

questions that may arise regarding financial reporting and compliance with the securities laws. Accordingly, the proposed rule would specifically require an issuer's audit committee to have the authority to engage outside advisors, including counsel, as it determines necessary to carry out its duties.<sup>69</sup>

*Questions regarding the proposed authority to engage advisors requirement:*

- Is any additional specificity needed for this requirement? For example, should we define what constitutes an "independent advisor?"

#### E. Funding

An audit committee's effectiveness may be compromised if it is dependent on management's discretion to compensate the independent auditor or the advisors employed by the committee, especially when potential conflicts of interest with management may be apparent. Accordingly, the proposed rule would require the issuer to provide for appropriate funding, as determined by the audit committee, in its capacity as a committee of the board of directors, for payment of compensation:

- To any registered public accounting firm engaged for the purpose of rendering or issuing an audit report or related work or performing other audit, review or attest services for the listed issuer; and
- To any advisors employed by the audit committee.

This proposed requirement would further the proposed standard relating to the audit committee's responsibility to appoint, compensate, retain and oversee the outside auditor. It also would add meaning to the proposed standard relating to the audit committee's authority to engage independent advisors. Not only could an audit committee be hindered in its ability to perform objectively its duties by not having control over the ability to compensate these advisors, but the role of the advisors also could be compromised if they are required to rely on management for compensation. Thus, absent such a provision, both the audit committee and the advisors could be less willing to address disagreements or other issues with management.

*Questions regarding the proposed funding requirement:*

- Is any additional specificity needed for this requirement? For example,

should a specific agreement or arrangement be required to provide for the appropriate funding?

- Should there be any limit on the amount of compensation that could be requested by the audit committee? If so, who should set these limits (e.g., the full board)? Should the audit committee's request be limited to "reasonable" compensation? Who would determine what is "reasonable"? How would such limits be consistent with the policy and purposes of the Sarbanes-Oxley Act? Is the fact that the audit committee members ultimately are elected by, and answerable to, shareholders sufficient to address any concern over compensation limits?

#### F. Application and Implementation of the Proposed Standards

##### 1. SROs Affected

Section 10A(m) of the Exchange Act by its terms applies to all national securities exchanges and national securities associations. These entities, to the extent that their listing standards do not already comply with the proposals, will be required to issue or modify their rules, subject to Commission review, to conform their listing standards.<sup>70</sup> Under our proposals, the new requirements would need to be operative by the SROs no later than the first anniversary of the publication of our final rule in the **Federal Register**. The SROs are not precluded from adopting additional listing standards regarding audit committees, as long as they are consistent with the proposed rule.

To facilitate timely implementation of the proposals, we propose that each SRO must provide to the Commission, no later than 60 days after publication of our final rule in the **Federal Register**, proposed rules or rule amendments that comply with our final rule. Further, each SRO would need to have final rule or rule amendments that comply with our final rule approved by the Commission no later than 270 days after publication of our final rule in the **Federal Register**. We request comment below on the appropriateness of these periods.

The OTC Bulletin Board (OTCBB), the Pink Sheets and the Yellow Sheets would not be affected by the proposed requirements, and therefore issuers whose securities are quoted on these interdealer quotation systems similarly would not be affected, unless their securities also are listed on an exchange

or Nasdaq.<sup>71</sup> Each of these quotation systems does not provide issuers with the ability to list their securities, but is a quotation medium for the over-the-counter securities market that collects and distributes market maker quotes to subscribers. These interdealer quotation systems do not maintain or impose listing standards, nor do they have a listing agreement or arrangement with the issuers whose securities are quoted through them. Although market makers may be required to review and maintain specified information about the issuer and to furnish that information to the interdealer quotation system,<sup>72</sup> the issuers whose securities are quoted on such systems do not have any filing or reporting requirements with the system.<sup>73</sup>

*Questions regarding the proposed application to SROs*

- Do the proposed implementation dates provide sufficient time for SROs to propose and obtain Commission approval for new or amended rules to meet the requirements of the proposals? Is the date by when the standards would need to be operative appropriate? If not, what other dates would be appropriate? What factors should the Commission consider in determining these dates?

##### 2. Securities Affected

In enacting Section 10A(m) of the Exchange Act, Congress made no distinction regarding the type of securities to be covered. Section 10A(m)(1)(A) of the Exchange Act prohibits the listing of "any security" of an issuer that does not meet the new standards for audit committees. Accordingly, the proposed rule would apply not just to voting equity securities, but to any listed security, regardless of its type, including debt securities, derivative securities and other types of listed securities. We believe investors in all securities of an issuer, whether common equity or fixed income, would benefit from the increased financial oversight of an issuer that would result from a strong and effective audit committee.

<sup>71</sup> The OTCBB is operated by The Nasdaq Stock Market, Inc., which is owned by the NASD. Information about the OTCBB can be found at [www.otcbb.com](http://www.otcbb.com). The Pink Sheets and the Yellow Sheets (as well as the corresponding Electronic Quotation Service) are operated by Pink Sheets LLC. Information about the Pink Sheets, the Yellow Sheets and the Electronic Quotation Service can be found at [www.pinksheets.com](http://www.pinksheets.com).

<sup>72</sup> See 17 CFR 240.15c2-11.

<sup>73</sup> However, under OTCBB rules, issuers of securities quoted on the OTCBB must be subject to periodic filing requirements with the Commission or other regulatory authority. See NASD Rule 6530.

<sup>69</sup> The proposed requirement would not preclude access to or advice from the company's internal counsel or regular outside counsel. It also would not require an audit committee to retain independent counsel.

<sup>70</sup> An SRO that wished to do so could satisfy the requirements of the rule by requiring that a listed issuer must comply with Exchange Act Rule 10A-3.