

### ***Summary of Final NYSE Corporate Governance Rules***

#### **Executive Summary**

On November 4, 2003, the Securities and Exchange Commission (“SEC”) issued an order approving significant amendments to the corporate governance requirements of the New York Stock Exchange (“NYSE”). The new requirements are the culmination of a series of proposed rules and amendments from the NYSE that have occurred over more than a year. The NYSE rules require that, among other things:

- Issuers have a majority of independent directors and members of the board meet tightened standards for qualifying as an independent director;
- Non-management directors conduct separate regularly scheduled meetings;
- Issuers have a nominating/corporate governance committee and a compensation committee, each of which is comprised entirely of independent directors and has a charter outlining certain minimum duties and responsibilities;
- Audit committee members meet more stringent standards of independence and audit committees assume increased powers and responsibilities that must be documented in a charter;
- Issuers adopt and disclose corporate governance guidelines and a code of business conduct and ethics; and
- The CEO of each listed company must certify as to compliance with NYSE corporate governance listing standards and provide written notification to the NYSE of any material noncompliance with these standards.

In addition, on June 30, 2003, the SEC issued an order approving rule changes of the NYSE requiring shareholder approval of most equity compensation plans.

#### ***Companies subject to the new rules***

The NYSE’s final rules apply in full to all companies with common equity securities listed on the NYSE, with exceptions from certain requirements for various types of entities, including certain limited partnerships and companies in bankruptcy, closed-end and open-end funds, passive business organizations in the form of trusts and “controlled companies.”

A “controlled company” is a company of which more than 50% of the voting power is held by an individual, a group or another company. A controlled company is not required to have a majority-independent board or comply with the new requirements as to nominating/corporate governance committees or compensation committees. A controlled company that chooses to take advantage of any or all of these exemptions must disclose that choice, that it is a controlled company and the basis for the determination in its annual proxy statement or, if the company does not file an annual proxy statement, in the company’s annual report on Form 10-K filed with the SEC. Controlled companies must comply with the other requirements contained in the new NYSE rules.

### ***Effective dates for the new rules***

In general, companies will have until the earlier of their first annual meeting after January 15, 2004 or October 31, 2004 to comply with the new rules. However, if a company with a classified board would be required (other than by virtue of an independent audit committee requirement of Rule 10A-3 under the Securities Exchange Act of 1934, as amended ("Exchange Act")) to change a director who would not normally stand for election in such annual meeting, such director may continue in office until the second annual meeting after January 15, 2004, but no later than December 31, 2005. Companies listing in conjunction with their initial public offering will be permitted to comply with certain requirements on a phased-in basis.

Companies listing upon transfer from another market have 12 months from the date of transfer in which to comply with any requirement to the extent the market on which they were listed did not have the same requirement. To the extent the other market has a substantially similar requirement but also had a transition period from the effective date of that market's rule, which period had not yet expired, the company will have the same transition period as would have been available to it on the other market. This transition period for companies transferring from another market will not apply to the audit committee requirements of Exchange Act Rule 10A-3 unless a transition period is available thereunder.

### ***Director independence requirements***

The NYSE's final rules require that a majority of each listed company's directors qualify as "independent directors." The board must make an affirmative determination that a director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company). The NYSE stated in commentary that the board should consider the issue not merely from the standpoint of the director, but also from the standpoint of persons or organizations with whom the director has an affiliation. Because the concern is independence from management, the NYSE does not view ownership of even a significant amount of stock, by itself, as a bar to an independence finding.

The basis for a board determination that a relationship is not material must be disclosed in the annual proxy statement or, if the company does not file an annual proxy statement, in the annual report on Form 10-K. To facilitate the determination of whether a director has a "material relationship" with the issuer, the board may adopt and disclose categorical standards, which standards must be disclosed, and may make a general disclosure if a director meets these standards. Any determination of independence for a director who does not meet these standards must be specifically explained. In the event that a director with a relationship that does not fit within these categorical standards is determined to be independent, a board must disclose the basis for its determination.

In addition to requiring the absence of a material relationship, the final rules prohibit a finding that a director is independent in the following situations:

- A director who is an employee, or whose immediate family member is an executive officer, of the company is not independent until three years after the end of such employment relationship.
- A director who receives, or whose immediate family member receives, more than \$100,000 per year in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service), is not independent until three years after ceasing to receive more than \$100,000 per year in such compensation.
- A director who is affiliated with or employed by, or whose immediate family member is affiliated with or employed in a professional capacity by, a present or former internal or external auditor of the company is not independent until three years after the end of the affiliation or the employment or auditing relationship.
- A director who is employed, or whose immediate family member is employed, as an executive officer of another company where any of the listed company's present executives serve on that company's compensation committee is not independent until three years after the end of such service or the employment relationship.

- A director who is an executive officer or an employee, or whose immediate family member is an executive officer, of a company that makes payments to, or receives payments from, the listed company for property or services in an amount which, in any single fiscal year, exceeds the greater of \$1 million, or 2% of such other company's consolidated gross revenues, is not independent until three years after falling below such threshold.

"Immediate family member" is defined to include a person's spouse, parents, children, siblings, mothers- and fathers-in-law, sons- and daughters-in-law, brothers- and sisters-in-law, and anyone (other than domestic employees) who shares such person's home. When applying the look-back provisions to determine director independence, listed companies need not consider individuals who are no longer immediate family members as a result of legal separation or divorce, or those who have died or become incapacitated.

In order to facilitate a smooth transition to the new director independence standards, the NYSE will phase in the "look-back" provisions by applying only a one-year look-back for the first year after adoption of these new independence standards. The three-year look-back periods provided for in the director independence requirements will begin to apply only from and after November 4, 2004, the date the final rules were adopted.

### ***Non-management directors must conduct executive sessions***

Under the final NYSE rules, the non-management directors of a listed company must convene regularly scheduled executive sessions without members of management in attendance. Non-management directors are directors who are not company officers (as that term is defined in Rule 16a-1(f) under the Exchange Act), and may thus include non-officer directors who are not independent for other reasons. The NYSE has recommended that executive sessions be conducted at least once per year and has stated that executive sessions are important not only to foster better communication among non-management directors, but also to prevent any negative inference from attaching to the calling of executive sessions. The NYSE has suggested in commentary to the final rules that, if the non-management directors include persons who are not "independent directors," as defined under the new rules, at least one separate session of independent directors should be convened annually.

There need not be a single presiding director at such executive sessions of the non-management directors; however, if a director is chosen to preside at these meetings, that director's name must be disclosed in the annual meeting proxy statement or, if the company does not file an annual proxy statement, in the annual report on Form 10-K. In order that interested parties may be able to make their concerns known to the non-management directors, companies must disclose a method for such parties to communicate directly with the presiding director or with the non-management directors as a group. Companies may, if they wish, utilize for this purpose the same procedures they have established to comply with the requirements for the receipt of complaints as to accounting and related matters under Exchange Act Rule 10A-3.

### ***Independent nominating/corporate governance committee required***

Under the NYSE's final rules, each listed company is required to have a nominating/corporate governance committee composed entirely of "independent directors," as defined above. In addition, the committee must have a written charter that addresses:

- The committee's purpose and responsibilities, including identification of individuals qualified to become board members (consistent with criteria approved by the board), selection of (or recommendation that the board select) the director nominees for the next annual meeting of shareholders, development and recommendation to the board of a set of corporate governance principles applicable to the company, and oversight of the evaluation of the board and management; and
- An annual performance evaluation of the nominating/corporate governance committee.

The NYSE recommends, but does not require, that the committee charter should provide that if a search firm is used to identify candidates for director, the nominating/corporate governance committee should have the sole authority to retain and terminate the search firm, including the sole authority to approve the search firm's fees and other retention terms. The final rules provide an exception that, if a company is legally required by contract or otherwise to provide third parties with the ability to nominate directors (e.g. through preferred stock rights, stockholders' agreements or management agreements) the selection and nomination of such directors need not be subject to the nominating committee process.

### ***Independent compensation committee required***

Under the NYSE's final rules, each listed company is required to have a compensation committee composed entirely of "independent directors" as defined above. In addition, the committee must have a written charter that addresses:

- The committee's purpose and responsibilities, including direct responsibility for: (1) reviewing and approving corporate goals and objectives relevant to CEO compensation, evaluating the CEO's performance in light of the goals and objectives and, either as a committee or together with the other independent directors (as directed by the board), determining and approving the CEO's compensation level based on this evaluation, (2) making recommendations to the board with respect to non-CEO compensation, incentive-compensation plans and equity-based plans, and (3) producing a compensation committee report on executive compensation as required by the SEC to be included in the company's annual proxy statement or, if the company does not file a proxy statement, in the company's annual report on Form 10-K; and
- An annual performance evaluation of the compensation committee.

The NYSE commentary indicates that the committee charter should provide that if a compensation consultant is to assist in the evaluation of director, CEO or executive officer compensation, the compensation committee should have the sole authority to retain and terminate the consulting firm, including the sole authority to approve the consultant's fees and other retention terms. The commentary to the final rules states that nothing in the rules should be read to prohibit a board discussion of the CEO's compensation.

### ***Heightened standards for audit committee membership***

The final rules require that each listed company's audit committee have a minimum of three members, each of whom qualifies as an independent director under the standards applicable to directors generally, as well as the independence criteria for audit committee members set forth in Exchange Act Rule 10A-3. In addition, the existing standards of the NYSE require each member of the audit committee to be "financially literate" as such qualification is interpreted by the company's board in its business judgment, or must become financially literate within a reasonable period of time after appointment to the audit committee. Further, at least one member of the audit committee must have accounting or related financial management expertise, as the company's board interprets such qualification in its business judgment.

While the NYSE does not require that a listed company's audit committee include a person who satisfies the definition of "audit committee financial expert" as set out in Item 401(e) of Regulation S-K, a board may presume (as stated in the NYSE commentary) that such a person has accounting or related financial management expertise. Note that disclosure of whether a company has an "audit committee financial expert" serving on its audit committee is required by the SEC only in an annual report, although a company may include such information in its proxy or information statement and incorporate that disclosure into its annual report if it complies with the applicable rules for incorporation by reference.

### ***Duties and responsibilities of the audit committee***

The NYSE's final rules require the audit committee of each listed company to have a written charter that addresses the committee's purpose which, at a minimum, must be to: (1) assist board oversight of the integrity of the financial statements, compliance with legal and regulatory requirements, the independent auditor's qualifications and independence, and the performance of the internal audit function and independent auditors; and (2) prepare an audit committee report as required by SEC rules to be included in the annual proxy statement. Additionally, the audit committee charter must also provide for an annual performance evaluation of the committee.

The final rules also state that the audit committee charter must include the duties and responsibilities of the audit committee, which must include those responsibilities set forth in Exchange Act Rule 10A-3 relating to: (1) registered public accounting firms, (2) complaints relating to accounting, internal accounting controls or auditing matters, (3) authority to engage advisors and (4) funding as determined by the audit committee. In addition, the audit committee's duties must include the following:

- At least annually, obtain and review a report by the independent auditor describing: (1) the audit firm's internal quality control procedures, (2) any material issues raised by the most recent internal quality control review, or peer review, of the firm, or by an inquiry or investigation by governmental or professional authorities, within the preceding five years, respecting one or more audits carried out by the firm, and any steps taken to deal with any such issues and (3) all relationships between the independent auditor and the company;
- Discuss the annual audited financial statements and quarterly financial statements with management and the independent auditor, including the company's disclosure under "Management's Discussion and Analysis of Financial Condition and Results of Operations";
- Discuss earnings releases, as well as financial information and earnings guidance provided to analysts and rating agencies;
- Discuss policies with respect to risk assessment and risk management;
- Meet separately, periodically, with management, with internal auditors (or other personnel responsible for the internal audit function) and with independent auditors;
- Review with the independent auditor any audit problems or difficulties and management's response;
- Set clear hiring policies for employees or former employees of the independent auditors; and
- Report regularly to the board of directors.

Explaining these new requirements, the NYSE stated in commentary that the audit committee should discuss earnings guidance and financial information generally, but need not discuss in advance each earnings release or each instance in which a company may provide earnings guidance. In addition, the audit committee should discuss guidelines and policies to govern the process by which risk assessment and management is undertaken, but need not be the sole body responsible for risk assessment and management.

### ***Adoption and disclosure of corporate governance guidelines***

The final rules require each listed company to adopt and disclose corporate governance guidelines addressing what the NYSE views as the following key areas of universal importance: (1) director qualification standards, including independence; (2) director responsibilities, including attendance at meetings and advance review of materials; (3) director access to management and independent advisors; (4) director compensation, including general principles for determining the form and amount of director compensation; (5) director orientation and continuing education; (6) management succession, including principles for CEO selection and performance review; and (7) annual performance evaluation of the board. The NYSE acknowledges that no set of guidelines would be appropriate for every company. Companies must disclose these guidelines on their websites, and each company's annual report on Form 10-K must state that this information is available on the company's website and that the information is available in print to any investor who requests it.

### ***Adoption of code of business conduct and ethics***

The final rules require each listed company to adopt a code of business conduct and ethics for its directors, officers and employees, and promptly disclose any waivers of the code for directors and executive officers. The code must address the following topics: (1) conflicts of interest; (2) misappropriation of corporate opportunities; (3) confidentiality; (4) fair dealing; (5) protection and proper use of company assets; (6) compliance with laws, rules and regulations (including insider trading laws); and (7) encouraging the reporting of any illegal or unethical behavior. The code must provide that any waiver of the code for directors and executive officers may be made only by the board of directors or a committee of the board.

### ***Annual certification and notification of noncompliance by CEO***

The final rules require the CEO of each listed company to certify on an annual basis that he or she is not aware of any violation by the company of the NYSE corporate governance listing standards. This certification must be disclosed in the company's annual report to shareholders or, if the company does not prepare an annual report to shareholders, in the company's annual report on Form 10-K. CEOs are also required to promptly notify the NYSE in writing after any executive officer of the listed company becomes aware of any material noncompliance with any applicable provisions of these new NYSE corporate governance requirements.

### ***Internal audit function required***

The final rules require each listed company to have an internal audit function. The rules do not place parameters on the scope or nature of the procedures to be conducted by the internal audit function, leaving such determinations to the discretion of each listed company. A company may choose to outsource this function to a third party service provider other than its independent auditor.

### ***Effects of new rules on foreign private issuers***

Listed companies that are foreign private issuers are permitted to follow home country practice in lieu of the provisions of the new NYSE rules, except that such companies are required to: (1) comply with the audit committee member independence requirements of Exchange Act Rule 10A-3 described above; (2) comply with the CEO notification and certification requirements as to compliance with NYSE listing standards; and (3) disclose significant differences between their corporate governance practices and those followed by domestic companies under the NYSE listing standards. The NYSE has stated in commentary to the final rules that any discussion of differences between an issuer's home country governance practices and the NYSE standards requires only a brief, general summary of the significant differences, not a cumbersome analysis.

### ***Issuance of public reprimand letter***

The NYSE may issue a public reprimand letter to a company that violates a listing standard. The NYSE has recognized in its commentary to the new rules that suspending trading or delisting a company can be harmful to the very shareholders that the listing standards seek to protect. Therefore, these measures are used sparingly and judiciously. The lesser sanction of a public reprimand letter is intended to deter companies from violating the NYSE's corporate governance or other listing standards. For companies that repeatedly or flagrantly violate the listing standards, the NYSE has clarified that suspension and delisting remain the ultimate penalties.

### ***Shareholder approval of equity compensation plans***

On June 30, 2003, the SEC issued an order approving rule changes by the NYSE requiring shareholder approval of most equity compensation plans. The new rules generally require shareholder approval for the adoption of equity compensation plans, including stock option plans, as well as repricings and material revisions to such plans' changes, with certain limited exceptions. The new rules eliminate the exception to the shareholder approval requirements for "broadly based" plans. However, shareholder approval is generally not required for equity compensation plans adopted prior to June 30, 2003 unless such plan is later materially amended.

Examples of revisions that are considered material include revisions that: (i) materially increase the number of shares to be issued under the plan other than to reflect a reorganization, stock split, merger, spinoff or similar transaction or an automatic increase pursuant to an "evergreen" formula where the plan term exceeds 10 years; (ii) materially expand the class of employees, directors or other service providers eligible to participate in the plan; (iii) materially extend the term of the plan; (iv) expand the types of awards available under the plan; (v) materially change the method of determining the strike price of options under the plan; and (vi) delete or limit any provision prohibiting repricing of options.

The final NYSE rules state that the following are either not considered equity compensation plans or are otherwise exempt from the shareholder approval requirements as long as they are approved by the company's independent compensation committee or a majority of the company's independent directors and the listed company notifies the NYSE in writing when it uses any of the following exemptions:

- tax qualified and parallel excess plans;
- plans that merely provide a convenient way to purchase shares on the open market or from the issuer at fair market value;
- the conversion, replacement or adjustment of equity compensation awards in a merger or acquisition transaction to reflect the transaction;
- post-merger and acquisition grants of equity compensation awards under certain plans acquired in merger or acquisition transactions, provided certain conditions are met;
- employment inducement awards; and
- plans made available to all shareholders generally.

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