

## Client Alert

# NYSE and Nasdaq Corporate Governance Amendments

In August 2004, the New York Stock Exchange submitted, and subsequently amended, a proposal to amend its corporate governance rules, which, among other things, seeks to clarify the director independence standards.<sup>1</sup> Separately, Nasdaq adopted amendments to its corporate governance rules, which are currently effective, clarifying the director independence standards regarding payments from a listed company.<sup>2</sup> The respective amendments are in response to numerous requests received by the NYSE and Nasdaq for clarification and interpretation of the corporate governance rules originally approved by the SEC on November 4, 2003.

### NYSE Proposed Amendments

The NYSE proposes to amend the definition of “independent director” as follows:

- For the independence standard relating to a director or a family member who received more than \$100,000 in direct compensation from a listed company, the proposed amendments clarify that the look-back requirement will apply to any rolling 12-month period in the three years preceding the date of determination, addressing the concern that the look-back period could be read to extend for more than three years.
- For the independence standard relating to a director or a family member who is or was an executive officer of another company where a current executive officer of the listed company serves or served as a member of the other company’s compensation committee, the proposed amendments clarify that the service on the compensation committee must be *at the same time* as the employment of the director or family member as an executive officer of the other company.
- For the independence standard relating to payments to or from a company exceeding \$1 million or 2% of another other company’s consolidated gross revenues, the proposed amendments clarify that rather than excluding charitable organizations from the definition of “companies” as currently provided, only *contributions* to charitable organizations, and

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<sup>1</sup> Securities and Exchange Commission Release No. 34-50298; File No. SR-NYSE-2004-41. A copy of the Release is available on the SEC website at [www.sec.gov/rules/sro/nyse/34-50298.pdf](http://www.sec.gov/rules/sro/nyse/34-50298.pdf).

<sup>2</sup> Securities and Exchange Commission Release No. 34-49901; File No. SR-NASD-2004-080 and Release No. 34-49903; File No. SR-NASD-2004-086. Copies of the Releases are available on the SEC website at [www.sec.gov/rules/sro/nasd.shtml](http://www.sec.gov/rules/sro/nasd.shtml).

not commercial or other business-related payments, are excluded for purposes of this standard.

- For the independence standard relating to employment or affiliation of a director or a family member with a present or former internal or external auditor, the proposed amendments substantively amend the standard to narrow its scope in most cases. The current requirements preclude an independence determination because of *past* personal or family member employment or affiliation with an auditing firm, even though the person involved never worked on the listed company account.
  - The revised standard would preclude an independence determination for:
    - any director or family member who is a current partner of the audit firm;
    - any director who is a current employee of the audit firm;
    - any family member who is a current employee of the audit firm participating in the firm’s audit, assurance or tax compliance (but not tax planning) practice; and
    - any director or family member who is a former partner or employee of the audit firm who personally worked on the listed company’s audit during the past three years.
  - The revised standard would preclude an independence determination for one new category of persons — a director with a family member who is a current partner of the audit firm. Under the current standard, such a family member would not impact a director’s independence if the family member did not act in a “professional capacity” at the audit firm. The proposed amendments would allow a listed company until the first annual meeting after January 1, 2005 to replace a director who is independent under the current standard but not the amended standard.
  - For purposes of this standard only, the definition of “immediate family member” would be narrowed to mean a spouse, minor child or stepchild, or an adult child or stepchild sharing a home with the director.

The proposed amendments also add a definition of “executive officer” (which incorporates the definition of “officer” under Exchange Act Rule 16a-1(f)) and clarify that service as an interim executive officer (and not just an interim Chairman or CEO, as currently provided) will not trigger the look-back provisions of the independence standards relating to employment by the listed company and direct compensation paid by the listed company.

The proposed amendments also specifically require that a listed company identify its independent directors in its annual proxy statement (or Form 10-K if the company does not file a proxy statement).

The proposed amendments also seek to clarify a number of other NYSE corporate governance rules, including that:

- The audit committee must meet to review and discuss the listed company's financial statements and must review the company's specific MD&A disclosures.
- The non-CEO compensation on which the compensation committee should focus is that of the listed company's executive officers.
- If the listed company does not limit the number of audit committees on which its audit committee members serve to *three or less*, the board must determine that such simultaneous service would not impair the member's ability to serve effectively on the listed company's audit committee. Currently, the NYSE rules do not specify a threshold limit above which the determination requirement would be triggered.
- A non-management director must preside over each executive session of the non-management directors and if the same director does not preside at every session, the listed company's annual proxy statement (or Form 10-K if the company does not file a proxy statement) must disclose the procedure by which a presiding director is selected for each session.
- The listed company's annual proxy statement (or Form 10-K if the company does not file a proxy statement) must disclose the method for communicating directly with the presiding director or the non-management directors as a group. Currently, the NYSE rules do not specify where such disclosure should appear.
- The listed company's annual proxy statement (or Form 10-K if the company does not file a proxy statement) must disclose that the company's corporate governance guidelines, committee charters and codes of business conduct and ethics are available on the company's website. Currently, such disclosure is only required in the listed company's Form 10-K.
- The listed company must submit to the NYSE an annual written affirmation and interim written affirmations in the event of any changes to the listed company's board of directors or the board committees subject to the NYSE rules.

The SEC requested that comments on the proposed amendments be submitted no later than September 29, 2004. Comments may be submitted electronically:

- On the SEC's Internet comment form ([www.sec.gov/rules/sro.shtml](http://www.sec.gov/rules/sro.shtml)); or
- By e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov).

All comments should refer to File No. SR-NYSE-2004-41 (in the subject line if sent by e-mail).

### Nasdaq Amendments

The amendments to Nasdaq's corporate governance rules were effective June 22, 2004 and amend the definition of "independent director" as follows:

- For the independence standard relating to a director or a family member who received payments of more than \$60,000, the proposed amendments clarify that:

- the look-back requirement will apply to any rolling 12-month period in the three years preceding the date of determination, rather than looking at the past three fiscal years (which in some circumstances could result in a look-back period of almost four years);
- the receipt by a director of standard, non-preferential loans made by a financial institution in the ordinary course of business would not impair a director's independence;
- the receipt by a director of standard, non-preferential payments made by a financial institution in the ordinary course of business, such as interest payments made by a bank on deposits, certificates of deposit or savings bonds, or other payments made by a financial institution to its customers where the financial institution is acting in an agency capacity, would not impair a director's independence.

September 14, 2004

For Additional Information

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