March 12, 2003

Nancy J. Sanow, Esq.
Assistant Director
Division of Market Regulation
Mail Stop 1001
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: File No. SR-NYSE-2003-06
Proposal Relating to Director Independence Standards

Dear Ms. Sanow:

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934, we hereby enclose for filing nine copies of the above-captioned filing, at least one of which has been manually signed, and one copy of the filing on a diskette in Word 6.0 format.

This proposal amends and restates a portion of the proposals previously filed with the Commission in File No.SR-NYSE-2002-33 (August 16, 2002). Four copies of comment letters received by the NYSE relating to this proposal are attached. Additional comment letters were previously provided to the Commission, as required by Instruction F to Form 19b-4, with File No. SR-NYSE-2002-33.

Very truly yours,

Enclosure

SR-NYSE-2003-06

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 19b-4

Proposed Rule Change

by

New York Stock Exchange, Inc.
March 12, 2003

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

Consists of 40 pages

1. Text of the Proposed Rule Change

(a) On August 16, 2002, the New York Stock Exchange (the "Exchange" or "NYSE") filed with the Securities and Exchange Commission (the "SEC" or the "Commission") amendments to its Listed Company Manual to implement significant changes to its listing standards aimed at helping to restore investor confidence by empowering and ensuring the independence of directors and strengthening corporate governance practices[1] ("SR-NYSE-2002-33" or the "NYSE Corporate Governance Proposals"). On October 7, 2003, at the SEC's request, the Exchange separately filed with the SEC a proposal relating to shareholder approval of equity-compensation plans, which had previously been filed as a part of the NYSE Corporate Governance Proposals.[2] The Commission staff has also requested that we excerpt from the NYSE Corporate Governance Proposals and file separately the provisions relating to director independence, to enable the Commission to address this issue separately from the remainder of the NYSE Corporate Governance Proposals. Accordingly, this filing contains subsections (1) and (2) of proposed Section 303A of our Listed Company Manual, amended in certain respects from the provisions as filed in SR-NYSE-2002-33.

(b) Except as otherwise noted below, the Exchange does not believe that the proposed rule change will have any direct effect, or any significant indirect effect, on any other Exchange rule in effect at the time of this filing.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

(a) The Exchange's Board of Directors approved this proposed rule change on August 1, 2002. No further action by the Board of Directors or the membership of the Exchange is required. Therefore, the Exchange's internal procedures with respect to the proposed rule change are complete.

(b) The persons from the Exchange staff prepared to respond to questions and comments on the proposed rule change are:

Janice O'Neill
Vice President
Corporate Compliance
(212) 656-2407

James F. Duffy
Senior Vice President & Associate
General Counsel
(212) 656-5855

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[1] File No. SR-NYSE-2002-33 (August 16, 2002).

[2] See Securities Exchange Act Release No. 46620 (October 8, 2002) 67 FR 63486 (October 11, 2002) (SR-NYSE-2002-46).

3. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

(a) Purpose

The New York Stock Exchange has long pioneered advances in corporate governance. The NYSE has required companies to comply with listing standards for nearly 150 years, and has periodically amended and supplemented those standards when the evolution of our capital markets has demanded enhanced governance standards or disclosure.

On February 13, 2002, then SEC Chairman Harvey Pitt asked the Exchange to review its corporate governance listing standards. In conjunction with that request, the NYSE appointed a Corporate Accountability and Listing Standards Committee (the "Committee") to review the NYSE's current listing standards, along with recent proposals for reform, with the goal of enhancing the accountability, integrity and transparency of the Exchange's listed companies.

The Committee believed that the Exchange could best fulfill this goal by building upon the strength of the NYSE and its listed companies in the areas of corporate governance and disclosure. This approach recognizes that new prohibitions and mandates, whether adopted by the NYSE, the SEC or Congress, cannot guarantee that directors, officers and employees will always give primacy to the ethical pursuit of shareholders' best interests. The system depends upon the competence and integrity of corporate directors, as it is their responsibility to diligently oversee management while adhering to unimpeachable ethical standards. The Exchange now seeks to strengthen checks and balances and give diligent directors better tools to empower them and encourage excellence. In seeking to empower and encourage the many good and honest people that serve NYSE-listed companies and their shareholders as directors, officers and employees, the Exchange seeks to avoid recommendations that would undermine their energy, autonomy and responsibility.

The proposed new corporate governance listing requirements are designed to further the ability of honest and well-intentioned directors, officers and employees to perform their functions effectively. The resulting proposals will also allow shareholders to more easily and efficiently monitor the performance of companies and directors in order to reduce instances of lax and unethical behavior.

In preparing the recommendations it made to the NYSE Board, the Committee had the benefit of the testimony of 17 witnesses and written submissions from 21 organizations or interested individuals. The Committee also examined the excellent governance practices that many NYSE listed companies have long followed. In addition, the Committee reviewed extensive commentary recommending improvement in corporate governance and disclosure, statements by the President of the United States and members of his Cabinet, as well as pending SEC proposals and legislation introduced in Congress.

On June 6, 2002, the Committee submitted its Report and initial recommendations to the NYSE Board of Directors.[3] President Bush, then SEC Chairman Harvey Pitt, members of Congress, CEOs of listed companies, institutional investors and state pension funds, organizations such as the Business Roundtable and the Council of Institutional Investors, and leading academics and commentators expressed strong support for the Committee's initiatives. The Committee also received insightful and practical suggestions for the improvement of its recommendations from experts within the NYSE, listed companies, institutional investors, outside organizations and interested individuals. In addition to many face-to-face meetings and telephone calls, the Exchange received over 300 comment letters.

Many of the commentators argued for, or sought, guidance from the Exchange at a level of detail inconsistent with the role that the Committee was asked to fulfill. However, where appropriate the Committee reflected cogent comments in clarifications and modifications to its recommendations.

Following approval of the NYSE Board of Directors on August 1, 2002, on August 16, 2002, the NYSE filed the NYSE Corporate Governance Proposals with the SEC, proposing rule changes to its corporate governance standards which reflect the findings of the Committee. The proposals for new corporate governance listing standards for companies listed on the Exchange will be codified in a new section 303A of the Exchange's Listed Company Manual (the "Manual").[4]

The standards in proposed Section 303A will apply to all companies listing common stock on the Exchange, and to business organizations in non-corporate form such as limited partnerships, business trusts and REITs. However, consistent with past practice regarding corporate governance standards, the Exchange will not apply such standards to passive business organizations in the form of trusts (such as royalty trusts), nor will it

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[3] Report of the NYSE Corporate Accountability and Listing Standards Committee, June 6, 2002.

[4] In its report to the NYSE Board, the Committee set forth basic principles followed in many cases by explanation and clarification. The Exchange is adopting the recommendations as standards in substantially the form they were made by the Committee and adopted by the NYSE Board. Accordingly, the format used will state a basic principle, with the additional explanation and clarifications included as "commentary."

While many of the requirements set forth in this new rule are relatively specific, the Exchange is articulating a philosophy and approach to corporate governance that companies are expected to carry out as they apply the requirements to the specific facts and circumstances that they confront from time to time. Companies and their boards are expected to apply the requirements carefully and in good faith, making reasonable interpretations as necessary, and disclosing the interpretations that they make.

apply them to derivatives and special purpose securities such as those described in Sections 703.16, 703.19, 703.20 and 703.21 of the Manual.[5]

As noted above, subsequent to the filing of the NYSE Corporate Governance Proposals, the SEC requested that the NYSE file proposed Section 303A(8) (relating to shareholder approval of equity-compensation plans) and the proposed amendment to NYSE Rule 452 (which prohibits member organizations from giving a proxy to vote on equity-compensation plans absent specific instructions from a beneficial holder) separately from its remaining proposals to facilitate SEC processing. The Exchange made this separate filing with the SEC on October 7, 2002, and it was published for public comment on October 8, 2002.[6]

The SEC has now requested that the NYSE excerpt from the NYSE Corporate Governance Proposals and file separately the provisions related to director independence, to enable the Commission to address the issue separately from the remainder of the NYSE Corporate Governance Proposals. Accordingly, this filing contains subsections (1) and (2) of proposed Section 303A of the Manual, amended in certain respects from the provisions as originally filed in SR-NYSE-2002-33.[7] It is our understanding that the SEC wishes to publish these subsections for public comment prior to publishing the remainder of the NYSE Corporate Governance Proposals, but that it does not intend to approve or make these provisions effective prior to the remainder of the NYSE Corporate Governance Proposals. Rather, the remaining proposals will be published for comment in a separate filing, and it is expected that the NYSE Corporate Governance Proposals will be given final approval and made effective as a whole, albeit with different transition mechanisms or effective dates for particular provisions.

The Exchange wishes to point out three items that arise as a result of the substance or process of the enactment of the Sarbanes-Oxley Act of 2002 (the “Sarbanes-Oxley Act”) and the SEC’s implementing rules.

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[5] The Exchange has traditionally applied its corporate governance standards to listed closed-end management companies. The Exchange considers the significantly expanded standards and requirements provided for in proposed Section 303A to be unnecessary for closed-end management companies given the pervasive federal regulation applicable to them. However, closed-end management companies will be required to continue to comply with the audit committee requirements, as they are enhanced and expanded in proposed subsections (6) and (7) of Section 303A.

[6] See Securities Exchange Act Release No. 46620 (October 8, 2002); 67 FR 63486 (October 11, 2002) (SR-NYSE-2002-46).

[7] The amended provisions utilize certain specific financial criteria in lieu of the previously proposed employment test. The amended proposals also phase in “look-back” or “cooling-off” periods, rather than apply them immediately. In this way, directors are not retroactively disqualified for affiliations that were permissible in the past.

Immediate Family

Certain close family relationships preclude independence under our proposal rule. The operative definition of "immediate family" is unchanged from that contained in SR-NYSE-2002-33, which in turn is the same as that employed in the NYSE's current rule regarding the independent audit committee.[8]

When the SEC proposed its rules implementing Section 301 of the Sarbanes-Oxley Act, it proposed a more limited concept of family. The Exchange defines "immediate family" as including "a person's spouse, parents, children, siblings, mothers-in-law and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, and anyone (other than employees) who shares such person's home." The SEC proposal includes only a person's spouse, minor children or stepchildren or children or stepchildren sharing the director's home.

Foreign Private Issuers

The Exchange wishes to clarify that, as applied to foreign private issuers, its corporate governance standards continue generally to defer to home-country practices. In proposed Section 303A (11) of the NYSE Corporate Governance Proposals, the NYSE noted that, "Both SEC rules and NYSE policies have long recognized that foreign private issuers differ from domestic companies in the regulatory and disclosure regimes and customs they follow, and that it is appropriate to accommodate those differences."

The Sarbanes-Oxley Act provides that the Exchange must require foreign private issuers to comply with the independent audit committee requirements set forth in Section 301 of the Sarbanes-Oxley Act, as implemented by the SEC rules. However, consistent with the traditional NYSE approach, the Exchange would require listed foreign private issuers to comply only with the independence requirements of Section 301 of the Sarbanes-Oxley Act and the SEC rule adopted thereunder, but not with any additional proposed independence requirements to be codified in Sections 303A (1) and (2) of the Manual. Listed foreign private issuers disclose to the public any significant ways in which their home-country corporate governance practices differ from those followed by domestic companies under NYSE listing standards.

Effective Date of Independence Standards

Regarding the effective date of these new standards, companies that do not already have majority-independent boards will need time to recruit qualified independent directors, and companies with classified boards may need additional time to implement the new standards in a series of director elections. Accordingly, all listed companies will be required to comply with these standards no later than eighteen months following SEC approval of these proposed Exchange rules. If, for example, the final NYSE rules are approved by the SEC on October 31, 2003, the practical effect would be that companies

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[8] Section 303.02(A) of the Manual.

desiring to deal with this matter at their annual shareholder meeting will have until their first annual meeting held after April 30, 2004 to come into compliance.

It is also appropriate to give companies with classified boards additional time to comply if a change would be required for a director who would not normally stand for election in the first annual meeting after April 30, 2004. In such cases the company will have an additional year to effect the change in that director position.

Companies listing in conjunction with their initial public offering must comply within 24 months of listing. Companies listing upon transfer from another market will have 24 months from the date of transfer in which to comply with this standard 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 the rule, which period had not yet expired, the company will have at least as long a transition period as would have been available to it on the other market.

Independence Standards

The following are the NYSE's proposed requirements relating to director independence as proposed to be codified in Sections 303A (1) and (2) of the Manual.

Section 303A

1. Listed companies must have a majority of independent directors.

Commentary: Effective boards of directors exercise independent judgment in carrying out their responsibilities. Requiring a majority of independent directors will increase the quality of board oversight and lessen the possibility of damaging conflicts of interest.

A company of which more than 50% of the voting power is held by an individual, a group or another company need not have a majority of independent directors on its board or have nominating/corporate governance and compensation committees composed of independent directors.[9] A controlled company that chooses to take advantage of this exemption must disclose in its annual meeting proxy that it is a controlled company and the basis for that determination. However, all controlled companies must have at least a minimum three person audit committee composed entirely of independent directors, and otherwise comply with the audit committee requirements provided for in this Section 303A.

2. In order to tighten the definition of "independent director" for purposes of these standards:

(a) No director qualifies as "independent" unless the board of directors affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or

[9] The Exchange notes that this exemption will affect only a small percentage of its listed companies.

officer of an organization that has a relationship with the company). Companies must disclose these determinations.

Commentary: It is not possible to anticipate, or explicitly to provide for, all circumstances that might signal potential conflicts of interest, or that might bear on the materiality of a director's relationship to a listed company. Accordingly, it is best that boards making "independence" determinations broadly consider all relevant facts and circumstances. In particular, when assessing the materiality of a director's relationship with the company, the board should consider the issue not merely from the standpoint of the director, but also from that of persons or organizations with which the director has an affiliation. Material relationships can include commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships (among others). However, as the concern is independence from management, the Exchange 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 company's annual proxy statement. In this regard, a board may adopt and disclose categorical standards to assist it in making determinations of independence 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. A company must disclose any standard it adopts. It may then make the general statement that the independent directors meet the standards set by the board without detailing particular aspects of the immaterial relationships between individual directors and the company (except where there is a presumption of non-independence, as described in the commentary to Paragraph 2(b) below). In the event that a director with a business or other relationship that does not fit within the disclosed standards is determined to be independent, a board must disclose the basis for its determination. This approach provides investors with an adequate means of assessing the quality of a board's independence and its independence determinations while avoiding excessive disclosure of immaterial relationships.

(b) In addition:

(i) 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 presumed not to be independent until five years after he or she ceases to receive more than $100,000 per year in such compensation.

Commentary: A listed company's board may negate this presumption with respect to a director if the board determines (and no independent director dissents) that, based upon the relevant facts and circumstances, such compensatory relationship is not material. Any affirmative determination of independence made by the board in these circumstances must be specifically explained in the listed company's proxy statement and cannot be covered by a categorical standard adopted in accordance with the

commentary to Paragraph 2(a) above. If a person who received more than $100,000 per year in direct compensation from a listed company dies or becomes incapacitated, the presumption of non-independence applicable to his or her immediate family members will cease immediately upon such death or determination of incapacity.

(ii) 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 auditor of the company is not "independent" until five years after the end of either the affiliation or the auditing relationship.

(iii) 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 serves on that company's compensation committee is not "independent" until five years after the end of such service or the employment relationship.

(iv) A director who is an executive officer or an employee, or whose immediate family member is an executive officer, of another company (A) that accounts for at least 2% or $1 million, whichever is *greater*, of the listed company's consolidated gross revenues, or (B) for which the listed company accounts for at least 2% or $1 million, whichever is *greater*, of such other company's consolidated gross revenues, in each case is not "independent" until five years after falling below such threshold.

Commentary: An "immediate family member" includes 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 employees) who shares such person's home.

Transition Rule. During the five years immediately following [insert the effective date of this listing standard], each five year "look back" period referenced in sub-paragraphs (b)(i) through (b)(iv) shall instead be the period since [insert effective date of this listing standard]. For example, if a director received in excess of $100,000 per year in direct compensation from a listed company during the year prior to [insert effective date of this listing standard], there will be no required presumption that the director is not independent unless such compensatory relationship extended past [insert effective date of this listing standard].

(b) Statutory Basis

The basis under the Securities Exchange Act of 1934 ("Exchange Act") for this proposed rule change is the requirement under Section 6(b)(5)[10] that an exchange have rules that are designed to prevent fraudulent and manipulative acts and practices, to promote just

[10] 15 U.S.C. 78(f)(b)(5).

and equitable principles of trade, to remove impediments to, and perfect the mechanism of a free and open market and, in general, to protect investors and the public interest.

4. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that this proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

While the comments received by the Exchange were addressed to the Committee Recommendations in their entirety, the Exchange will summarize here those comments that were most specifically directed to the proposals contained in subsections (1) and (2) of proposed Section 303A.

Overview

A. Widespread Support for the Recommendations.

The vast majority of commentators, including listed companies, institutional investors, and other interested organizations and individuals enthusiastically embraced the Committee's recommendations for new corporate governance and listing standards for the NYSE.

B. Concerns of Smaller Companies

While most large companies, law firms and institutions expressed general support for the proposals, commentators who characterized themselves as smaller businesses voiced concern. All of these companies complained that the recommendations seem to have been structured for a large-company model, without taking into account the disproportionate impact the proposed rules would have on smaller companies. In particular, they argued that the Committee's recommendations for separate nominating and compensation committees, together with its requirement of majority-independent boards, combined to effectively require that smaller companies enlarge their relatively small boards. These constituents were particularly concerned with the increased costs that compliance with the recommendations would entail. They argued that this will cause the diversion of shareholder value to unrelated third parties and the misdirection of board and management time and effort from productive to bureaucratic activities.

C. Difficulty of Obtaining Independent Directors

Several large companies expressed concern that the new rules will make it more difficult for companies to find quality independent directors because of the increased responsibilities and time commitment that the rules will require of independent directors (especially audit committee members), as well as a perceived increase in such directors' exposure to liability.

Majority-Independent Boards

Many commentators applauded the recommendation that listed companies be required to maintain majority-independent boards. However, numerous constituents, large and small, raised concerns that the requirement would have a variety of adverse consequences.

A. Controlled Companies

Most prominently, more than half of the commenting companies noted that the majority independent board requirement would create insuperable difficulties for companies controlled by a shareholder or parent company. They argued that the rule would be inequitable as applied to them in that it would deprive a majority holder of its shareholder rights; unnecessary in that the Committee's other recommendations (in particular the independent committee and disclosure requirements) would adequately protect minority shareholders; and undesirable in that it would reduce access to capital markets by discouraging spin-offs, by inducing some currently public companies to go private rather than lose control of their subsidiary, and by discouraging those who manage buyout funds and venture capital funds from using initial public offerings and NYSE listings as a means for achieving liquidity and raising capital. One company argued that the majority-independent board requirement would vitiate the ability of a parent to effectively manage its subsidiary, in the process denying to shareholders of the parent the benefits associated with its controlling stake in the subsidiary and requiring them instead to transfer control of the subsidiary to third parties.

Similarly, commentators suggested that companies that are majority-owned by officers and directors should be exempt from this recommendation. One such company argued that where corporate insiders own a majority of the stock of a company, the interests of outside minority shareholders can be adequately protected by the proposed requirement of an independent compensation committee. Family-owned companies also expressed concern with the majority-independence requirement because the proposal would limit the families' involvement with the board.

One commenter specifically stated that even controlled companies should be subject to the majority independence requirement. This commenter was particularly concerned with dual class companies where an investor or group can control voting power without owning a majority of the company's outstanding shares.

The provision in subsection (1) of Section 303A exempting controlled companies from the requirements to have a majority independent board and independent nominating and compensation committees is intended to address the bulk of these comments.

Tighter "Independent Director" Definition

Most commentators were in favor of tightening the definition of "independence," with only a quarter advocating the continued use of existing standards. Certain institutional investors praised with particular emphasis the five-year look-back on compensation committee

interlocks. However, commentators have raised several general questions, described below, as well as numerous specific questions with respect to materiality determinations.

A. Share Ownership

Many commentators expressed a desire for additional clarification of the interaction between share ownership and independence. Several commentators opposed viewing any degree of share ownership as a per se bar to "independence" (absent such other factors as an employment relationship or other financial or personal tie to the company). They argued that directors who own or represent institutions that own very significant economic stakes in the listed companies are often effective guardians of shareholders' interests not only as members of the full board but also of compensation and nominating committees, while directors whose only stake in the membership on the board is the director's fee may be unduly loyal to management. Several venture capitalists raised a similar concern that they will run afoul of the new independence definition, even though venture capitalists, acting as fiduciaries to funds with significant shareholdings, typically have all the qualities that the independent director definition is intended to ensure. The question of the impact of ownership on independence was particularly vexing to companies with listed subsidiaries. They were concerned that a director who is deemed independent with respect to a parent company may not be considered independent with respect to the parent-controlled subsidiary.

The Exchange has clarified in subsection (2) of Section 303A that, since the concern is independence from management, ownership of even a significant amount of stock, by itself, is not necessarily a bar to an independence finding.

B. Safe Harbors for Independence Determinations

Several financial institutions specifically applauded the committee's recommendation that non-materiality determinations be made on a case-by-case basis and publicly disclosed and justified. However, a number of companies objected to the affirmative determination requirement, requesting that the NYSE specify a safe harbor for materiality. These companies cite the competing demands on the board's time and attention; the likelihood that the "no material relationship" requirement will unduly shrink the pool of qualified directorship candidates; and the possibility that the fact-specific inquiry required will expose directors to additional scrutiny and potential liability, which they may be unwilling to assume without additional compensation and/or protection.

Many commentators would like to be able to fulfill their affirmative determination requirement through the establishment of their own safe harbors. For example, one commentator attached a detailed safe harbor proposal covering various types of credit transactions. In addition, a vast majority of commenting banks and financial institutions asked for clarification regarding the treatment of loans to directors. In light of the existing regulatory framework that controls relationships between a bank and its directors and affiliated entities, banks desired to establish categorically that arm's-length loans to directors do not negate independence. Numerous companies and organizations argue that if there are no material relationships, the NYSE should allow the statement of reasons for the board's

determination of independence to be omitted from the proxy statement, and suggest that the rules should not require details of each relationship regardless of size.

The Exchange has clarified in subsection (2) of Section 303A that categorical standards are permissible.

C. Five-Year Cooling-Off Period

More than half of the companies commenting on this issue protested that five years is too long, advocating a two-to-three year period instead. Five companies, reflecting their individual circumstances, requested an exemption for interim CEOs who have served for less than one year. One commentator objected to subjecting all former employees to the cooling-off period, recommending that the prohibition be limited to former executive officers only. Several commentators agreed with the five-year period for former employees, but found the period too long with respect to compensation committee interlocking directorates. Notably, one company thought that the five-year look-back on interlocking directorates would strain parent-subsidiary relations. Likewise, one parent of a controlled public subsidiary expressed its belief that its executives should be able to sit on the subsidiary's compensation committee to ensure that subsidiary's compensation policies are compatible with those of its parent. In addition, a few companies asked whether the inquiry ends by examining the present and past relationships at companies where directors are currently employed, or if one must search back for possible interlocks at companies that may have since been acquired or dissolved – pointing out that with the immediate family overlay to the rule, the latter inquiry could become extremely cumbersome. Several financial institutions (along with several smaller companies) took issue with the blanket exclusion of family members for five years. One company argued that when a family member's relationship has terminated, there should be independence. Another commentator recommended that relatives of deceased or disabled former officers be classified as independent as long as they themselves have no financial involvement other than ownership in the company. Another commenter expressed concern that the proposal relating to a family member employed by a company's auditor or former auditor did not limit the prohibition to employees of an audit firm who were involved with the audit or who influenced the audit.

The Exchange has clarified several of these issues with specified provisions in subsection (2)(b) of Section 303A.

6. Extension of Time Period for Commission Action

The Exchange does not consent to an extension of the time period specified in Section 19(b)(2)[11] of the Exchange Act.

[11] 15 U.S.C. 78s(6)(2).

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

   Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

   This proposed rule change is not based on the rules of another self-regulatory organization or of the Commission.

9. Exhibits

   Exhibit 1 - Form of Notice of Proposed Rule Change for Publication in the Federal Register

   Exhibit 2 –Written Comments on the Proposed Rule

   Comment letter of the Council of Institutional Investors, dated November 8, 2002.

   Comment letter of Three-Five Systems, Inc., dated December 10, 2002.

   Earlier comment letters received by the NYSE with respect to this proposal were previously provided to the SEC in connection with SR-NYSE-2002-33.

   Exhibit A –Text of the Proposed Rule Change

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the self-regulatory organization has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

New York Stock Exchange, Inc.

By ______________________________

Mary Yeager
Assistant Corporate Secretary

Exhibit 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- : File No. SR-NYSE-2003-06)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc. Relating to Director Independence Standards.

Date

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), [1] and Rule 19b-4 thereunder,[2] notice is hereby given that on March 12, 2003, the New York Stock Exchange, Inc. filed with the Securities and Exchange Commission the proposed rule change as described in items I, II, III below, which items have bee prepared by the self-regulatory organization. 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

(a) On August 16, 2002, the New York Stock Exchange (the "Exchange" or "NYSE") filed with the Securities and Exchange Commission (the "SEC" or the "Commission") amendments to its Listed Company Manual to implement significant changes to its listing standards aimed at helping to restore investor confidence by empowering and ensuring the independence of directors and strengthening corporate governance practices[3] ("SR-NYSE-2002-33" or the "NYSE Corporate Governance Proposals"). On October 7, 2003, at the SEC's request, the Exchange separately filed with the SEC a proposal relating to shareholder approval of equity-compensation plans, which had previously been filed as a part of the NYSE Corporate

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4

3 File No. SR-NYSE-2002-33 (August 16, 2002).

Governance Proposals.[4] The Commission staff has also requested that we excerpt from the NYSE Corporate Governance Proposals and file separately the provisions relating to director independence, to enable the Commission to address this issue separately from the remainder of the NYSE Corporate Governance Proposals. Accordingly, this filing contains subsections (1) and (2) of proposed Section 303A of our Listed Company Manual, amended in certain respects from the provisions as filed in SR-NYSE-2002-33.

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 self-regulatory organization included statements concerning the purpose of and basis for the proposed rule change. The text of these statements may be examined at the places specified in item IV below and is set forth in Sections A, B, and C below.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The New York Stock Exchange has long pioneered advances in corporate governance. The NYSE has required companies to comply with listing standards for nearly 150 years, and has periodically amended and supplemented those standards when the evolution of our capital markets has demanded enhanced governance standards or disclosure.

On February 13, 2002, then SEC Chairman Harvey Pitt asked the Exchange to review its corporate governance listing standards. In conjunction with that request, the NYSE appointed a Corporate Accountability and Listing Standards Committee (the “Committee”) to review the

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[4] See Securities Exchange Act Release No. 46620 (October 8, 2002) 67 FR 63486 (October 11, 2002) (SR-NYSE-2002-46).

NYSE's current listing standards, along with recent proposals for reform, with the goal of enhancing the accountability, integrity and transparency of the Exchange's listed companies.

The Committee believed that the Exchange could best fulfill this goal by building upon the strength of the NYSE and its listed companies in the areas of corporate governance and disclosure. This approach recognizes that new prohibitions and mandates, whether adopted by the NYSE, the SEC or Congress, cannot guarantee that directors, officers and employees will always give primacy to the ethical pursuit of shareholders' best interests. The system depends upon the competence and integrity of corporate directors, as it is their responsibility to diligently oversee management while adhering to unimpeachable ethical standards. The Exchange now seeks to strengthen checks and balances and give diligent directors better tools to empower them and encourage excellence. In seeking to empower and encourage the many good and honest people that serve NYSE-listed companies and their shareholders as directors, officers and employees, the Exchange seeks to avoid recommendations that would undermine their energy, autonomy and responsibility.

The proposed new corporate governance listing requirements are designed to further the ability of honest and well-intentioned directors, officers and employees to perform their functions effectively. The resulting proposals will also allow shareholders to more easily and efficiently monitor the performance of companies and directors in order to reduce instances of lax and unethical behavior.

In preparing the recommendations it made to the NYSE Board, the Committee had the benefit of the testimony of 17 witnesses and written submissions from 21 organizations or interested individuals. The Committee also examined the excellent governance practices that many NYSE listed companies have long followed. In addition, the Committee reviewed extensive commentary recommending improvement in corporate governance and disclosure,

statements by the President of the United States and members of his Cabinet, as well as pending SEC proposals and legislation introduced in Congress.

On June 6, 2002, the Committee submitted its Report and initial recommendations to the NYSE Board of Directors.[5] President Bush, then SEC Chairman Harvey Pitt, members of Congress, CEOs of listed companies, institutional investors and state pension funds, organizations such as the Business Roundtable and the Council of Institutional Investors, and leading academics and commentators expressed strong support for the Committee's initiatives. The Committee also received insightful and practical suggestions for the improvement of its recommendations from experts within the NYSE, listed companies, institutional investors, outside organizations and interested individuals. In addition to many face-to-face meetings and telephone calls, the Exchange received over 300 comment letters.

Many of the commentators argued for, or sought, guidance from the Exchange at a level of detail inconsistent with the role that the Committee was asked to fulfill. However, where appropriate the Committee reflected cogent comments in clarifications and modifications to its recommendations.

Following approval of the NYSE Board of Directors on August 1, 2002, on August 16, 2002, the NYSE filed the NYSE Corporate Governance Proposals with the SEC, proposing rule changes to its corporate governance standards which reflect the findings of the Committee. The proposals for new corporate governance listing standards for companies listed on the Exchange will be codified in a new section 303A of the Exchange's Listed Company Manual (the "Manual").[6]

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5 Report of the NYSE Corporate Accountability and Listing Standards Committee, June 6, 2002.

6 In its report to the NYSE Board, the Committee set forth basic principles followed in many cases by explanation and clarification. The Exchange is adopting the

The standards in proposed Section 303A will apply to all companies listing common stock on the Exchange, and to business organizations in non-corporate form such as limited partnerships, business trusts and REITs. However, consistent with past practice regarding corporate governance standards, the Exchange will not apply such standards to passive business organizations in the form of trusts (such as royalty trusts), nor will it apply them to derivatives and special purpose securities such as those described in Sections 703.16, 703.19, 703.20 and 703.21 of the Manual.[7]

As noted above, subsequent to the filing of the NYSE Corporate Governance Proposals, the SEC requested that the NYSE file proposed Section 303A(8) (relating to shareholder approval of equity-compensation plans) and the proposed amendment to NYSE Rule 452 (which prohibits member organizations from giving a proxy to vote on equity-compensation plans absent specific instructions from a beneficial holder) separately from its remaining proposals to

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recommendations as standards in substantially the form they were made by the Committee and adopted by the NYSE Board. Accordingly, the format used will state a basic principle, with the additional explanation and clarifications included as "commentary."

While many of the requirements set forth in this new rule are relatively specific, the Exchange is articulating a philosophy and approach to corporate governance that companies are expected to carry out as they apply the requirements to the specific facts and circumstances that they confront from time to time. Companies and their boards are expected to apply the requirements carefully and in good faith, making reasonable interpretations as necessary, and disclosing the interpretations that they make.

7 The Exchange has traditionally applied its corporate governance standards to listed closed-end management companies. The Exchange considers the significantly expanded standards and requirements provided for in proposed Section 303A to be unnecessary for closed-end management companies given the pervasive federal regulation applicable to them. However, closed-end management companies will be required to continue to comply with the audit committee requirements, as they are enhanced and expanded in proposed subsections (6) and (7) of Section 303A.

facilitate SEC processing. The Exchange made this separate filing with the SEC on October 7, 2002, and it was published for public comment on October 8, 2002.[8]

The SEC has now requested that the NYSE excerpt from the NYSE Corporate Governance Proposals and file separately the provisions related to director independence, to enable the Commission to address the issue separately from the remainder of the NYSE Corporate Governance Proposals. Accordingly, this filing contains subsections (1) and (2) of proposed Section 303A of the Manual, amended in certain respects from the provisions as originally filed in SR-NYSE-2002-33.[9] It is our understanding that the SEC wishes to publish these subsections for public comment prior to publishing the remainder of the NYSE Corporate Governance Proposals, but that it does not intend to approve or make these provisions effective prior to the remainder of the NYSE Corporate Governance Proposals. Rather, the remaining proposals will be published for comment in a separate filing, and it is expected that the NYSE Corporate Governance Proposals will be given final approval and made effective as a whole, albeit with different transition mechanisms or effective dates for particular provisions.

The Exchange wishes to point out three items that arise as a result of the substance or process of the enactment of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act") and the SEC's implementing rules.

Immediate Family

Certain close family relationships preclude independence under our proposal rule. The operative definition of "immediate family" is unchanged from that contained in SR-NYSE-

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8 See Securities Exchange Act Release No. 46620 (October 8, 2002); 67 FR 63486 (October 11, 2002) (SR-NYSE-2002-46).

9 The amended provisions utilize certain specific financial criteria in lieu of the previously proposed employment test. The amended proposals also phase in "look-back" or

2002-33, which in turn is the same as that employed in the NYSE's current rule regarding the independent audit committee.[10]

When the SEC proposed its rules implementing Section 301 of the Sarbanes-Oxley Act, it proposed a more limited concept of family. The Exchange defines "immediate family" as including "a person's spouse, parents, children, siblings, mothers-in-law and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, and anyone (other than employees) who shares such person's home." The SEC proposal includes only a person's spouse, minor children or stepchildren or children or stepchildren sharing the director's home.

Foreign Private Issuers

The Exchange wishes to clarify that, as applied to foreign private issuers, its corporate governance standards continue generally to defer to home-country practices. In proposed Section 303A (11) of the NYSE Corporate Governance Proposals, the NYSE noted that, "Both SEC rules and NYSE policies have long recognized that foreign private issuers differ from domestic companies in the regulatory and disclosure regimes and customs they follow, and that it is appropriate to accommodate those differences."

The Sarbanes-Oxley Act provides that the Exchange must require foreign private issuers to comply with the independent audit committee requirements set forth in Section 301 of the Sarbanes-Oxley Act, as implemented by the SEC rules. However, consistent with the traditional NYSE approach, the Exchange would require listed foreign private issuers to comply only with the independence requirements of Section 301 of the Sarbanes-Oxley Act and the SEC rule adopted thereunder, but not with any additional proposed independence requirements to be

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"cooling-off" periods, rather than apply them immediately. In this way, directors are not retroactively disqualified for affiliations that were permissible in the past.

[10] Section 303.02(A) of the Manual.

codified in Sections 303A (1) and (2) of the Manual. Listed foreign private issuers disclose to the public any significant ways in which their home-country corporate governance practices differ from those followed by domestic companies under NYSE listing standards.

Effective Date of Independence Standards

Regarding the effective date of these new standards, companies that do not already have majority-independent boards will need time to recruit qualified independent directors, and companies with classified boards may need additional time to implement the new standards in a series of director elections. Accordingly, all listed companies will be required to comply with these standards no later than eighteen months following SEC approval of these proposed Exchange rules. If, for example, the final NYSE rules are approved by the SEC on October 31, 2003, the practical effect would be that companies desiring to deal with this matter at their annual shareholder meeting will have until their first annual meeting held after April 30, 2004 to come into compliance.

It is also appropriate to give companies with classified boards additional time to comply if a change would be required for a director who would not normally stand for election in the first annual meeting after April 30, 2004. In such cases the company will have an additional year to effect the change in that director position.

Companies listing in conjunction with their initial public offering must comply within 24 months of listing. Companies listing upon transfer from another market will have 24 months from the date of transfer in which to comply with this standard 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 the rule, which period had not yet expired, the company will have at least as long a transition period as would have been available to it on the other market.

Independence Standards

The following are the NYSE's proposed requirements relating to director independence as proposed to be codified in Sections 303A (1) and (2) of the Manual.

Section 303A

1. Listed companies must have a majority of independent directors.

Commentary: Effective boards of directors exercise independent judgment in carrying out their responsibilities. Requiring a majority of independent directors will increase the quality of board oversight and lessen the possibility of damaging conflicts of interest.

A company of which more than 50% of the voting power is held by an individual, a group or another company need not have a majority of independent directors on its board or have nominating/corporate governance and compensation committees composed of independent directors.[11] A controlled company that chooses to take advantage of this exemption must disclose in its annual meeting proxy that it is a controlled company and the basis for that determination. However, all controlled companies must have at least a minimum three person audit committee composed entirely of independent directors, and otherwise comply with the audit committee requirements provided for in this Section 303A.

2. In order to tighten the definition of "independent director" for purposes of these standards:

(a) No director qualifies as "independent" unless the board of directors affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or

[11] The Exchange notes that this exemption will affect only a small percentage of its listed companies.

officer of an organization that has a relationship with the company). Companies must disclose these determinations.

<u>Commentary</u>: It is not possible to anticipate, or explicitly to provide for, all circumstances that might signal potential conflicts of interest, or that might bear on the materiality of a director's relationship to a listed company. Accordingly, it is best that boards making "independence" determinations broadly consider all relevant facts and circumstances. In particular, when assessing the materiality of a director's relationship with the company, the board should consider the issue not merely from the standpoint of the director, but also from that of persons or organizations with which the director has an affiliation. Material relationships can include commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships (among others). However, as the concern is independence from management, the Exchange 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 company's annual proxy statement. In this regard, a board may adopt and disclose categorical standards to assist it in making determinations of independence 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. A company must disclose any standard it adopts. It may then make the general statement that the independent directors meet the standards set by the board without detailing particular aspects of the immaterial relationships between individual directors and the company (except where there is a presumption of non-independence, as described in the commentary to Paragraph 2(b) below). In the event that a director with a business or other relationship that does not fit within the disclosed standards is determined to be independent, a board must disclose the basis for its determination.

This approach provides investors with an adequate means of assessing the quality of a board's independence and its independence determinations while avoiding excessive disclosure of immaterial relationships.

(b) In addition:

(i) 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 presumed not to be independent until five years after he or she ceases to receive more than $100,000 per year in such compensation.

Commentary: A listed company's board may negate this presumption with respect to a director if the board determines (and no independent director dissents) that, based upon the relevant facts and circumstances, such compensatory relationship is not material. Any affirmative determination of independence made by the board in these circumstances must be specifically explained in the listed company's proxy statement and cannot be covered by a categorical standard adopted in accordance with the commentary to Paragraph 2(a) above. If a person who received more than $100,000 per year in direct compensation from a listed company dies or becomes incapacitated, the presumption of non-independence applicable to his or her immediate family members will cease immediately upon such death or determination of incapacity.

(ii) 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 auditor of the company is not "independent"

until five years after the end of either the affiliation or the auditing relationship.

(iii) 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 serves on that company's compensation committee is not "independent" until five years after the end of such service or the employment relationship.

(iv) A director who is an executive officer or an employee, or whose immediate family member is an executive officer, of another company (A) that accounts for at least 2% or $1 million, whichever is *greater*, of the listed company's consolidated gross revenues, or (B) for which the listed company accounts for at least 2% or $1 million, whichever is *greater*, of such other company's consolidated gross revenues, in each case is not "independent" until five years after falling below such threshold.

Commentary: An "immediate family member" includes 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 employees) who shares such person's home.

Transition Rule. During the five years immediately following [insert the effective date of this listing standard], each five year "look back" period referenced in sub-paragraphs (b)(i) through (b)(iv) shall instead be the period since [insert effective date of this listing standard]. For example, if a director received in excess of $100,000 per year in direct compensation from a listed company during the year prior to [insert effective date of this listing standard], there will

be no required presumption that the director is not independent unless such compensatory relationship extended past [insert effective date of this listing standard].

2. Statutory Basis

The basis under the Act for this proposed rule change is the requirement under Section 6(b)(5) of the Act[12] that an exchange have rules that are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to, and perfect the mechanism of a free and open market and, in general, to protect investors and the public interest.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

While the comments received by the Exchange were addressed to the Committee Recommendations in their entirety, the Exchange will summarize here those comments that were most specifically directed to the proposals contained in subsections 1 and 2 of proposed Section 303A.

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[12] 15 U.S.C. 78f(b)(5).

Overview

A. Widespread Support for the Recommendations.

The vast majority of commentators, including listed companies, institutional investors, and other interested organizations and individuals enthusiastically embraced the Committee's recommendations for new corporate governance and listing standards for the NYSE.

B. Concerns of Smaller Companies

While most large companies, law firms and institutions expressed general support for the proposals, commentators who characterized themselves as smaller businesses voiced concern. All of these companies complained that the recommendations seem to have been structured for a large-company model, without taking into account the disproportionate impact the proposed rules would have on smaller companies. In particular, they argued that the Committee's recommendations for separate nominating and compensation committees, together with its requirement of majority-independent boards, combined to effectively require that smaller companies enlarge their relatively small boards. These constituents were particularly concerned with the increased costs that compliance with the recommendations would entail. They argued that this will cause the diversion of shareholder value to unrelated third parties and the misdirection of board and management time and effort from productive to bureaucratic activities.

C. Difficulty of Obtaining Independent Directors

Several large companies expressed concern that the new rules will make it more difficult for companies to find quality independent directors because of the increased responsibilities and time commitment that the rules will require of independent directors (especially audit committee members), as well as a perceived increase in such directors' exposure to liability.

Majority-Independent Boards

Many commentators applauded the recommendation that listed companies be required to maintain majority-independent boards. However, numerous constituents, large and small, raised concerns that the requirement would have a variety of adverse consequences.

A. Controlled Companies

Most prominently, more than half of the commenting companies noted that the majority independent board requirement would create insuperable difficulties for companies controlled by a shareholder or parent company. They argued that the rule would be inequitable as applied to them in that it would deprive a majority holder of its shareholder rights; unnecessary in that the Committee's other recommendations (in particular the independent committee and disclosure requirements) would adequately protect minority shareholders; and undesirable in that it would reduce access to capital markets by discouraging spin-offs, by inducing some currently public companies to go private rather than lose control of their subsidiary, and by discouraging those who manage buyout funds and venture capital funds from using initial public offerings and NYSE listings as a means for achieving liquidity and raising capital. One company argued that the majority-independent board requirement would vitiate the ability of a parent to effectively manage its subsidiary, in the process denying to shareholders of the parent the benefits associated with its controlling stake in the subsidiary and requiring them instead to transfer control of the subsidiary to third parties.

Similarly, commentators suggested that companies that are majority-owned by officers and directors should be exempt from this recommendation. One such company argued that where corporate insiders own a majority of the stock of a company, the interests of outside minority shareholders can be adequately protected by the proposed requirement of an independent compensation committee. Family-owned companies also expressed concern with

the majority-independence requirement because the proposal would limit the families' involvement with the board.

One commenter specifically stated that even controlled companies should be subject to the majority independence requirement. This commenter was particularly concerned with dual class companies where an investor or group can control voting power without owning a majority of the company's outstanding shares.

The provision in subsection (1) of Section 303A exempting controlled companies from the requirements to have a majority independent board and independent nominating and compensation committees is intended to address the bulk of these comments.

Tighter "Independent Director" Definition

Most commentators were in favor of tightening the definition of "independence," with only a quarter advocating the continued use of existing standards. Certain institutional investors praised with particular emphasis the five-year look-back on compensation committee interlocks. However, commentators have raised several general questions, described below, as well as numerous specific questions with respect to materiality determinations.

A. Share Ownership

Many commentators expressed a desire for additional clarification of the interaction between share ownership and independence. Several commentators opposed viewing any degree of share ownership as a per se bar to "independence" (absent such other factors as an employment relationship or other financial or personal tie to the company). They argued that directors who own or represent institutions that own very significant economic stakes in the listed companies are often effective guardians of shareholders' interests not only as members of the full board but also of compensation and nominating committees, while directors whose only stake in the membership on the board is the director's fee may be unduly loyal to management.

Several venture capitalists raised a similar concern that they will run afoul of the new independence definition, even though venture capitalists, acting as fiduciaries to funds with significant shareholdings, typically have all the qualities that the independent director definition is intended to ensure. The question of the impact of ownership on independence was particularly vexing to companies with listed subsidiaries. They were concerned that a director who is deemed independent with respect to a parent company may not be considered independent with respect to the parent-controlled subsidiary.

The Exchange has clarified in subsection (2) of Section 303A that, since the concern is independence from management, ownership of even a significant amount of stock, by itself, is not necessarily a bar to an independence finding.

B. Safe Harbors for Independence Determinations

Several financial institutions specifically applauded the committee's recommendation that non-materiality determinations be made on a case-by-case basis and publicly disclosed and justified. However, a number of companies objected to the affirmative determination requirement, requesting that the NYSE specify a safe harbor for materiality. These companies cite the competing demands on the board's time and attention; the likelihood that the "no material relationship" requirement will unduly shrink the pool of qualified directorship candidates; and the possibility that the fact-specific inquiry required will expose directors to additional scrutiny and potential liability, which they may be unwilling to assume without additional compensation and/or protection.

Many commentators would like to be able to fulfill their affirmative determination requirement through the establishment of their own safe harbors. For example, one commentator attached a detailed safe harbor proposal covering various types of credit transactions. In addition, a vast majority of commenting banks and financial institutions asked for clarification

regarding the treatment of loans to directors. In light of the existing regulatory framework that controls relationships between a bank and its directors and affiliated entities, banks desired to establish categorically that arm's-length loans to directors do not negate independence. Numerous companies and organizations argue that if there are no material relationships, the NYSE should allow the statement of reasons for the board's determination of independence to be omitted from the proxy statement, and suggest that the rules should not require details of each relationship regardless of size.

The Exchange has clarified in subsection (2) of Section 303A that categorical standards are permissible.

C. Five-Year Cooling-Off Period

More than half of the companies commenting on this issue protested that five years is too long, advocating a two-to-three year period instead. Five companies, reflecting their individual circumstances, requested an exemption for interim CEOs who have served for less than one year. One commentator objected to subjecting all former employees to the cooling-off period, recommending that the prohibition be limited to former executive officers only. Several commentators agreed with the five-year period for former employees, but found the period too long with respect to compensation committee interlocking directorates. Notably, one company thought that the five-year look-back on interlocking directorates would strain parent-subsidiary relations. Likewise, one parent of a controlled public subsidiary expressed its belief that its executives should be able to sit on the subsidiary's compensation committee to ensure that subsidiary's compensation policies are compatible with those of its parent. In addition, a few companies asked whether the inquiry ends by examining the present and past relationships at companies where directors are currently employed, or if one must search back for possible interlocks at companies that may have since been acquired or dissolved – pointing out that with

the immediate family overlay to the rule, the latter inquiry could become extremely cumbersome. Several financial institutions (along with several smaller companies) took issue with the blanket exclusion of family members for five years. One company argued that when a family member's relationship has terminated, there should be independence. Another commentator recommended that relatives of deceased or disabled former officers be classified as independent as long as they themselves have no financial involvement other than ownership in the company. Another commenter expressed concern that the proposal relating to a family member employed by a company's auditor or former auditor did not limit the prohibition to employees of an audit firm who were involved with the audit or who influenced the audit.

The Exchange has clarified several of these issues with specified provisions in subsection (2)(b) of Section 303A.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

A. by order approve the proposed rule change, or

B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street N.W., Washington, D.C. 20549.

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room in 450 Fifth Street, N.W., Washington, D.C. 20549.

Copies of such filing will also be available for inspection and copying at the principal office of the above-mentioned self-regulatory organization. All submissions should refer to the file number in the caption above and should be submitted by [insert date 21 days from date of publication].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[13]

Margaret H. McFarland
Deputy Secretary

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[13] 17 CFR 200.30-3(a)(12).

Exhibit A

Text of the Proposed Rule Change
(All language is new)

Listed Company Manual

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303.00 Corporate Governance Standards

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Section 303A

1. Listed companies must have a majority of independent directors.

Commentary: Effective boards of directors exercise independent judgment in carrying out their responsibilities. Requiring a majority of independent directors will increase the quality of board oversight and lessen the possibility of damaging conflicts of interest.

A company of which more than 50% of the voting power is held by an individual, a group or another company need not have a majority of independent directors on its board or have nominating/corporate governance and compensation committees composed of independent directors.[1] A controlled company that chooses to take advantage of this exemption must disclose in its annual meeting proxy that it is a controlled company and the basis for that determination. However, all controlled companies must have at least a minimum three person audit committee composed entirely of independent directors, and otherwise comply with the audit committee requirements provided for in this Section 303A.

2. In order to tighten the definition of "independent director" for purposes of these standards:

(a) No director qualifies as "independent" unless the board of directors affirmatively determines that the 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). Companies must disclose these determinations.

Commentary: It is not possible to anticipate, or explicitly to provide for, all circumstances that might signal potential conflicts of interest, or that might bear on the materiality of a director's relationship to a listed company. Accordingly, it is best that boards making "independence" determinations broadly consider all relevant facts and circumstances. In particular, when assessing the materiality of a director's relationship with the company, the board should consider the issue not merely from the standpoint of

[1] The Exchange notes that this exemption will affect only a small percentage of its listed companies.

the director, but also from that of persons or organizations with which the director has an affiliation. Material relationships can include commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships (among others). However, as the concern is independence from management, the Exchange 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 company's annual proxy statement. In this regard, a board may adopt and disclose categorical standards to assist it in making determinations of independence 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. A company must disclose any standard it adopts. It may then make the general statement that the independent directors meet the standards set by the board without detailing particular aspects of the immaterial relationships between individual directors and the company (except where there is a presumption of non-independence, as described in the commentary to Paragraph 2(b) below). In the event that a director with a business or other relationship that does not fit within the disclosed standards is determined to be independent, a board must disclose the basis for its determination. This approach provides investors with an adequate means of assessing the quality of a board's independence and its independence determinations while avoiding excessive disclosure of immaterial relationships.

(b) In addition:

(i) 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 presumed not to be independent until five years after he or she ceases to receive more than $100,000 per year in such compensation.

<u>Commentary</u>: A listed company's board may negate this presumption with respect to a director if the board determines (and no independent director dissents) that, based upon the relevant facts and circumstances, such compensatory relationship is not material. Any affirmative determination of independence made by the board in these circumstances must be specifically explained in the listed company's proxy statement and cannot be covered by a categorical standard adopted in accordance with the commentary to Paragraph 2(a) above. If a person who received more than $100,000 per year in direct compensation from a listed company dies or becomes incapacitated, the presumption of non-independence applicable to his or her immediate family members will cease immediately upon such death or determination of incapacity.

(ii) 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 auditor of the company is not "independent"

until five years after the end of either the affiliation or the auditing relationship.

(iii) 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 serves on that company's compensation committee is not "independent" until five years after the end of such service or the employment relationship.

(iv) A director who is an executive officer or an employee, or whose immediate family member is an executive officer, of another company (A) that accounts for at least 2% or $1 million, whichever is *greater*, of the listed company's consolidated gross revenues, or (B) for which the listed company accounts for at least 2% or $1 million, whichever is *greater*, of such other company's consolidated gross revenues, in each case is not "independent" until five years after falling below such threshold.

Commentary: An "immediate family member" includes 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 employees) who shares such person's home.

Transition Rule. During the five years immediately following [insert the effective date of this listing standard], each five year "look back" period referenced in sub-paragraphs (b)(i) through (b)(iv) shall instead be the period since [insert effective date of this listing standard]. For example, if a director received in excess of $100,000 per year in direct compensation from a listed company during the year prior to [insert effective date of this listing standard], there will be no required presumption that the director is not independent unless such compensatory relationship extended past [insert effective date of this listing standard].

3. – 13. Reserved.

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Exhibit 2

Written Comment on the Proposed Rule

1. Comment letter of the Council of Institutional Investors, dated November 8, 2002.

2. Comment letter of Three-Five Systems, Inc., dated December 10, 2002.

Earlier comment letters received by the NYSE with respect to this proposal were previously provided to the SEC in connection with SR-NYSE-2002-33.