

## 2. Statutory Basis

The Exchange believes that the proposed rule change, as amended, is consistent with Section 6 of the Act,<sup>14</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act,<sup>15</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. The Exchange believes that its proposal, as amended, is intended to be essentially identical to those submitted by the NYSE and Nasdaq and approved by the Commission.<sup>16</sup>

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

Written comments on the proposed rule change were neither solicited nor received. The Exchange, however, did notify its issuers of the types of proposed rule changes that it was contemplating and has not received any objections to those proposals.

## III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying at the Commission's Public Reference

Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-CHX-2003-31 and should be submitted by November 28, 2003.

## IV. Commission's Findings and Order Granting Accelerated Approval to the Proposed Rule Change, As Amended

After careful review, the Commission finds that the Exchange's proposal, as amended, is consistent with the Act and the rules and regulations promulgated thereunder applicable to a national securities exchange and, in particular, with the requirements of Section 6(b) of the Act.<sup>17</sup> Specifically, the Commission finds that approval of the Exchange's proposal, as amended, is consistent with Section 6(b)(5) of the Act<sup>18</sup> in that it is designed to, among other things, facilitate transactions in securities; to prevent fraudulent and manipulative acts and practices; to promote just and equitable principles of trade; to remove impediments to and perfect the mechanism of a free and open market and a national market system; and, in general, to protect investors and the public interest; and does not permit unfair discrimination among issuers.

The Commission has long encouraged exchanges to adopt and strengthen their corporate governance listing standards in order to, among other things, restore investor confidence in the national marketplace. The Commission believes that the Exchange's amended proposal, which requires shareholder approval of equity compensation plans and which follows the Commission's approval of similar proposals by the NYSE, Nasdaq, and Amex<sup>19</sup> is the first step under this directive because it should have the effect of safeguarding the interests of shareholders, while placing certain restrictions on Exchange-listed companies.<sup>20</sup>

In addition, the Commission notes that the Exchange's proposal, as amended, is similar and almost identical to proposals by NYSE and

Nasdaq requiring shareholder approval of equity compensation plans that have previously been approved by the Commission.<sup>21</sup> The Commission believes that it has already considered and addressed the issues that may be raised by the Exchange's amended 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. Exception 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 exception from shareholder approval. In addition, the Exchange proposes to limit its exception 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 exception 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>22</sup> The

<sup>17</sup> 15 U.S.C. 78f(b). In approving the Exchange's proposal, as amended, the Commission has considered the proposed rule's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

<sup>18</sup> 15 U.S.C. 78f(b)(5).

<sup>19</sup> See *supra* note 4. The Commission notes that it has recently approved similar rules requiring shareholder approval of equity compensation plans for the Amex on an accelerated basis. The Amex's proposal is almost identical to, and based on, the NYSE and Nasdaq proposals. See Securities Exchange Act Release No. 48610 (October 9, 2003), 68 FR 59650 (October 16, 2003).

<sup>20</sup> The Commission notes that these new listing standards will apply to all companies listed on the CHX and will include both CHX's Tier I and Tier II designations.

<sup>21</sup> See *supra* notes 4 and 19.

<sup>22</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

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<sup>14</sup> 15 U.S.C. 78f(b).

<sup>15</sup> 15 U.S.C. 78f(b)(5).

<sup>16</sup> See *supra* note 4.