

Commission notes that the NYSE proposes an additional requirement that an issuer must notify it in writing when it uses this exemption from the shareholder approval requirement. Nasdaq has also committed to considering similar disclosure requirements. The Commission believes that such disclosure requirements would provide transparency to investors and reduce the potential for abuse of this exemption for inducement grants.<sup>119</sup>

In addition, one commenter pointed out an inconsistency between the NYSE and Nasdaq proposals—that the exemption for inducement grants as proposed in the Notice of the Nasdaq Proposal would exclude grants to previous employees and directors of the company, while the exemption for inducement grants as proposed in the Notice of the NYSE Proposal would allow grants to all new employees. In response to these concerns, the NYSE and Nasdaq clarified their respective exemptions for inducement grants and limited the exemptions to new employees or to previous employees being rehired after a bona fide period of interruption of employment, and to new employees in connection with an acquisition or merger. The Commission believes that these amendments to the exemption for inducement grants in the NYSE and Nasdaq proposals are consistent with the original intent of the exemption. The language requiring a bona fide period of interruption of employment for previous employees should help to prevent the inducement exemption from being used inappropriately. Furthermore, the proposed changes should address the commenters' concerns about consistency between the NYSE and Nasdaq proposals.

#### *B. Exemption From Shareholder Approval for Mergers and Acquisitions*

The Commission notes that several commenters objected to an exemption from shareholder approval for plans acquired in a merger or acquisition. These commenters stated that additional issuances under plans to shareholders of the acquired or targeted company could be dilutive to shareholders of the acquiring company. The commenters were also concerned that companies could use a merger or acquisition to acquire a plan that would otherwise not be approved by their shareholders.

While the Commission understands these concerns, it notes that both the

NYSE and Nasdaq exemptions contain safeguards that should prevent abuse in this area. First, only pre-existing plans that were previously approved by the acquired company's shareholders would be available to the listed company for post-transactional grants. In addition, shares under those previously approved plans could not be granted to individuals who were employed, immediately before the transaction, by the post-transaction listed company or its subsidiaries. The Commission also notes that, under both the NYSE and Nasdaq proposals, any shares reserved for listing in connection with a merger or acquisition pursuant to this exemption would be counted by the NYSE and Nasdaq in determining whether the transaction involved the issuance of 20% or more of the company's outstanding common stock, thereby requiring shareholder approval under the appropriate NYSE and Nasdaq rules. Finally, the Commission notes that the NYSE proposes an additional requirement that an issuer must notify it in writing when it uses this exemption from the shareholder approval requirement. Based on the above, the Commission believes that the NYSE and Nasdaq have provided measures to ensure that the exemption for mergers and acquisitions is only used in limited circumstances, which should help reduce the potential for dilution of shareholder interests.

#### *C. Exemption From Shareholder Approval for Tax Qualified and Parallel Nonqualified Plans*

Several commenters were critical of the exemption from shareholder approval for tax qualified and parallel nonqualified plans<sup>120</sup> and stated that these plans should be subject to shareholder approval. Many of these commenters were concerned that these types of plans are structured in a way to benefit only highly compensated employees and that participants in such plans could defer up to 100% of their compensation in stock under these plans.

The Commission believes that, given the extensive government regulation—the Internal Revenue Code and Treasury regulations—for qualified plans and the general limitations associated with parallel nonqualified plans, shareholders should not experience significant dilution as a result of this exemption. In addition, the Commission notes that NYSE and Nasdaq are

proposing to add an additional limitation under this exemption that a plan would not be considered a nonqualified parallel under the Nasdaq proposal or parallel excess plan under the NYSE proposal if employees who are participants in such plans receive employer contributions under the plans in excess of 25% of the participants' cash contributions. The Commission further notes that the NYSE proposes an additional requirement that an issuer must notify it in writing when it uses this exemption from the shareholder approval requirement. The Commission believes that, taken together, these limitations should reduce concerns regarding abuse of this exemption.

#### *D. Material Amendments to Plans*

The Commission notes that several commenters urged the NYSE and Nasdaq to adopt a similar definition for what constitutes a material amendment or revision to a plan requiring shareholder approval. Specifically, these commenters stated that the NYSE and Nasdaq should adopt a more uniform and enforceable definition. One commenter suggested that material revisions to plans should only include any increases in benefits, not decreases in benefits, under a plan.

In response to these concerns, the NYSE and Nasdaq have proposed amendments to their respective proposals and provided similar definitions of a material amendment or revision. A material amendment or revision under both proposals would now basically include: A material increase in the number of shares to be issued under the plan (other than to reflect a reorganization, stock split, merger, spinoff or similar transaction); an expansion of the type of awards available under the plan; a material expansion of the class of participants eligible to participate in the plan; a material extension of the term of the plan; a material change to limit or delete any provisions prohibiting repricing of options in a plan or for determining the strike or exercise price of options under a plan. In addition, the NYSE amended its proposal under "Material Revisions" to define "evergreen" and "formula" plans and introduced the new concept of "discretionary plan." The NYSE further described what would constitute a material revision to such plans and require shareholder approval. Nasdaq also amended its proposal to clarify when plans containing a formula for automatic increases (such as evergreen plans) and automatic grants would require shareholder approval.

The Commission believes that the NYSE and Nasdaq's non-exclusive lists

<sup>119</sup> The Commission urges Nasdaq to consider adopting a disclosure requirement similar to the NYSE's requirement.

<sup>120</sup> The Commission notes that the NYSE has replaced the term "parallel nonqualified plan" in its proposal with the term "parallel excess plan." Nasdaq has retained the term "parallel nonqualified plan" to describe such plans.