

thereunder,<sup>2</sup> notice is hereby given that on February 10, 2003, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange proposes to amend PCX Rule 3.6 in order to amend its pricing requirement for securities that underlie options traded on the Exchange ("underlying security"). The text of the proposed rule change follows. Additions are in *italics*. Deleted text is in brackets.

#### **Rules of the Board of Governors**

Rule 3.6. The underlying securities of option contracts traded on the Exchange shall be approved for Exchange transactions by the Board of Governors following the recommendation of the Options Listing Committee. In approving underlying securities, both the Options Listing Committee and the Board shall give due regard to, and the Board shall promulgate guidelines relative to, the following factors:

- (a)—No change.
- (1)–(3)—No change.

(4) [Either (i) the market price per share of the underlying security will have been at least \$7.50 for the majority of business days during the three calendar months preceding the date of selection, as measured by the lowest closing price recorded in any market in which the underlying security traded on each of the subject days;] (A) *If the underlying security is a "covered security" as defined under Section 18(b)(1)(A) of the Securities Act of 1933, the market price per share of the underlying security has been at least \$3.00 for the previous five consecutive business days preceding the date on which the Exchange submits a certificate to the Options Clearing Corporation for listing and trading. For purposes of this rule, the market price of such underlying security is measured by the closing price reported in the primary market in which the underlying security is traded.*

(B) *If the underlying security is not a "covered security", the market price per share of the underlying security has been at least \$7.50 for the majority of*

*business days during the three calendar months preceding the date of selection, as measured by the lowest closing price reported in any market in which the underlying security traded on each of the subject days, or [(ii)](a) the underlying security meets the guidelines for continued listing in Rule 3.7; (b) options on such underlying security are traded on at least one other registered national securities exchange; and (c) the average daily trading volume for such options over the last three (3) calendar months preceding the date of selection has been at least 5,000 contracts; and*

- (5)—No change.
  - (b)–(c)—No change.
- Commentary:  
.01–.04—No change.  
.05 (a)–(c)—No change.

(d) In the case of a Restructured Transaction that satisfies either or both of the conditions of subsections (a)(1) and (a)(2) to this Commentary .05 in which shares of a Restructured Security are sold in a public offering or pursuant to a rights distribution:

- (i)—No Change.
  - (ii) the exchange may certify that the market price of the Restructure Security satisfies the requirement of Rule 3.6(a)(4) by relying on the market price history of the Original Security prior to the ex-date for the Restructuring Transaction in the manner described by subsection (a) to this Commentary .05, but only if the Restructure Security has traded "regular way" on an exchange or automatic quotation system for at least five trading days immediately preceding the date of selection, and at the close of trading on each trading day preceding the date of selection, as well as the opening of trading on the date of selection the market price of the Restructure Security was at least \$7.50; or, if the Restructure Security is a Covered Security as defined in paragraph (a)(4) above, the market price of the Restructure Security was at least \$3.00; and
  - (iii)—No change.
- .06–.07—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 Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item III below. The Exchange 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**

##### **1. Purpose**

The Exchange proposes to amend its pricing requirement for underlying securities. Currently, PCX Rule 3.6 requires that the market price per share of any underlying security must be at least \$7.50 for the majority of business days during the three calendar months preceding the date of selection of an option class, as measured by the lowest closing price reported in any market in which the underlying security traded on each of the subject days.

The Exchange now proposes to amend Rule 3.6 to provide that, for underlying securities that are deemed Covered Securities, as defined under section 18(b)(1)(A) of the Securities Act of 1933 ("1933 Act"),<sup>3</sup> the closing market price of the underlying security must be at least \$3.00 per share for the five previous consecutive business days prior to the date on which PCX submits an option issue certification. For underlying securities that are not Covered Securities, the Exchange states that the current \$7.50 price per share requirement would continue to apply.

When the \$7.50 price requirement was first implemented, the listed options market was in its infancy. Now more than twenty-eight years after the PCX first started trading listed options, the Exchange states the listed options market is a mature market with sophisticated investors. The Exchange does not believe that this particular criteria serves to accomplish its presumed intended purpose, *i.e.*, to prevent the proliferation of option issues on overlying securities that lack liquidity needed to maintain fair and orderly markets. The Exchange states that it now seeks to move away from what it believes is a paternalistic approach to listing standards and allow the desires of its customers and the workings of the marketplace to determine the securities on which the Exchange will list options.

In determining to list any number of new option classes, the Exchange must

<sup>3</sup> Section 18(b)(1)(A) of the 1933 Act provides that, "(a) security is a covered security if such security is—listed, or authorized for listing, on the New York Stock Exchange or the American Stock Exchange, or listed, or authorized for listing, on the National Market System of the Nasdaq Stock Market \* \* \* 15 U.S.C. 77r(b)(1)(A). The term Covered Security, for the operation of proposed amendments to Rule 3.6 and Commentary .05 herein, would not include those securities defined under Section 18(b)(1)(B) of the 1933 Act. 15 U.S.C. 77r(b)(1)(B).

<sup>2</sup> 17 CFR 240.19b-4.