

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48836; File No. SR-Phlx-2003-51]

### Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment No. 1 Thereto by the Philadelphia Stock Exchange, Inc. Relating to Listing Standards Regarding Issuer's Audit Committees and Delisting Procedures

November 25, 2003.

#### I. Introduction

On July 14, 2003, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend Phlx Rule 849, Audit Committee/Conflicts of Interest, and Phlx Rule 811, Delisting Policies and Procedures.

The provisions in the proposed rule change mostly are intended to comply with the requirements mandated by Section 10A(m) of the Act<sup>3</sup> and Rule 10A-3 thereunder.<sup>4</sup> Additional changes in the proposal relate to audit committee charters, audit committee composition requirements, audit committee approval of related party transactions, and revisions to the Exchange's delisting rule. The Exchange also committed to adopt additional listing policies and requirements pertaining to issuer corporate governance.

The proposed rule change was published for comment in the **Federal Register** on October 16, 2003.<sup>5</sup> The Commission received no comments on the proposal. On November 20, 2003, the Phlx submitted an amendment to the proposed rule change.<sup>6</sup> This order approves the proposed rule change, publishes notice of Amendment No. 1,

and approves Amendment No. 1 on an accelerated basis.<sup>7</sup>

#### II. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>8</sup> Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>9</sup> which requires, among other things, that the Phlx's rules be designed to prevent fraudulent and manipulative acts and practices, and, in general, to protect investors and the public interest. Moreover, the Commission believes that the Exchange's proposal to add the new requirements concerning audit committees is appropriate and consonant with Section 10A(m) of the Act and Rule 10A-3 thereunder relating to audit committee standards for listed issuers. The Commission notes that the Phlx intends to file an additional rule proposal relating to other corporate governance listing standards.<sup>10</sup>

Furthermore, the Commission finds good cause, consistent with Section 19(b)(2) of the Act,<sup>11</sup> to approve Amendment No. 1 to the proposed rule change prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. In Amendment No. 1, the Phlx expanded, with respect to investment companies, the scope of the proposed provision regarding complaint procedures. Rule 10A-3 requires audit committees to establish procedures for "the confidential, anonymous submission by employees of the listed issuer of concerns regarding questionable accounting or auditing matters."<sup>12</sup> The amended Phlx proposal would require that audit committees of investment companies also establish procedures for the confidential, anonymous submission of such concerns by employees of the investment adviser, administrator, principal underwriter, or any other provider of accounting related services for the investment company, as well as employees of the investment company.

<sup>7</sup> Rule 10A-3 requires each national securities exchange and national securities association to have rules that comply with its requirements approved by the Commission no later than December 1, 2003. By the Commission approving the proposed rule change, the Exchange can comply with this deadline.

<sup>8</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>9</sup> 15 U.S.C. 78f(b)(5).

<sup>10</sup> See Notice at note .

<sup>11</sup> 15 U.S.C. 78s(b)(2).

<sup>12</sup> 17 CFR 240.10A-3(b)(3)(ii).

This revision responds to a recommendation by the Commission that self-regulatory organizations take into account, in adopting rules to comply with Rule 10A-3, the fact that most services are rendered to an investment company by employees of third parties, such as the investment adviser, rather than by employees of the investment company.<sup>13</sup> The Commission believes that it is appropriate to accelerate approval of this amendment, because it conforms the rule text to similar rules of the New York Stock Exchange, Inc. and the National Association of Securities Dealers, Inc. that were approved by the Commission,<sup>14</sup> and the amendment raises no new substantive issues.

#### III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether Amendment No. 1 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 in the Commission's Public Reference Room. Copies of such filings will also be available for inspection and copying at the principal office of the Phlx. All submissions should refer to File No. SR-Phlx-2003-51 and should be submitted by December 24, 2003.

#### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act<sup>15</sup>, that Amendment No. 1 is approved on an accelerated basis, and that the proposed rule change (File No. SR-Phlx-2003-51) be, and it hereby is, approved.

<sup>13</sup> See Securities Act Release No. 8220, Securities Exchange Act Release No. 47654, and Investment Company Act Release No. 26001 (April 9, 2003), 68 FR 18788 (April 16, 2003) (release adopting Rule 10A-3).

<sup>14</sup> See Securities Exchange Act Release Nos. 48745 (November 4, 2003), 68 FR 64154 (November 12, 2003) (approval of, among other proposals, File Nos. SR-NYSE-2002-33 and SR-NASD-2002-141).

<sup>15</sup> 15 U.S.C. 78s(b)(2).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78j-1(m).

<sup>4</sup> 17 CFR 240.10A-3.

<sup>5</sup> See Securities Exchange Act Release No. 48601 (October 8, 2003), 68 FR 59666 ("Notice").

<sup>6</sup> See letter from Carla Behnfeldt, Director, Legal Department New Product Development Group, Phlx, to Ira L. Brandriss, Special Counsel, Division of Market Regulation, Commission, dated November 19, 2003 ("Amendment No. 1"). In Amendment No. 1, with respect to investment companies, the Phlx expanded the scope of the requirement that audit committees establish procedures for the confidential, anonymous submission of concerns regarding questionable accounting or auditing matters.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>16</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48847; File No. SR-Phlx-2003-73]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1 and 2 Thereto by the Philadelphia Stock Exchange, Inc. Relating to the Demutualization of the Philadelphia Stock Exchange, Inc.

November 26, 2003.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on November 17, 2003, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. On November 24, 2003, the Phlx submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> On November 26, 2003, the Phlx submitted Amendment No. 2 to the proposed rule change.<sup>4</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Phlx, pursuant to Section 19(b)(1) and Rule 19b-4 thereunder,<sup>5</sup> proposes

to: (i) First amend Article FOURTH of its Certificate of Incorporation to eliminate the terms providing that it is "not for profit" and that "no dividend shall ever be paid by the Corporation" ("Plan of Conversion" and such amendment to the Certificate of Incorporation, the "Conversion Amendment"); and (ii) subsequently merge a newly created, wholly-owned shell subsidiary of the Phlx with and into the Phlx, with the Phlx surviving as a "demutualized"<sup>6</sup> Delaware stock corporation (the "Merger," and together with the Plan of Conversion, the "Plan of Demutualization") pursuant to an Agreement and Plan of Merger ("Merger Agreement").<sup>7</sup> In connection with the Plan of Demutualization, the Phlx will amend its Certificate of Incorporation ("Certificate of Incorporation"), By-laws ("By-laws") and Rules of the Board of Governors, Option Rules, ITS Rules and Options Floor Procedure Advices (collectively, the "Rules").<sup>8</sup> The Phlx will, upon completion of the Demutualization, issue pursuant to the Merger Agreement 100 shares of its Class A Common Stock to each equitable titleholder of an Exchange membership. As discussed more fully below, the Phlx will also issue one share of Series A-1 Preferred Stock, par value \$0.01 ("Series A Preferred Stock") to the "Phlx Member Voting Trust" (the "Trust") in accordance with an Amended and Restated Trust Agreement ("Trust Agreement").

The proposed changes to the Certificate of Incorporation, the By-laws and the Rules, as well as the Trust Agreement and the Conversion Amendment are collectively referred to herein as the "Proposed Rule Change." The text of the amendments to the Certificate of Incorporation, By-laws and Rules is available at the Office of the Secretary, the Phlx, and at the Commission.

#### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Phlx included statements concerning the purpose of and basis for the proposed rule change and discussed any

comments it received on the proposed rule change. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements. The text of the proposed rule change is available at the Office of the Secretary, the Phlx, at the Commission, and on the Commission's website.

##### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

###### 1. Purpose

The purpose of the Proposed Rule Change is to implement the Plan of Demutualization of the Phlx. In connection with such Plan of Demutualization, trading privileges will be separated from corporate ownership of the Phlx and will be made available exclusively through trading permits, as described in greater detail below.<sup>9</sup>

As a result of the Demutualization, the total of 50,500 shares of Class A Common Stock (100 shares per Seat) issued to existing equitable Seat holders will represent 100% of the common equity ownership in the Phlx outstanding immediately after the Demutualization, and all Members and holders of equity trading permits<sup>10</sup> who are affiliated with Member Organizations and are not suspended will be entitled to receive new Series A-1 Permits (described further below) to enable them to continue their activities on the Exchange without interruption. Similarly, Member Organizations will maintain their status upon their compliance with certain deposit and registration requirements, as described in greater detail below.

After the effective date of the Demutualization, the Exchange will continue to be a national securities exchange registered under Section 6 of the Act.<sup>11</sup> Except as will be necessary to implement the new permit structure to replace the existing structure of owning and leasing Seats as a basis for trading rights and Exchange memberships, the

<sup>9</sup>The Exchange, however, does plan to retain its existing Foreign Currency Option ("FCO") participations (as defined in Section 1-1(m) of the current By-laws). After the Demutualization, the ability to trade FCOs on the Phlx will also be available through a Series A-1 Permit, as set forth in proposed Rule 908(b).

<sup>10</sup>Pursuant to Rule 23 of the existing Phlx Rules, the Exchange has issued equity trading permits ("ETPs"), four of which are currently outstanding. As described in greater detail below, in the Demutualization, these ETPs will be eliminated in accordance with existing Rule 23 and pursuant to proposed Rule 971, and the rights and privileges of ETPs will be conferred on existing ETP holders by Permits, as described below.

<sup>11</sup>15 U.S.C. 78f.

<sup>16</sup>17 CFR 200.30-3(a)(12).

<sup>1</sup>15 U.S.C. 78s(b)(1).

<sup>2</sup>17 CFR 240.19b-4.

<sup>3</sup>See Letter from Edith Halihan, Deputy General Counsel, Phlx to Nancy Sanow, Assistant Director, Commission, Division of Market Regulation ("Division") dated November 21, 2003. ("Amendment No. 1"). In Amendment No. 1, the Phlx made technical conforming changes to the exhibits of the proposed rule change.

<sup>4</sup>See Letter from Edith Halihan, Deputy General Counsel, Phlx to Nancy Sanow, Assistant Director, Commission, Division dated November 26, 2003. ("Amendment No. 2"). In Amendment No. 2, the Phlx amended the proposed rule change to reflect that on November 25, 2003, the members of the Phlx (as that term is defined in Section I-1(b) of the current By-laws of the Phlx, the "Members") approved the Plan of Conversion, the Merger, and all transactions to be effected in connection therewith. Also, on November 18, 2003, holders of equitable title ("Owners") to memberships in the Phlx (each such membership a "Seat") voted to approve the Plan of Demutualization as a whole.

<sup>5</sup>17 CFR 240.19b-4

<sup>6</sup>This process is also referred to in this notice as the "Demutualization."

<sup>7</sup>Under the existing Certificate of Incorporation and By-laws and applicable law, the approval of the Owners is not required to effect the Plan of Demutualization.

<sup>8</sup>In certain limited cases, the proposed rule change also reflects the deletion of obsolete provisions and other necessary updates in the By-laws and the Phlx Rules that are not directly related to the Plan of Demutualization and are summarized in greater detail below.