE

RAN-02-38
December 31, 2002

TO:	**All PCX Members and Member Organizations** **ETP Holders and Sponsored Participants**
FROM:	**Department of Regulatory Policy**
SUBJECT:	**ArcaEx Midpoint Pricing Order Types** **(File No. SR-PCX-2002-53)**

On August 5, 2002 the Pacific Exchange, Inc. filed with the Securities and Exchange Commission a proposed rule change to adopt two new order types—a Midpoint Crossing Order and Midpoint Directed Fill. The two new order types would allow Users on the Archipelago Exchange ("ArcaEx") facility to receive executions priced between the NBBO at price increments finer than the minimum trading differential permitted under the Exchange's current rules. A Midpoint Cross Order is a Cross Order that is priced at the midpoint of the NBBO. The Midpoint Directed Fill is an additional feature of the ArcaEx system's price improvement algorithm that will enable market makers to match automatically against incoming Directed Orders at the midpoint price between the NBBO. On December 19, 2002, the SEC approved the proposed rule change.

The following is the text of the rule change. Questions regarding this bulletin may be directed to Peter Bloom at (415) 393-4166.

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EXHIBIT A

Text of the Rule Change:[1]

PCX Equities, Inc.

Rule 7
Equities Trading

Trading Differentials

Rule 7.6(a) – No change.

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

Commentary:

.01 – .04 – No change.

.05 The minimum price variation ("MPV") for quoting and entry of orders in equity securities traded on the Archipelago Exchange is [shall be] $0.01[; provided, however, at all times the MPV shall be consistent with the Decimalization Implementation Plan].

.06 The minimum price improvement increment ("MPII") on the Archipelago Exchange shall be equal to $0.01 or 10% of the NBBO spread, whichever is more; provided, however, that if the transaction involves either a Midpoint Cross Order or a Midpoint Directed Fill and if the NBBO bid/ask differential is one minimum price variation, then the MPII is one-half of the minimum price variation.

.07 Notwithstanding Commentaries .03 and .05 above, Midpoint Cross Orders and Midpoint Directed Fills may be executed and reported in increments as small as one-half of the minimum price variation.

(b) – No change.

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Rule 7.31(a) – (i) – No change.

(j) Directed Fill. Any Market Maker with the appropriate technology, as determined from time to time by the Corporation may submit a standing instruction to the Archipelago Exchange for the parameters of a Directed Fill, including, but not limited to, the size of the order, the Users that may send such Market Maker a Directed Order, the price improvement algorithm and the period of time the instruction is effective. The Market Maker's Directed Fill described in the instruction will only be generated in response to a Directed Order directed to such Market Maker. The Directed Fill is a limit order with (1) a size that is equal to or less than the size of the Directed Order and (2) a price that improves the BBO by an automatically preset amount, which, except as provided in Rule 7.6(a), Commentary .06, must be equal to or greater than the MPII, pursuant to a price improvement algorithm; provided, however, the Directed Fill will not be generated if the price is not equal to or better than the NBBO. A Market Maker may modify the parameters of the instruction for a Directed Fill from time to time, as the Corporation permits.

(k) – (r) – No change.

(s) Cross Order. A two-sided order with instructions to match the identified buy-side with the identified sell-side at a specified price (the "cross price"). For the purposes of this Rule 7.31(s), an order of block size shall have the same meaning as set forth in Rule 7.57. A Cross Order will be executed as follows; provided, however, no Cross Orders shall be matched at the cross price without interacting with any orders in the Arca Book unless the cross price improves the BBO by the MPII, except as provided in Rule 7.6(a), Commentary .06.

(1) – (2) – No change.

(t) – (x) – No change.

(y) Midpoint Cross Order. A Cross Order that is priced at the midpoint of the NBBO. The Corporation will reject a Cross Order designated for midpoint pricing when a locked or crossed market exists in that security.

(z) Midpoint Directed Fill. A Directed Fill that is priced at the midpoint of the NBBO. When a locked or crossed market exists in the security, the inbound Directed Order will bypass the Directed Order Process and immediately enter the Display Order Process for execution pursuant to Rule 7.37(b).

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