

identical to proposals by NYSE and Nasdaq requiring shareholder approval of equity compensation plans that have previously been approved by the Commission.<sup>15</sup> The Commission believes that it has already considered and addressed the issues that may be raised by the Exchange's proposal when it approved these proposals. The Commission notes that approval of the Exchange's proposal, as amended, will conform the Exchange's shareholder approval requirements for equity compensation plans with those of the NYSE and Nasdaq, and will immediately impose the same requirements on the Exchange's issuers as those imposed upon NYSE, Nasdaq, and Amex issuers. The adoption of these standards by the Exchange is an important step to ensure that issuers will not be able to avoid shareholder approval requirements for equity compensation plans based on their listed marketplace.

#### *A. Exemption From Shareholder Approval for Inducement Grants*

The Commission believes that the requirement that the issuance of all inducement grants be subject to review by either the issuer's independent compensation committee or a majority of the board's independent directors, under the Exchange's amended proposal, should prevent abuse of this exemption from shareholder approval. In addition, the Exchange proposes to limit its exemption for inducement grants 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 limitations should help to prevent the inducement exemption from being used inappropriately.

The Commission notes that the Exchange is proposing to include a requirement, similar to the requirement under the NYSE and Nasdaq's recently approved shareholder approval rules, that, promptly following the grant of any inducement award, companies must disclose in a press release the material terms of the award, including the recipient(s) of the award and the number of shares involved.<sup>16</sup> The

Commission notes that the Exchange is also proposing a requirement, similar to the requirements under the NYSE and Nasdaq's recently approved shareholder approval rules,<sup>17</sup> that an issuer must notify it in writing when it uses this exemption, and/or any other exemption, from its shareholder approval requirement. The Commission believes that these disclosure and notification requirements will provide transparency to investors and should reduce the potential for abuse of this exemption for inducement grants.

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

The Commission notes that the Exchange's exemption from shareholder approval for mergers and acquisitions contains 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 the Exchange's proposal, as amended, any shares reserved for listing in connection with a merger or acquisition pursuant to this exemption would be counted by the Exchange in determining whether the transaction involved the issuance of 20% or more of the company's outstanding common stock, thereby requiring shareholder approval. Finally, the Commission notes that the Exchange proposes an additional requirement that an issuer must notify it in writing when it uses this exemption, and/or any other exemption, from its shareholder approval requirement. Based on the above, the Commission believes that the Exchange has 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*

The Commission believes that, given the extensive government regulation—the Internal Revenue Code and Treasury regulations—for tax qualified plans and the general limitations associated with

shareholders and equity compensation plans that have not been approved by shareholders.

<sup>17</sup> See Section 303A(8) of the NYSE's *Listed Company Manual* and NASD Rules 4310(c)(17)(A) and 4320(e)(15)(A).

parallel nonqualified plans, shareholders should not experience significant dilution as a result of this exemption. In addition, the Commission notes that the Exchange proposes to add a limitation under this exemption that a plan would not be considered a nonqualified parallel plan under its proposal if employees who are participants in such a plan receive employer contributions under the plan in excess of 25% of the participants' cash compensation. The Commission further notes that the Exchange proposes an additional requirement that an issuer must notify it in writing when it uses this exemption, and/or any other exemption, from its shareholder approval requirement. The Commission believes that, taken together, these limitations should reduce concerns regarding abuse of this exemption from the shareholder approval requirements.

In addition, the Commission notes that, similar to the exemptions in the NYSE and Nasdaq's recently approved shareholder approval rules, the Exchange proposes to adopt an exemption from the shareholder approval requirements for an equity compensation plan that provides non-U.S. employees with substantially the same benefits as a comparable Section 401(a) plan, Section 423 plan or parallel excess plan that the listed company provides to its U.S. employees, but for features necessary to comply with applicable foreign tax law. The Commission believes that this change will conform the Exchange's shareholder approval rule to that of the NYSE and Nasdaq and will provide greater clarity for issuers regarding tax qualified, non-discriminatory employee benefit plans and parallel nonqualified plans for their non-U.S. employees.

#### *D. Material Revisions to Plans*

The Commission notes that the Exchange proposes to provide a non-exclusive list, similar to lists found in the NYSE and Nasdaq's shareholder approval rules,<sup>18</sup> as to what constitutes a material revision to a plan. As noted above, material revisions to plans will require shareholder approval under Exchange rules. A material revision under the Exchange's amended proposal would include, but is not limited to: 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

<sup>15</sup> See *supra* notes 6 and 14.

<sup>16</sup> This disclosure would, of course, be in addition to any information that is required to be disclosed in annual reports filed with the Commission. For example, Item 201(d) of Regulation S-K [17 CFR 229.201(d)] and Item 201(d) of Regulation S-B [17 CFR 228.201(d)] require issuers to present—in their annual reports on Form 10-K or Form 10-KSB—separate, tabular disclosure concerning equity compensation plans that have been approved by

<sup>18</sup> See *supra* note 6; see also *supra* note 14.