

change, as amended, from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange, through its wholly owned subsidiary, PCX Equities, Inc. ("PCXE"), is proposing to amend its Corporate Governance and Disclosure Policies. The Exchange states that these changes are aimed at helping to restore investor confidence by strengthening listed companies' corporate governance practices.⁴ The text of the proposed rule change, as amended, is set forth below.⁵ Text in brackets indicates material to be deleted, and text in italics indicates material to be added.⁶

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PCX Equities, Inc.

Rule 5

Listings

Rules 5.1–5.2—No change.

Section 3. Corporate Governance and Disclosure Policies

Corporate Governance and Disclosure Policies

Rule 5.3 The Corporation shall require that specific corporate governance and disclosure policies be established by domestic issuers of any equity security listed pursuant to Rule 5.2. *Issuers of securities under the Tier I designation must comply with the provisions of Rules 5.3(c)–(o). Issuers of securities under the Tier II designation must comply with the provisions of Rules 5.3(a)–(i)(4) and 5.3(k)(5). Issuers of any*

security that is listed pursuant to the Rules of the Corporation must comply with the provisions of Rule 5.3(k)(5). [The Corporation, however, will not require an issuer of such security under the Tier II designations to comply with the provisions for an audit committee as set forth in this Rule 5.3(b).]

Rule 5.3(a)—No change.

Independent Directors [/Audit Committee]

Rule 5.3(b). Independent Directors [/Audit Committee]

The Corporation shall require that each listed domestic issuer have at least two independent directors on its board of directors. [Such issuer shall maintain an audit committee. All audit committee members shall be independent directors that satisfy the audit committee requirement set forth below.

[(1) Audit Committee Charter. The board of directors must adopt and approve a formal written charter for the audit committee. The audit committee must review and reassess the adequacy of the formal written charter on an annual basis. The charter must specify the following:

[(i) The scope of the audit committee's responsibilities and how it carries out those responsibilities, including structure, processes, and membership requirements;

[(ii) That the outside auditor is ultimately accountable to the board of directors and the audit committee of the company, that the audit committee and board of directors have the ultimate authority and responsibility to select, evaluate, and, where appropriate, replace the outside auditor (or to nominate the outside auditor to be proposed for shareholder approval in any proxy statement); and

[(iii) That the audit committee is responsible for ensuring that the outside auditor submits on a periodic basis to the audit committee a formal written statement delineating all relationships between the auditor and the company and that the audit committee is responsible for actively engaging in a dialogue with the outside auditor with respect to any disclosed relationships or services that may impact the objectivity and independence of the outside auditor and for recommending that the board of directors take appropriate action in response to the outside auditors' report to satisfy itself of the outside auditors' independence.

[(2) Composition/Expertise Requirement of Audit Committee Members.

[(i) Each audit committee will consist of at least three independent directors,

all of whom have no relationship to the company that may interfere with the exercise of their independence from management and the company ("Independent");

[(ii) Each member of the audit committee must be financially literate, as such qualification is interpreted by the company's board of directors in its business judgment, or must become financially literate within a reasonable period of time after his or her appointment to the audit committee; and

[(iii) At least one member of the audit committee must have accounting or related financial management expertise, as the Board of Directors interprets such qualification in its business judgment.

[(3) Independence Requirement of Audit Committee Members. In addition to the definition of Independent provided in 5.3(b)(2)(i), the following restrictions shall apply to every audit committee member:

[(i) Employees. A director who is an employee (including non-employee executive officers) of the company or any of its affiliates may not serve on the audit committee until three years following the termination of his or her employment. In the event the employment relationship is with a former parent or predecessor of the company, the director could serve on the audit committee after three years following the termination of the relationship between the company and the former parent or predecessor. "Affiliate" includes a subsidiary, sibling company, predecessor, parent company, or former parent company.

[(ii) Business Relationship. A director (a) who is a partner, controlling shareholder, or executive officer of an organization that has a business relationship with the company, or (b) who has a direct business relationship with the company (e.g., a consultant) may serve on the audit committee only if the company's board of directors determines in its business judgment that the relationship does not interfere with the director's exercise of independent judgment. In making a determination regarding the independence of a director pursuant to this paragraph, the board of directors should consider, among other things, the materiality of the relationship to the company, to the director, and, if applicable, to the organization with which the director is affiliated.

["Business relationships" can include commercial, industrial, banking, consulting, legal, accounting and other relationships. A director can have this relationship directly with the company, or the director can be a partner, officer

⁴ The Commission notes that the PCX will consider amendments to the proposed rule change once the Commission approves proposals on corporate governance matters filed by other exchanges. Telephone conversation between Steven B. Matlin, Senior Counsel, PCX, and Ira L. Brandriss, Special Counsel, Division of Market Regulation ("Division"), Commission, on October 23, 2003.

⁵ The rule text as set forth herein includes several minor technical revisions that the Exchange has committed to correct by filing an amendment. Telephone conversation between Steven B. Matlin, Senior Counsel, PCX, and Ira L. Brandriss, Special Counsel, Division, Commission, on October 23, 2003.

⁶ The Commission notes that the PCX listing rules provide standards for the listing of two different tiers of securities, to which the proposed rule change makes reference. As stated in PCX Rule 5.2(b): "A listing under the Tier I designation generally signifies that the company has achieved maturity and high status in its industry in terms of assets, earnings, and shareholder interest, and acceptance. The Tier II designation is limited, except for specific circumstances as discussed [earlier in the provision], to the listing of common stock, preferred stock, bonds and debentures, and warrants. A listing under the Tier II designation generally signifies that the company has limited commercial operations, lower capitalization, and lacks a demonstrated earnings history."