

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-CSE-2003-11 and should be submitted by November 28, 2003.

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

After careful review, the Commission finds that the Exchange's proposal 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.¹⁰ Specifically, the Commission finds that approval of the Exchange's proposal is consistent with Section 6(b)(5) of the Act¹¹ 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 proposal, which requires shareholder approval of equity compensation plans and which follows the Commission's approval of similar proposals by the NYSE, Nasdaq, and Amex¹² 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.

In addition, the Commission notes that the Exchange's proposal 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.¹³ 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 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 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.¹⁴ 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,¹⁵ 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, 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 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

¹⁰ 15 U.S.C. 78f(b). In approving the Exchange's proposal, the Commission has considered the proposed rule's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

¹¹ 15 U.S.C. 78f(b)(5).

¹² 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).

¹³ See *supra* notes 4 and 12.

¹⁴ 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 shareholders and equity compensation plans that have not been approved by shareholders.

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