

structure. In short, the Exchange proposes to restructure its governance architecture so that it will have a Board of Directors ("Board") that is independent of members, member organizations, and listed issuers, and whose membership includes only one officer of the Exchange. The Exchange also proposes to create a Board of Executives that is representative of securities firms, listed issuers, and institutional investors. In addition, the NYSE proposes that its regulatory unit report directly to a fully independent committee of the Board, and not to NYSE management. The Exchange represents that the proposed rule change would guarantee the independence of its regulatory function both from members and member organizations and from inappropriate linkage with its marketplace function, yet would retain sufficient proximity to the marketplace to assure the market sensitivity that, in the Exchange's view, is fundamental to effective regulation.

A description of the most significant changes to the NYSE Constitution follows.

A. Board of Directors

The NYSE proposes to reduce the size of its Board, which previously had 24 members plus as many as three members of NYSE management, to between 6 and 12 members, plus the Chairman of the Board and the Chief Executive Officer (if different than the Chairman). The Board would be required to meet not less than four times per year, and directors would serve one-year terms.⁷

Board members (excluding the Chief Executive Officer) would be required to be independent of the management of the Exchange, the membership of the Exchange, and issuers of securities listed on the Exchange. Among other things, no director (other than the Chief Executive Officer) could be a member of the NYSE; an officer or employee of the NYSE; a person employed by or affiliated, directly or indirectly, with a member organization of the NYSE or with a broker or dealer that engages in a business involving substantial direct contact with securities customers; or an executive officer of a listed issuer. In addition, no director (excluding the Chief Executive Officer) would qualify as independent unless the Board affirmatively determined that the director had no material relationship with the Exchange. The Board would be required to adopt specific standards relating to such determination,

comparable to standards required of issuers listed on the Exchange.⁸

The selection process for Board members would be designed to enable the Exchange to comply with the "fair representation" requirements of section 6(b)(3) of the Act.⁹ Under the proposed amendments to the Constitution, the Nominating & Governance Committee (which, under the proposal, would be composed solely of independent directors) ultimately would be responsible for recommending to the Board candidates for Board membership. The amendments further would require, however, that the "Industry Members" of the Board of Executives, described below, recommend candidates constituting twenty percent of the number of directors to be elected by members of the Exchange, but in no event fewer than two directors.¹⁰

If a single individual serves as both the Chairman and Chief Executive Officer ("CEO"), the Board would be required to designate a director as a "lead director" to preside over executive sessions of the Board. The CEO would not be permitted to participate in executive sessions. The Board would be required to publicly disclose the lead director's name and the means by which interested parties could communicate with the lead director.¹¹

The Board would be required to compile and distribute an annual nominating report listing the nominees for positions to be elected by the members. The Board would also be required to appoint the members of the Board of Executives.¹²

B. Board of Executives

Pursuant to the proposed Constitutional amendments, the Board would be required to establish a Board

of Executives which, subject to the Board's ultimate authority, review, and oversight (and except with respect to the responsibilities delegated to the Standing Committees, discussed below), would advise the CEO in his or her management of the operations of the Exchange.¹³ The Board of Executives would consist of the Chairman of the Board, who would be the Chairman of the Board of Executives; the CEO (if different than the Chairman); and at least 20 but no more than 25 additional members, who would serve for one-year terms. The Board of Executives would be required to meet not less than six times per year.

The members of the Board of Executives would be required to include at least six individuals who are either the chief executive or a principal executive officer of a member organization that engages in a business with direct contact with securities customers; at least two individuals who are either the chief executive or a principal executive officer of a specialist member organization; and at least two floor representatives other than specialists. The members of the Board of Executives from these categories would be known collectively as the "Industry Members" of the Board of Executives. The Board of Executives also would be required to include at least two lessor members who are not affiliated with a broker or dealer in securities; at least four individuals who are either the chief executive or a principal executive officer of an institution that is a significant investor in equity securities, at least one of whom is a fiduciary of a public pension fund; and at least four individuals who are either the chief executive or principal executive officer of a listed company.¹⁴

If the Board were to increase the size of the Board of Executives, it must strive to maintain approximately the same balance between Industry Members and other members of the Board of Executives as set forth above. If the Board were to increase the size of the Board of Executives, it would also be free to add members to the Board of

⁸ The Board would be required to adopt these standards by effecting a rule change within the meaning of section 19(b)(1) of the Act. The Commission recently approved revisions to the Exchange's corporate governance standards for its listed issuers that, among other things, set forth criteria for determining whether a director is "independent." See Securities Exchange Act Release No. 48745 (November 4, 2003), 68 FR 64154 (November 12, 2003) ("NYSE/Nasdaq Corporate Governance Listing Standards Approval Order").

⁹ 15 U.S.C. 78f(b)(3). Section 6(b)(3) of the Act requires the rules of a national securities exchange to provide for the fair representation of its members in the selection of directors and the administration of its affairs, and provide that one or more directors be representative of issuers and investors and not be associated with a member of the exchange, broker or dealer. See *infra* notes 15–21 and accompanying text for a discussion of fair representation.

¹⁰ See *infra* note 17 and accompanying text.

¹¹ NYSE Constitution, Article IV, Section 2.

¹² NYSE Constitution, Article IV, Section 1.

¹³ NYSE Constitution, Article V, Section 1.

¹⁴ *Id.* The Commission notes that the reconstituted NYSE Board recently voted to further amend the provisions of the NYSE Constitution relating to the composition of the Board of Executives to: (1) Add a representative of individual investors who are retail clients of member organizations; and (2) remove the requirement that specialist representatives be chief executive or principal executive officers of specialist firms, but require that each such representative be registered as a specialist and spend substantial time on the floor of the Exchange. See Additional Amendments Letter, *supra* note 4.

⁷ NYSE Constitution, Article IV, Section 2.