

*minimis* or immaterial fees to make the requirement less restrictive.<sup>60</sup>

We are not persuaded that such an exception is an appropriate deviation from the explicit mandate in Exchange Act section 10A(m). We believe the policies and purposes behind that section, and particularly the use of the term “any” when describing such fees in the statute, weighs against providing for such an exception. Further, given the narrow class of services covered by the final rule, the lack of a *de minimis* exception should be less necessary. Moreover, if the level of compensation that the member or associated entity receives is truly *de minimis* and immaterial, we are not persuaded that requiring an issuer to locate another provider so that the member can remain qualified for audit committee service would be overly burdensome. In section II.F.5, we provide a limited accommodation to address the concerns by some commenters regarding an audit committee member that ceases to be independent for reasons outside the member’s reasonable control.

### 3. Affiliated Person of the Issuer or Any Subsidiary Thereof

Consistent with the express requirement in Exchange Act section 10A(m)(3)(B)(ii), the second basic criterion for determining independence is that a member of the audit committee of an issuer that is not an investment company may not be an affiliated person of the issuer or any subsidiary of the issuer apart from his or her capacity as a member of the board and any board committee. Consistent with the Proposing Release, we are defining the terms “affiliate” and “affiliated person” consistent with our other definitions of these terms under the securities laws, such as in Exchange Act rule 12b-2<sup>61</sup> and Securities Act rule 144,<sup>62</sup> with an additional safe harbor.<sup>63</sup> We are defining “affiliate” of, or a person “affiliated” with, a specified person, to mean “a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with,

the person specified.”<sup>64</sup> We are defining the term “control” consistent with our other definitions of this term under the Exchange Act<sup>65</sup> as “the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise.”<sup>66</sup> Commenters generally supported this approach.<sup>67</sup>

Our definition of “affiliated person” for non-investment companies, like our existing definitions of this term for these issuers, requires a factual determination based on a consideration of all relevant facts and circumstances. To facilitate the analysis on facts and circumstances where we are presumptively comfortable, we are adopting a safe harbor for that aspect of the definition of “affiliated person,” with minor modifications from the original proposal.<sup>68</sup> Under the safe harbor as adopted, a person who is not an executive officer or a shareholder owning 10% or more of any class of voting equity securities of a specified person will be deemed not to control such specified person.<sup>69</sup> Many commenters supported the safe harbor and the certainty it will provide to non-affiliates.<sup>70</sup> We have clarified in the final rule, in response to several commenter suggestions, that the ownership prong should be based on ownership of any class of voting equity securities, instead of any class of equity securities.

The Proposing Release specified that those that cannot rely on the safe harbor would not be deemed to be or presumed to be affiliates. Those persons would

need to conduct a facts and circumstances analysis of control. Nevertheless, some commenters and others reporting on the proposals were concerned that the 10% shareholder prong in the safe harbor somehow is, is implied to be, or would become viewed as an upper ownership limit for non-affiliate status.<sup>71</sup> We have no intention of this being the case. While SROs in their listing rules could establish an upper ownership limit that would preclude independence, the safe harbor in Exchange Act Rule 10A-3 does not establish such a limit. The safe harbor is designed to identify a group of those that are *not* affiliates so as to provide comfort to those individuals or entities that no additional facts and circumstances analysis is necessary. It only creates a safe harbor position for non-affiliate status. Failing to meet the 10% ownership threshold has no bearing on whether a particular person is an affiliate based on an evaluation of all facts and circumstances. A director who is not an executive officer but beneficially owns more than 10% of the issuer’s voting equity could be determined to be not an affiliate under a facts and circumstances analysis of control.

We continue to believe that a 10% ownership limit is an appropriate threshold to presume (along with the other aspects of the safe harbor) that a person is *not* an affiliate. Accordingly, we are not changing that threshold. However, the safe harbor does not in any way specify or imply that a certain level of share ownership automatically presumes that a person is an affiliate. To prevent further misconceptions, we have added an explicit paragraph to the final rule to reinforce these points.

We received several comments regarding how beneficial ownership is to be determined for purposes of the safe harbor, as well as for other aspects of the rule, such as the multiple listing exception. Accordingly, we have included an instruction to the final rule to clarify that calculations of beneficial ownership are to be made consistent with Exchange Act rule 13d-3.<sup>72</sup>

The proposed rules would have deemed a director, executive officer, partner, member, principal or designee of an affiliate to be an affiliate. While some commenters expressed specific

<sup>60</sup> See, e.g., the Letters of AICPA; America’s Community Bankers; American Bankers Association; American Stock Exchange, Inc. (“Amex”); Cleary; Cravath; Ford Motor Company; NYCBA; PwC; S&C.

<sup>61</sup> 17 CFR 240.12b-2.

<sup>62</sup> 17 CFR 230.144.

<sup>63</sup> Exchange Act section 3(a)(19), in defining several terms in relation to investment companies, includes a definition of “affiliated person” by reference to the Investment Company Act. Because that definition is tailored to investment companies, the definition in Exchange Act Rule 10A-3 uses a definition for non-investment companies consistent with our other definitions of “affiliate” for non-investment companies.

<sup>64</sup> See Exchange Act Rule 10A-3(e)(1)(i).

<sup>65</sup> See, e.g., Exchange Act Rule 12b-2.

<sup>66</sup> See Exchange Act Rule 10A-3(e)(4).

<sup>67</sup> See, e.g., the Letters of ABA; Cleary; CSC; Matsushita Electric Industrial Co., Ltd. (“Matsushita”); PwC; Greg Swallow.

<sup>68</sup> See Exchange Act rule 10A-3(e)(1). Note that this safe harbor does not address the question of whether a person “is controlled by, or is under common control with” the issuer. We proposed a similar safe harbor from the definition of “affiliate” for Securities Act rule 144 in 1997. See Release No. 33-7391 (Feb. 20, 1997) [62 FR 9246].

<sup>69</sup> The Proposing Release also would have included a requirement that the person not be a director. Several commenters pointed out that this requirement is ambiguous because all audit committee members would be directors and the affiliate prohibition would already exclude capacity as a director. Accordingly, that requirement has been removed in the final rule. Also, the final rule clarifies that the safe harbor is available not just for determinations with respect to the issuer, but to any “specified person.” Thus, it is also available for determinations with respect to subsidiaries of the issuer, which are also covered by the affiliate prohibition.

<sup>70</sup> See, e.g., the Letters of Cleary; CSC; Matsushita; Nippon Keidanren (Japan Business Federation); PwC; Greg Swallow.

<sup>71</sup> See, e.g., the Letters of ABA; Cravath; National Venture Capital Association; The News Corporation Limited. See also Roberta S. Karmel, “Federalization of the Law Regarding Audit Committees,” *New York Law Journal*, vol. 229, p. 3 (Feb. 20, 2003).

<sup>72</sup> 17 CFR 240.13d-3.