

- ADMIRALTY & MARITIME
- ANTITRUST & TRADE REGULATION
- APPELLATE LITIGATION
- AVIATION
- BANKING
- BANKRUPTCY, RESTRUCTURING & CREDITORS-DEBTORS RIGHTS
- BUSINESS & COMMERCIAL LITIGATION
- CLASS ACTION DEFENSE
- COMMERCIAL LENDING & FINANCE
- CONSTRUCTION
- CORPORATE & SECURITIES
- EMPLOYEE BENEFITS, ERISA, & EXECUTIVE COMPENSATION
- ENERGY
- ENVIRONMENTAL & TOXIC TORTS
- ERISA, LIFE, HEALTH & DISABILITY INSURANCE LITIGATION
- GAMING
- GOVERNMENT RELATIONS
- HEALTH CARE
- INTELLECTUAL PROPERTY
- INTERNATIONAL
- INTERNATIONAL FINANCIAL SERVICES
- LABOR RELATIONS & EMPLOYMENT
- MERGERS & ACQUISITIONS
- PRODUCTS LIABILITY
- PROFESSIONAL LIABILITY
- PROJECT DEVELOPMENT & FINANCE
- PUBLIC FINANCE
- REAL ESTATE: LAND USE, DEVELOPMENT & FINANCE
- TAX (INTERNATIONAL, FEDERAL AND STATE)
- TELECOMMUNICATIONS & UTILITIES
- TRUSTS, ESTATES & PERSONAL PLANNING
- VENTURE CAPITAL & EMERGING COMPANIES
- WHITE COLLAR CRIME

SEC APPROVES AMENDMENTS TO NYSE CORPORATE GOVERNANCE RULES

By Douglas N. Currault II and Izabela M. Chabinska

On November 3, 2004, the Securities and Exchange Commission approved the New York Stock Exchange's proposed amendments and clarifications of certain of its corporate governance standards set forth in Section 303A of the NYSE Listed Company Manual that were initially approved by the SEC on November 4, 2003. ([Click here to link to our November 2003 E*Zine summarizing the SEC's approval of the NYSE corporate governance rules.](#))

We have summarized below the principal clarifying and substantive changes of the amendments.

Definition of Independent Director

The amendments to Section 303A.02 of the NYSE Listed Company Manual primarily relate to the bright-line tests that directors must satisfy to be deemed independent. The amendments also clarify other aspects of Section 303A.02, as noted below.

- Modify the commentary to Sections 303A.02(b)(i) and (ii) to clarify that service as an interim executive officer (and not only as an interim chairman or CEO as previously required) will not trigger the look-back provisions in those sections.
- Reformulate the wording for the bright-line independence test in Section 303A.02(b)(ii) to clarify the look-back period. As revised, a director will not be independent if the director or an immediate family member of the director received more than \$100,000 in direct compensation from the company "during any twelve-month period within the last three years."
- Revise the bright-line test in Section 303A.02(b)(iii) ("Director-Auditor Relationship Test"), which precludes independence where a director or immediate family member of the director is employed by or affiliated with a present or former internal or external auditor of the company. The revised test now provides that a director is not independent if:

- ADMIRALTY & MARITIME
- ANTITRUST & TRADE REGULATION
- APPELLATE LITIGATION
- AVIATION
- BANKING
- BANKRUPTCY, RESTRUCTURING & CREDITORS-CREDITORS RIGHTS
- BUSINESS & COMMERCIAL LITIGATION
- CLASS ACTION DEFENSE
- COMMERCIAL LENDING & FINANCE
- CONSTRUCTION
- CORPORATE & SECURITIES
- EMPLOYEE BENEFITS, ERISA, & EXECUTIVE COMPENSATION
- ENERGY
- ENVIRONMENTAL & TOXIC TORTS
- ERISA, LIFE, HEALTH & DISABILITY INSURANCE LITIGATION
- GAMING
- GOVERNMENT RELATIONS
- HEALTH CARE
- INTELLECTUAL PROPERTY
- INTERNATIONAL FINANCIAL SERVICES
- LABOR RELATIONS & EMPLOYMENT
- MERGERS & ACQUISITIONS
- PRODUCTS LIABILITY
- PROFESSIONAL LIABILITY
- PROJECT DEVELOPMENT & FINANCE
- PUBLIC FINANCE
- REAL ESTATE: LAND USE, DEVELOPMENT & FINANCE
- TAX (INTERNATIONAL, FEDERAL AND STATE)
- TELECOMMUNICATIONS & UTILITIES
- TRUSTS, ESTATES & PERSONAL PLANNING
- VENTURE CAPITAL & EMERGING COMPANIES
- WHITE COLLAR CRIME

- the director or an immediate family member of the director is a current partner of the company's internal or external auditor;
- the director is a current employee of the company's internal or external audit firm;
- the director has an immediate family member who is a current employee of the company's internal or external audit firm and who participates in the firm's audit, assurance or tax compliance (but not tax planning) practice; or
- the director or an immediate family member of the director was a partner or employee of the company's internal or external audit firm and personally worked on the company's audit during the past three years.
- Provide that listed companies have until their first annual shareholders' meeting after June 30, 2005 to replace a director who was independent under the previous Director-Auditor Relationship Test but would not be under the revised test.
- Revise the commentary to Section 303A.02(b)(v) to clarify that payments to a charitable organization that are related to a listed company's business relationship with that organization would be subject to the test regarding the independence of a director who held, or whose immediate family member held, certain positions in the charitable organization that received the payments.
- Clarify that the three-year look-back periods for determining director independence under Section 303A.02(b) apply from and after November 4, 2004.
- Clarify that listed companies are required to identify which of their directors have been deemed independent.
- Define the term "executive officer" as used throughout Section 303A to have the same meaning specified for the term "officer" in Rule 16a-1(f) under the Securities Exchange Act of 1934.

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- ANTITRUST & TRADE REGULATION
- APPELLATE LITIGATION
- AVIATION
- BANKING
- BANKRUPTCY, RESTRUCTURING & CREDITORS-DEBTORS RIGHTS
- BUSINESS & COMMERCIAL LITIGATION
- CLASS ACTION DEFENSE
- COMMERCIAL LENDING & FINANCE
- CONSTRUCTION
- CORPORATE & SECURITIES
- EMPLOYEE BENEFITS, ERISA, & EXECUTIVE COMPENSATION
- ENERGY
- ENVIRONMENTAL & TOXIC TORTS
- ERISA, LIFE, HEALTH & DISABILITY INSURANCE LITIGATION
- GAMING
- GOVERNMENT RELATIONS
- HEALTH CARE
- INTELLECTUAL PROPERTY
- INTERNATIONAL
- INTERNATIONAL FINANCIAL SERVICES
- LABOR RELATIONS & EMPLOYMENT
- MERGERS & ACQUISITIONS
- PRODUCTS LIABILITY
- PROFESSIONAL LIABILITY
- PROJECT DEVELOPMENT & FINANCE
- PUBLIC FINANCE
- REAL ESTATE: LAND USE, DEVELOPMENT & FINANCE
- TAX (INTERNATIONAL, FEDERAL AND STATE)
- TELECOMMUNICATIONS & UTILITIES
- TRUSTS, ESTATES & PERSONAL PLANNING
- VENTURE CAPITAL & EMERGING COMPANIES
- WHITE COLLAR CRIME

Requirements for Non-Management Directors

As revised, the commentary to Section 303A.03 clarifies that a non-management director must preside over each executive session of the non-management directors, but the same director is not required to preside at all such sessions.

Requirements for Compensation Committees

Section 303A.05(b)(i)(B) has been revised to clarify that the compensation committee must make recommendations to the board with respect to non-CEO executive officer compensation. The amendments also make clear that a company's board of directors may delegate its authority to approve non-CEO executive officer compensation to the board's compensation committee.

Duties of the Audit Committee

The amendments to Section 303A.07(c)(iii)(B) clarify that a company's audit committee must review and discuss the company's financial statements and MD&A disclosures.

Disclosures of Guidelines and Codes and Methods of Communication

The amendments also require that a company state in its annual proxy statement or, if the company does not file a proxy statement, its Form 10-K, that its corporate governance guidelines, charters of its "most important committees" (*i.e.*, audit committee and, if applicable, compensation and nominating committees), and code of business conduct and ethics are available on its website and in print to any shareholder requesting them.

Foreign Private Issuer Disclosures

The amendments clarify that foreign private issuers must disclose the significant differences between their actual corporate governance practices (as opposed to their home country practices as previously required) and those required of U.S. companies under Section 303A.

Certifications and Affirmations

The amendments clarify that the annual certification in which the CEO certifies that he or she is not aware of any violation by the company of

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- ANTITRUST & TRADE REGULATION
- APPELLATE LITIGATION
- AVIATION
- BANKING
- BANKRUPTCY, RESTRUCTURING & CREDITORS-DEBTORS RIGHTS
- BUSINESS & COMMERCIAL LITIGATION
- CLASS ACTION DEFENSE
- COMMERCIAL LENDING & FINANCE
- CONSTRUCTION
- CORPORATE & SECURITIES
- EMPLOYEE BENEFITS, ERISA, & EXECUTIVE COMPENSATION
- ENERGY
- ENVIRONMENTAL & TOXIC TORTS
- ERISA, LIFE, HEALTH & DISABILITY INSURANCE LITIGATION
- GAMING
- GOVERNMENT RELATIONS
- HEALTH CARE
- INTELLECTUAL PROPERTY
- INTERNATIONAL
- INTERNATIONAL FINANCIAL SERVICES
- LABOR RELATIONS & EMPLOYMENT
- MERGERS & ACQUISITIONS
- PRODUCTS LIABILITY
- PROFESSIONAL LIABILITY
- PROJECT DEVELOPMENT & FINANCE
- PUBLIC FINANCE
- REAL ESTATE: LAND USE, DEVELOPMENT & FINANCE
- TAX (INTERNATIONAL, FEDERAL AND STATE)
- TELECOMMUNICATIONS & UTILITIES
- TRUSTS, ESTATES & PERSONAL PLANNING
- VENTURE CAPITAL & EMERGING COMPANIES
- WHITE COLLAR CRIME

the NYSE corporate governance listing standards may be qualified, but that any qualifications must be disclosed.

Finally, the amendments add a new Section 303A.12(c) requiring companies to submit annual written affirmations to the NYSE in the form specified by the NYSE, providing the NYSE with details of compliance or non-compliance with Section 303A, as well as interim written affirmations each time a change occurs in the company's board or any of its board committees subject to Section 303A. This requirement will also apply to listed open-end management investment companies, foreign private issuers and companies listing only preferred stock or debt securities on the NYSE.

Effective Date

The amended NYSE corporate governance rules became effective on November 3, 2004.

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ANTITRUST & TRADE REGULATION

APPELLATE LITIGATION

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BANKING

BANKRUPTCY, RESTRUCTURING &
CREDITORS-DEBTORS RIGHTS

BUSINESS & COMMERCIAL LITIGATION

CLASS ACTION DEFENSE

COMMERCIAL LENDING & FINANCE

CONSTRUCTION

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DISABILITY INSURANCE LITIGATION

GAMING

GOVERNMENT RELATIONS

HEALTH CARE

INTELLECTUAL PROPERTY

INTERNATIONAL

INTERNATIONAL FINANCIAL SERVICES

LABOR RELATIONS & EMPLOYMENT

MERGERS & ACQUISITIONS

PRODUCTS LIABILITY

PROFESSIONAL LIABILITY

PROJECT DEVELOPMENT & FINANCE

PUBLIC FINANCE

REAL ESTATE: LAND USE,
DEVELOPMENT & FINANCE

TAX (INTERNATIONAL,
FEDERAL AND STATE)

TELECOMMUNICATIONS & UTILITIES

TRUSTS, ESTATES &
PERSONAL PLANNING

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Please remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues you may contact the head of our Corporate and Securities practice group:

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