

company's audit committee or another independent body of the board of directors. For purposes of the rule, "related party transactions" would refer to transactions required to be disclosed pursuant to Commission Regulation S-K, Item 404.<sup>164</sup> Nasdaq proposes that the Related Party Transactions Proposal become operative on January 15, 2004.<sup>165</sup>

### 13. Application to Foreign Issuers and Certain Other Issuers

NASD Rule 4350 currently provides that foreign issuers are not required to do any act that is contrary to a law, rule or regulation of any public authority exercising jurisdiction over such issuer or that is contrary to generally accepted business practices in the issuer's country of domicile. Currently, Nasdaq may provide exemptions from the requirements of NASD Rule 4350 as may be necessary or appropriate to carry out this intent. In the Nasdaq Issuer Applicability Proposal, as amended,<sup>166</sup> Nasdaq proposes to amend this rule and add Interpretive Material to clarify that the authority to grant exemptions from the corporate governance standards applies only to foreign private issuers and does not apply to the extent that such exemption would be contrary to the federal securities laws, including, without limitation, section 10A(m) of the Exchange Act and Rule 10A-3 thereunder. Nasdaq also proposes to provide that a foreign issuer that receives an exemption from NASD Rule 4350 would be required to disclose in its annual reports filed with the Commission each requirement from which it is exempted and describe the home country practice, if any, followed by the issuer in lieu of these requirements. In addition, a foreign issuer making its initial public offering or first U.S. listing on Nasdaq would be required to disclose any such exemptions in their registration statement.

In addition, Nasdaq proposes that management investment companies (including business development companies) would be subject to all of the requirements of NASD Rule 4350, except that management investment companies registered under the Investment Company Act would be exempt from the requirements of NASD Rule 4350(c) and (n), which pertain to board and key committee independence requirements and codes of conduct.<sup>167</sup>

Nasdaq proposed these exemptions in light of the fact that registered management investment companies are already subject to a pervasive system of federal regulation.

Finally, Nasdaq proposes that cooperative entities, such as agricultural cooperatives that are structured to comply with relevant state law and federal tax law and that do not have a publicly traded class of common stock would be exempt from NASD Rule 4350(c); however, such entities would be required to comply with all federal securities laws, including, without limitation, section 10A(m) of the Exchange Act and Rule 10A-3 thereunder.<sup>168</sup>

Nasdaq proposes that asset-backed issuers and other passive issuers,<sup>169</sup> such as unit investment trusts, would be exempt from NASD Rule 4350(c) and (n), which pertain to board and key committee independence requirements and codes of conduct, and the audit committee requirements of NASD Rule 4350(d).<sup>170</sup> Nasdaq noted that these revisions are commensurate with provisions contained in Rule 10A-3.

### 14. Proposed Implementation of New Requirements

In Amendment No. 3 to the Nasdaq Issuer Applicability Proposal,<sup>171</sup> Nasdaq proposed to set out in NASD Rule 4350(a)(5) the proposed dates by which listed companies would be required to comply with the rule changes to NASD Rules 4200 and 4350 that are the subject of this Order. In order to allow companies to make necessary adjustments in the course of their regular annual meeting schedule, and consistent with Exchange Act Rule 10A-3, the rule would establish the deadlines for compliance listed below. During the transition period between the date of approval of the rule filing by the Commission and the deadline indicated for each rule change, companies that have not brought themselves into compliance with the new rules would be required to comply with the previously existing rules, as applicable.<sup>172</sup>

<sup>168</sup> *Id.*

<sup>169</sup> These are issuers that are organized as trusts or other unincorporated associations that do not have a board of directors or persons acting in a similar capacity and whose activities are limited to passively owning or holding (as well as administering and distributing amounts in respect of) securities, rights, collateral or other assets on behalf of or for the benefit of the holders of the listed securities.

<sup>170</sup> See Amendment Nos. 2 and 3 to the Nasdaq Issuer Applicability Proposal.

<sup>171</sup> See *supra* note 24.

<sup>172</sup> To make the application of the rules easier to understand, Nasdaq also proposed in Amendment

Companies would be required to be in compliance with the new rules by the following dates:

The provisions of Rule 4200(a) and Rule 4350(c), (d) and (m) regarding director independence, independent committees, and notification of noncompliance would be required to be implemented by:

- July 31, 2005 for foreign private issuers<sup>173</sup> and small business issuers (as defined in Rule 12b-2<sup>174</sup>); and
- For all other listed issuers, by the earlier of: (1) The listed issuer's first annual shareholders meeting after January 15, 2004; or (2) October 31, 2004.

In the case of an issuer with a staggered board, with the exception of the audit committee requirements, the issuer would have until its second annual meeting after January 15, 2004, but not later than December 31, 2005, to implement all new requirements relating to board composition, if the issuer would be required to change a director who would not normally stand for election at an earlier annual meeting. Such issuers would be required to comply with the audit committee requirements pursuant to the implementation schedule noted above.

Issuers that have listed or will be listed in conjunction with their initial public offering would be afforded exemptions from all board composition requirements consistent with the exemptions afforded in Rule 10A-3(b)(1)(iv)(A). That is, for each committee that the company adopts, the company would be required to have one independent member at the time of listing, a majority of independent members within 90 days of listing, and all independent members within one year. The rule would note, however, that investment companies are not afforded the exemptions in Rule 10A-3(b)(1)(iv)(A). Issuers could choose not to adopt a compensation or nomination committee and could instead rely upon a majority of the independent directors to discharge responsibilities under the rules. These issuers would be required to meet the majority independent board requirement within one year of listing.

Companies transferring from other markets with a substantially similar requirement would be afforded the

No. 3 to the Nasdaq Issuer Applicability Proposal to adopt Rules 4200A and 4350A, which would set forth the sections of existing Rules 4200 and 4350 that will continue to be applicable until the deadlines for compliance with the proposed changes.

<sup>173</sup> See Section II.C.13., *supra* for a discussion of the treatment of foreign private issuers under the Nasdaq proposals.

<sup>174</sup> 17 CFR 240.12b-2.

<sup>164</sup> See NASD Rule 4350(h).

<sup>165</sup> See Amendment No. 3 to the Nasdaq Related Party Transactions Proposal, *supra* note 19.

<sup>166</sup> See *supra* notes 22 to 24.

<sup>167</sup> *Id.*