

By the Commission.

**Elizabeth M. Murphy,**  
Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-68641; File No. SR-BX-  
2012-063]

### Self-Regulatory Organizations; NASDAQ OMX BX, Inc.; Notice of Filing of Amendment No. 1, and Order Granting Accelerated Approval of Proposed Rule Change, as Modified by Amendment No. 1, To Amend the Listing Rules for Compensation Committees To Comply With Rule 10C-1 Under the Act and Make Other Related Changes

January 11, 2013.

#### I. Introduction

On September 25, 2012, NASDAQ OMX BX, Inc. (“BX” 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 modify the Exchange’s rules for compensation committees of listed issuers to comply with Rule 10C-1 under the Act and make other related changes. The proposed rule change was published for comment in the **Federal Register** on October 15, 2012.<sup>3</sup> The Commission subsequently extended the time period in which to either approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change, to January 13, 2013.<sup>4</sup> The Commission received no comment letters on the proposed rule change.<sup>5</sup> On January 8,

2013, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>6</sup> This order approves the proposed rule change, as modified by Amendment No. 1 thereto, on an accelerated basis.

#### II. Description of Proposed Rule Change

##### A. Background: Rule 10C-1 Under the Act

On March 30, 2011, to implement Section 10C of the Act, as added by Section 952 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”),<sup>7</sup> the Commission proposed Rule 10C-1 under the Act,<sup>8</sup> which directs each national securities exchange (hereinafter, “exchange”) to prohibit the listing of any equity security of any issuer, with certain exceptions, that does not comply with the rule’s requirements regarding compensation committees of listed issuers and related requirements regarding compensation

advisers. On June 20, 2012, the Commission adopted Rule 10C-1.<sup>9</sup>

Rule 10C-1 requires, among other things, each exchange to adopt rules providing that each member of the compensation committee<sup>10</sup> of a listed issuer must be a member of the board of directors of the issuer, and must otherwise be independent.<sup>11</sup> In determining the independence standards for members of compensation committees of listed issuers, Rule 10C-1 requires the exchanges to consider relevant factors, including, but not limited to: (a) The source of compensation of the director, including any consulting, advisory or other compensatory fee paid by the issuer to the director (hereinafter, the “Fees Factor”); and (b) whether the director is affiliated with the issuer, a subsidiary of the issuer or an affiliate of a subsidiary of the issuer (hereinafter, the “Affiliation Factor”).<sup>12</sup>

In addition, Rule 10C-1 requires the listing rules of exchanges to mandate that compensation committees be given the authority to retain or obtain the advice of a compensation adviser, and have direct responsibility for the appointment, compensation and oversight of the work of any compensation adviser they retain.<sup>13</sup> The exchange rules must also provide that each listed issuer provide for appropriate funding for the payment of reasonable compensation, as determined by the compensation committee, to any compensation adviser retained by the compensation committee.<sup>14</sup> Finally, among other things, Rule 10C-1 requires each exchange to provide in its rules that the compensation committee of each listed issuer may select a compensation consultant, legal counsel or other adviser to the compensation committee only after taking into consideration six factors specified in Rule 10C-1,<sup>15</sup> as well as any other

No. 68639 (January 11, 2013) (File No. SR-NYSE-2012-49) (“NYSE Approval Order”).

<sup>6</sup> In Amendment No. 1, BX: (a) Added language to proposed Rule 5605(d)(3) to set forth in detail the requirements of Rule 10C-1(b)(2)-(4) regarding the authority of a compensation committee to retain compensation advisers, the requirement that a listed company fund such advisers, and the independence assessment required to be made before selecting or receiving advice from such advisers, rather than incorporating these details by reference as in the original proposal, *see infra* notes 51-58 and accompanying text; (b) revised the dates by which companies currently listed on BX will be required to comply with the new rules, *see infra* notes 76-82 and accompanying text; (c) revised the phase-in schedule for companies that cease to be Smaller Reporting Companies to comply with the full range of the new requirements, *see infra* notes 89-92 and accompanying text; (d) added a preamble to the new rules clarifying that, during the transition periods until the new rules apply, a company must continue to comply with the corresponding provisions, if any, in the current rules, *see infra* note 76; and (e) revised the proposed rules to state that the independence assessment of compensation advisers required of compensation committees does not need to be conducted for advisers whose roles are limited to those entitled to an exception from the adviser disclosure rules under Item 407(e)(3)(iii) of Regulation S-K. *See infra* notes 59-60 and accompanying text.

In Amendment No. 1 the Exchange also made conforming changes to the Purpose section of the proposal, provided explanations for the revisions, and clarified certain matters, *see, e.g., infra* notes 58, 114, and 119 and accompanying text; and also added, as Exhibit 3 to the proposal, the form that it will provide for companies to certify their compliance with the rules. The Exchange states that, while no comments were submitted regarding its proposed rule change, some of the changes contained in Amendment No. 1 were made in response to comments submitted on Nasdaq’s substantially similar proposal. *See supra* note 5 and *infra* note 123.

<sup>7</sup> Public Law 111-203, 124 Stat. 1900 (2010).

<sup>8</sup> *See* Securities Act Release No. 9199, Securities Exchange Act Release No. 64149 (March 30, 2011), 76 FR 18966 (April 6, 2011) (“Rule 10C-1 Proposing Release”).

<sup>9</sup> *See* Securities Act Release No. 9330, Securities Exchange Act Release No. 67220 (June 20, 2012), 77 FR 38422 (June 27, 2012) (“Rule 10C-1 Adopting Release”).

<sup>10</sup> For a definition of the term “compensation committee” for purposes of Rule 10C-1, *see* Rule 10C-1(c)(2)(i)-(iii).

<sup>11</sup> *See* Rule 10C-1(a) and (b)(1).

<sup>12</sup> *See id.* *See also* Rule 10C-1(b)(1)(iii)(A), which sets forth exemptions from the independence requirements for certain categories of issuers. In addition, an exchange may exempt a particular relationship with respect to members of a compensation committee from these requirements as it deems appropriate, taking into consideration the size of an issuer and any other relevant factors. *See* Rule 10C-1(b)(1)(iii)(B).

<sup>13</sup> *See* Rule 10C-1(b)(2).

<sup>14</sup> *See* Rule 10C-1(b)(3).

<sup>15</sup> *See* Rule 10C-1(b)(4). The six factors, which BX proposes to set forth explicitly in its rules, are specified in the text accompanying note 55, *infra*.

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

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

<sup>3</sup> *See* Securities Exchange Act Release No. 68018 (October 9, 2012), 77 FR 62547 (“Notice”).

<sup>4</sup> *See* Securities Exchange Act Release No. 68313 (November 28, 2012), 77 FR 71853 (December 4, 2012).

<sup>5</sup> The Commission received eight comments on a substantially similar proposal by The Nasdaq Stock Market, LLC (“Nasdaq”) by parties that did not specifically comment on the BX filing, and received a response letter from Nasdaq on these comment letters. *See* Securities Exchange Act Release No. 68013 (October 9, 2012), 77 FR 62563 (October 15, 2012) (Notice of File No. SR-NASDAQ-2012-109) (“Nasdaq Proposal”) and comment letters relating to the Nasdaq Proposal. *See also* Securities Exchange Act Release No. 68640 (January 11, 2013) (“Nasdaq Approval Order”). The Nasdaq Approval Order contains a discussion of the comments received on the Nasdaq Proposal and Nasdaq’s response. *See also* Securities Exchange Act Release

factors identified by the relevant exchange in its listing standards.<sup>16</sup>

### *B. BX's Proposed Rule Change, as Amended*

To comply with Rule 10C-1, BX proposes to amend two sections of its rules<sup>17</sup> concerning corporate governance requirements for companies listed on the Exchange: BX Venture Market Rule 5605, "Boards of Directors and Committees," and Rule 5615, "Exemptions from Certain Corporate Governance Requirements." In addition, BX proposes to make some other changes to its rules regarding compensation committees.<sup>18</sup>

To accomplish these changes, the Exchange proposes to replace current paragraph (d) of Rule 5605, entitled "Independent Director Oversight of Executive Officer Compensation," with a new paragraph (d) entitled "Compensation Committee Requirements." Current paragraph (d) provides that compensation of the executive officers of a listed company must be determined, or recommended to the company's board for determination, either by a compensation committee comprised solely of "Independent Directors"<sup>19</sup>; or, as an alternative to a formal committee, by a majority of the board's Independent Directors in a vote in which only Independent Directors participate ("Alternative Option").<sup>20</sup>

#### 1. Compensation Committee Composition and Independence Standards

First, BX proposes that each listed company be required to have a

compensation committee.<sup>21</sup> The Alternative Option described above would be eliminated. In addition, BX proposes that the compensation committee be required to be composed of at least two members, each of whom must be an Independent Director as defined in BX's rules and also meet the additional independence requirements described below.<sup>22</sup>

In discussing the proposed elimination of the Alternative Option, BX stated that it had considered whether the Alternative Option remains appropriate, "given the heightened importance of compensation decisions in today's corporate governance environment." The Exchange concluded that "there are benefits from a board having a standing committee dedicated solely to oversight of executive compensation."<sup>23</sup> BX added that, since it does not currently have any listed companies, it does not believe that eliminating the Alternative would be unduly burdensome. In discussing the proposed requirement that the committee have at least two members, the Exchange stated that "[g]iven the importance of compensation decisions to stockholders, BX believes that it is appropriate to have more than one director responsible for these decisions."<sup>24</sup>

BX also proposes that a compensation committee must have a formal written charter.<sup>25</sup> Under this provision, a listed company must certify that it has adopted such a charter and that its compensation committee will review and reassess the adequacy of that charter on an annual basis.<sup>26</sup>

The charter must specify the scope of the committee's responsibilities and

how it carries out those responsibilities, including structure, processes, and membership requirements.<sup>27</sup> It must specify the committee's responsibility for determining or recommending to the board for determination, the compensation of the CEO and all other executive officers of the company, and provide that the CEO may not be present during voting or deliberations on his or her compensation.<sup>28</sup> In addition, the charter must specify the committee's responsibilities and authority set forth in the Exchange's rules with respect to retaining its own advisers; appointing, compensating, and overseeing such advisers; considering certain independence factors before selecting advisers; and receiving funding from the company to engage them, which are discussed in detail below.<sup>29</sup>

BX's rules currently require each member of a listed company's compensation committee to be an Independent Director as defined in BX Rule 5605(a)(2).<sup>30</sup> Rule 10C-1, as discussed above, provides that exchange standards must require compensation committee members to be independent, and further provides that each exchange, in determining independence for this purpose, must consider relevant factors, including the Fees Factor and Affiliation Factor described above. In its proposal, BX discussed its consideration of these factors,<sup>31</sup> and proposed the following<sup>32</sup>:

With respect to the Fees Factor, BX proposes to adopt a provision stating that each member of a compensation committee of a listed company must not accept directly or indirectly any consulting, advisory or other compensatory fee from the listed

<sup>16</sup> Other provisions in Rule 10C-1 relate to exemptions from the rule and a requirement that each exchange provide for appropriate procedures for a listed issuer to have a reasonable opportunity to cure any defects that would be the basis for the exchange, under Rule 10C-1, to prohibit the issuer's listing.

<sup>17</sup> References in this filing to BX Rules refer to the listing rules for the Exchange's BX Venture Market.

<sup>18</sup> While BX does not presently list any securities, its rules for the BX Venture Market have been approved by the Commission. BX is proposing to modify its compensation-related listing rules for this market, as required by Rule 10C-1.

<sup>19</sup> "Independent Directors," as defined in BX Rule 5605(a)(2) and used herein, includes a two-part test for independence. The rule sets forth seven specific categories of directors who cannot be considered independent because of certain discrete relationships ("the bright-line tests"); and also provides that a listed company's board must make an affirmative determination that each independent director has no relationship that, in the opinion of the board, "would interfere with the exercise of independent judgment in carrying out the responsibilities of a director." *Id.* See also the Interpretive Material to Rule 5605.

<sup>20</sup> The current rule also provides that the chief executive officer ("CEO") may not be present during voting or deliberations regarding the CEO's own compensation. See Rule 5605(d)(1).

<sup>21</sup> See proposed Rule 5605(d)(2).

<sup>22</sup> *Id.* For the definition of "Independent Director," see *supra* note 19.

<sup>23</sup> See Notice, *supra* note 3, for the Exchange's more complete explanation of its reasons for the proposed change, including a discussion of whether eliminating the Alternative Option would pose an undue hardship on companies to be listed on the Exchange.

<sup>24</sup> See *id.* for the Exchange's more complete discussion of the proposed size requirement.

<sup>25</sup> See proposed BX Rule 5605(d)(1). As discussed further in Section II.B.3., a Smaller Reporting Company may adopt either a formal written compensation committee charter or a board resolution that specifies the committee's responsibilities and authority.

<sup>26</sup> The Commission notes that Rule 10C-1 does not require a listed issuer specifically to have a charter. As noted above, however, see *supra* notes 13-15 and accompanying text, Rule 10C-1 does require a compensation committee to have certain specified authority and responsibilities. Often, listed issuers will specify authority and responsibilities of this kind in a charter in any case. The proposed rule requires them to have a charter, and to include this authority and set of responsibilities in addition to the required content discussed *infra* at text accompanying notes 27-29.

<sup>27</sup> Proposed Rule 5605(d)(1)(A). BX states that this requirement is copied from the Exchange's similar listing rule relating to audit committee charters, Rule 5605(c)(1), except that the annual review and reassessment requirement is written prospectively, rather than retrospectively. The proposed rule change includes a conforming revision to make the audit committee review and reassessment prospective, as well. See Notice.

<sup>28</sup> Proposed Rule 5605(d)(1)(B)-(C). BX states that these provisions are based upon BX's current compensation-related listing rules, except that the Alternative Option discussed above is not available under the proposed rule change. See *supra* note 21 and accompanying text.

<sup>29</sup> See proposed Rule 5605(d)(1)(D) and *infra* notes 49-58 and accompanying text. Because Smaller Reporting Companies are not required to comply with the provisions relating to compensation advisers in proposed BX Rule 5605(d)(3), see *infra* notes 62-67, their charters or board resolutions are not required to reflect these responsibilities.

<sup>30</sup> See *supra* note 19.

<sup>31</sup> Notice, *supra* note 3.

<sup>32</sup> These additional factors would not apply to the selection of members of the compensation committee of a Smaller Reporting Company. See *infra* note 64.

company or any of its subsidiaries.<sup>33</sup> In discussing its review of its current listing rules and the Fees Factor, BX noted that its rules for audit committees of listed companies, in meeting the criteria of Rule 10A-3 under the Act, prohibit an audit committee member from accepting such fees. The Exchange concluded that “there is no compelling justification to have different standards for audit and compensation committee members” with respect to the Fees Factor.<sup>34</sup>

As currently permitted under BX’s rules for audit committee members, however, the proposed rule would permit a compensation committee member to receive fees for his or her membership on the committee, on the company’s board, or on any other board committee.<sup>35</sup> In addition, a compensation committee member would be permitted to receive fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the company, provided that such compensation is not contingent in any way on continued service.<sup>36</sup>

With respect to the Affiliation Factor, BX proposes that, in determining whether a director is eligible to serve on the compensation committee, the company’s board also must consider whether the director is affiliated with the company, a subsidiary of the company, or an affiliate of a subsidiary of the company to determine whether such affiliation would impair the director’s judgment as a member of the compensation committee.<sup>37</sup> In discussing its review of its current rules and its consideration of the Rule 10C-1 requirement in this area,<sup>38</sup> the Exchange noted that its rules for audit committees of listed companies, in meeting the criteria of Rule 10A-3 under the Act, prohibit an audit committee member from being an affiliated person of the issuer or any subsidiary thereof. The Exchange said that it concluded, however, that “such a blanket prohibition would be inappropriate for compensation committees.”<sup>39</sup> BX believes that “it may be appropriate for certain affiliates, such as representatives of significant stockholders, to serve on compensation committees since their interests are likely aligned with those of other

stockholders in seeking an appropriate executive compensation program.”<sup>40</sup>

Although Rule 10C-1 requires that exchanges consider “relevant factors” not limited to the Fees and Affiliation Factors, BX states that, after reviewing its current and proposed listing rules, it concluded that these rules are sufficient to ensure the independence of compensation committee members. The Exchange therefore determined not to propose further independence requirements.<sup>41</sup>

BX proposes a cure period for a failure of a listed company to meet its committee composition requirements. The proposed cure period is the same as the cure period currently provided in BX’s rules for noncompliance with the requirement to have a majority independent board.<sup>42</sup> Under the provision, if a listed company fails to comply with the compensation committee composition requirements due to one vacancy, or if one compensation committee member ceases to be independent due to circumstances beyond the member’s reasonable control, the company must regain compliance by the earlier of the next annual shareholders meeting or one year from the occurrence of the event that caused the noncompliance.<sup>43</sup> The proposed rule also requires a company relying on this provision to provide notice to BX immediately upon learning of the event or circumstance that caused the noncompliance.

However, if the annual shareholders meeting occurs no later than 180 days following the event that caused the noncompliance, the company instead has 180 days from the event to regain compliance. As explained by BX, this provides a company at least 180 days to cure noncompliance and would typically allow a company to regain compliance in connection with its next annual meeting.<sup>44</sup>

BX’s current rules relating to compensation committees include an exception that allows a director who is not an Independent Director to be appointed to such a committee under exceptional and limited circumstances, as long as that director is not a current officer, an employee, or the family member of an officer or employee.<sup>45</sup> The exception applies, however, only if the committee is comprised of at least three members and the company’s board

determines that the individual’s membership on the committee is required by the best interests of the company and its shareholders.<sup>46</sup> A compensation committee member may not serve longer than two years under this exception, and a company relying on the exception must make certain disclosures on its Web site or in its proxy statement regarding the nature of the relationship and the reasons for the determination.

BX proposes to retain the exception under the proposed rule change, and to permit a listed company to avail itself of the allowance even for a director who fails the new requirements regarding the Fees and Affiliation Factors,<sup>47</sup> with an additional change pertaining to the exception, generally. Nasdaq recently amended an identical provision for exceptional and limited circumstances in its rules to allow a company to rely on the exception for a non-Independent Director who is a family member of a non-executive employee of the company, and BX proposes to make the same revision.<sup>48</sup>

The Exchange believes that this exception is an important means to allow companies flexibility as to board and committee membership and composition in unusual circumstances. The Exchange further believes that the exception may be particularly important for smaller companies.

## 2. Authority of Committees to Retain Compensation Advisers; Funding; and Independence of Compensation Advisers

In its proposed rule change, as modified by Amendment No. 1,<sup>49</sup> BX proposes to fulfill the requirements imposed by Rule 10C-1(b)(2)-(4) under the Act by setting forth those requirements in full in its own rules.<sup>50</sup>

<sup>46</sup> See *id.*

<sup>47</sup> See proposed Rule 5605(d)(2)(b).

<sup>48</sup> See Securities Exchange Act Release No. 67468 (July 19, 2012), 77 FR 43618 (July 25, 2012) (File No. SR-NASDAQ-2012-062). Nasdaq made the same change to its exceptional and limited circumstances exception for audit committee members, and BX also proposes, in its filing, to make a conforming change to its identical exception for audit committee members. BX notes that under both the current and proposed versions of the exception for audit committee members, a company could not rely on the exception for a director who does not meet the criteria set forth in Section 10A(m)(3) of the Exchange Act and the rules thereunder to allow a director to serve on the audit committee. See 15 U.S.C. 78j-1(m)(3) and 17 CFR 240.10A-3(b)(1).

<sup>49</sup> See *supra* note 6. BX’s proposal as submitted originally incorporated the requirements of Rule 10C-1(b)(2)-(4) by reference. The Exchange amended the proposal to set forth those requirements explicitly.

<sup>50</sup> Rule 10C-1(b)(4) does not include the word “independent” before “legal counsel” and requires

<sup>33</sup> See proposed Rule 5605(d)(2)(A).

<sup>34</sup> See Notice.

<sup>35</sup> See *supra* note 33.

<sup>36</sup> *Id.*

<sup>37</sup> See proposed Rule 5605(d)(2)(A).

<sup>38</sup> See Notice.

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> *Id.*

<sup>42</sup> See Rule 5605(b)(1)(A) regarding the majority board requirement.

<sup>43</sup> See proposed Rule 5605(d)(4).

<sup>44</sup> See Notice.

<sup>45</sup> See current Rule 5605(d)(3).

Thus, proposed BX Rule 5605(d)(3), as amended, provides that the compensation committee of a listed company may, in its sole discretion, retain or obtain the advice of a compensation consultant, legal counsel or other adviser.<sup>51</sup> Further, the compensation committee shall be directly responsible for the appointment, compensation and oversight of the work of any compensation consultant, legal counsel and other adviser retained by the compensation committee.<sup>52</sup> In addition, the listed company must provide for appropriate funding, as determined by the compensation committee, for payment of reasonable compensation to a compensation consultant, legal counsel or any other adviser retained by the compensation committee.<sup>53</sup>

Proposed BX Rule 5605(d)(3), as amended, also sets forth explicitly, in accordance with Rule 10C–1, that the compensation committee may select, or receive advice from, a compensation consultant, legal counsel or other adviser to the compensation committee, other than in-house legal counsel, only after taking into consideration the six factors set forth in Rule 10C–1 regarding independence assessments of compensation advisers.<sup>54</sup>

The six factors, which are set forth in full in the proposed rule, are: (i) The provision of other services to the issuer by the person that employs the compensation consultant, legal counsel or other adviser; (ii) the amount of fees received from the issuer by the person that employs the compensation consultant, legal counsel or other adviser, as a percentage of the total revenue of the person that employs the compensation consultant, legal counsel or other adviser; (iii) the policies and procedures of the person that employs the compensation consultant, legal counsel or other adviser that are designed to prevent conflicts of interest;

an independence assessment for any legal counsel to a compensation committee, other than in-house counsel. In setting forth the requirements of Rule 10C–1(b)(2) and (3), BX has deleted the word “independent” prior to “legal counsel” so as to avoid confusion.

<sup>51</sup> See Item 9 of Amendment No. 1.

<sup>52</sup> See *id.* The proposal, as amended, also includes a provision, derived from Rule 10C–1, stating that nothing in these rules may be construed: (i) To require the compensation committee to implement or act consistently with the advice or recommendations of the compensation consultant, legal counsel or other adviser to the compensation committee; or (ii) to affect the ability or obligation of a compensation committee to exercise its own judgment in fulfillment of the duties of the compensation committee. *Id.*

<sup>53</sup> See *id.*

<sup>54</sup> See Rule 10C–1(b)(4).

(iv) any business or personal relationship of the compensation consultant, legal counsel or other adviser with a member of the compensation committee; (v) any stock of the issuer owned by the compensation consultant, legal counsel or other adviser; and (vi) any business or personal relationship of the compensation consultant, legal counsel, other adviser or the person employing the adviser with an executive officer of the issuer.<sup>55</sup>

Proposed Rule 5605(d)(3), as amended, also clarifies that nothing in the rule requires a compensation consultant, legal counsel or other compensation adviser to be independent, only that the compensation committee consider the enumerated independence factors before selecting, or receiving advice from, a compensation adviser.<sup>56</sup> It further clarifies that compensation committees may select, or receive advice from, any compensation adviser they prefer, including ones that are not independent, after considering the six independence factors set forth in the rule.<sup>57</sup> In Amendment No. 1, BX emphasizes that a compensation committee is not required to retain an independent compensation adviser; rather, a compensation committee is required only to conduct the independence analysis described in Rule 10C–1 before selecting a compensation adviser.<sup>58</sup>

In Amendment No. 1, BX also added language to the provision regarding the independence assessment of compensation advisers<sup>59</sup> to state that the compensation committee is not required to conduct an independence assessment for a compensation adviser that acts in a role limited to the following activities for which no disclosure is required under Item 407(e)(3)(iii) of Regulation S–K: (a) Consulting on any broad-based plan that does not discriminate in scope, terms, or operation, in favor of executive officers or directors of the company, and that is available generally to all salaried employees; and/or (b) providing information that either is not customized for a particular issuer or that is customized based on parameters that are not developed by the adviser, and about which the adviser does not provide advice.

<sup>55</sup> Rule 10C–1(b)(4)(i)–(vi).

<sup>56</sup> See *id.*

<sup>57</sup> See *id.*

<sup>58</sup> See Item 2 of Amendment No. 1.

<sup>59</sup> See proposed Rule 5605(d)(3), as amended by Amendment No. 1.

BX states that this exception copies language from Item 407(e)(3)(iii) of Regulation S–K, which provides a limited exception to the Commission’s requirement for a registrant to disclose any role of compensation consultants in determining or recommending the amount and form of a registrant’s executive and director compensation.<sup>60</sup> The Exchange believes that its proposed exception from the independence assessment requirement is appropriate because the types of services excepted do not raise conflict of interest concerns, and noted that this is the same reason for which the Commission excluded these types of services from the disclosure requirement in Item 407(e)(3)(iii) of Regulation S–K.<sup>61</sup>

### 3. Application to Smaller Reporting Companies

Rule 10C–1 includes an exemption for smaller reporting companies from all the requirements included within the rule.<sup>62</sup> Consistent with this Rule 10C–1 provision, BX, as a general matter, proposes that a smaller reporting company, as defined in Rule 12b–2 under the Act (hereinafter, a “Smaller Reporting Company”), not be subject to the new requirements set forth in its proposal specifically to comply with Rule 10C–1.<sup>63</sup> Thus, BX proposes not to require Smaller Reporting Companies to comply with the enhanced independence standards for members of compensation committees relating to compensatory fees and affiliation.<sup>64</sup>

In addition, a Smaller Reporting Company will not be required to include in its compensation committee charter (or, as discussed below, in a board resolution) a grant of authority to the committee to retain compensation advisers, a requirement that the company fund such advisers, and a requirement that the committee consider independence factors before selecting such advisers. As stated by BX, the exception for Smaller Reporting Companies also means that the compensation committees of such companies are not required to review and reassess the adequacy of their charters on an annual basis.<sup>65</sup> The

<sup>60</sup> See 17 CFR 229.407(e)(3)(iii).

<sup>61</sup> See Amendment No. 1.

<sup>62</sup> See *supra* Section II.A.

<sup>63</sup> See proposed Rule 5605(d)(5).

<sup>64</sup> See *supra* text accompanying notes 33 and 37.

<sup>65</sup> See Notice. In addition, a Smaller Reporting Company, like other listed companies, will be required to certify that it has adopted a formal written compensation committee charter (or, if it so chooses, a board resolution) that specifies the scope of the committee’s responsibilities and its responsibility for determining or recommending to the board for determination the compensation of the

Exchange believes that this approach will minimize new costs imposed on Smaller Reporting Companies and allow them some flexibility not allowed for larger companies.

BX proposes not to exclude a Smaller Reporting Company, however, from its proposal to require a listed company to have, and to certify that it has and will continue to have, a compensation committee of at least two members, each of whom must be an Independent Director as defined in the Exchange's Rule 5605(a)(2).<sup>66</sup> In its discussion of the rules from which Smaller Reporting Companies are not exempt, BX notes that its current listing rules regarding compensation committees do not provide any exemptions for Smaller Reporting Companies.<sup>67</sup>

#### 4. Exemptions

BX proposes that its existing exemptions from the Exchange's compensation-related listing rules currently in place, which are set forth in BX Rule 5615, apply also to the new requirements of the proposed rule change. These include exemptions for asset-backed issuers and other passive issuers, limited partnerships, management investment companies registered under the Investment Company Act of 1940 ("registered management investment companies").<sup>68</sup> BX states that each of these categories has "traditionally been exempt from BX's compensation-related listing rules," and believes that the reasons for the exemptions apply to the new requirements, as well.<sup>69</sup>

Asset-backed issuers and other passive issuers have been exempted, according to the Exchange, because they do not have a board of directors or persons acting in a similar capacity and their activities are limited to passively owning or holding (as well as administering and distributing amounts in respect of) assets on behalf of or for the benefit of the holders of the listed securities. BX further states that the structure of limited partnerships requires that public investors have

CEO and other executive officers. See *supra* notes 27–28.

<sup>66</sup> See proposed Rule 5605(d)(5). See also proposed interpretive material IM–5605–6. As noted above, listed companies other than Smaller Reporting Companies and other exempted issuers must comply with the additional independence requirements for compensation committee members set forth in proposed BX Rule 5605(d)(2)(A). See discussion in Section II.B.1., *supra*.

<sup>67</sup> See Notice.

<sup>68</sup> See Rule 5615(a)(1), (4), and (5).

<sup>69</sup> See Notice. See also discussion below at note 79, *infra*, for transition periods for companies that currently use the Alternative Option and do not have compensation committees.

limited rights and the general partners make all significant decisions about the operation of the limited partnership, and, as such, limited partners do not expect to have a voice in the operations of the partnership. Registered management investment companies, the Exchange states, are already subject to a pervasive system of federal regulation in certain areas of corporate governance.

Finally, BX proposes to add exemptions to its compensation committee rules for cooperatives and controlled companies, which BX proposes to define as companies "of which more than 50% of the voting power for the election of directors is held by an individual, a group or another company." Certain member-owned cooperatives that list their preferred stock are required to have their common stock owned by their members, and BX believes that because of their unique structure and the fact that they do not have a publicly traded class of common stock, they should be exempt from its compensation committee rules.<sup>70</sup> The proposed exemption for controlled companies, BX states, recognizes that majority shareholders, including parent companies, have the right to select directors and control certain key decisions, such as executive officer compensation, by virtue of their ownership rights.<sup>71</sup> The Exchange further states that the proposed exemptions for cooperatives and controlled companies are modeled after the similar exemptions in Nasdaq's rules.<sup>72</sup>

Concerning foreign private issuers, BX's current rules permit any such issuer to follow its home country practice in lieu of many of BX's corporate governance listing standards, including the Exchange's compensation-related listing rules.<sup>73</sup> This allowance is granted on condition that the issuer

<sup>70</sup> See Notice.

<sup>71</sup> See *id.* BX further notes that controlled companies also are exempt from all of the requirements of Rule 10C–1. See Rule 10C–1(b)(5)(ii).

<sup>72</sup> See Nasdaq Listing Rule 5615(a)(2), Nasdaq IM–5615–2, Nasdaq Listing Rule 5615(c) and Nasdaq IM–5615–5.

<sup>73</sup> See Rule 5615(a)(3). Under BX's listing rules, "foreign private issuer" has the same meaning as under Rule 3b–4 under the Exchange Act. See Rule 5005(a)(18). BX's listing rules have traditionally provided qualified exemptions for foreign private issuers so that such 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, except to the extent such exemptions would be contrary to the public securities laws. See Securities Exchange Act Release No. 48745 (November 4, 2003), 68 FR 64154, 64165 (November 12, 2003) (SR–NASD–2002–138).

discloses in its annual report filed with the Commission each requirement that it does not follow and describes the home country practice followed by the issuer in lieu of such requirement.<sup>74</sup> BX proposes that this allowance continue to apply generally to the Exchange's compensation committee rules as revised by the instant proposal on the same condition, namely that the issuer discloses each requirement it does not follow and describes the home country practice it follows in lieu of such requirement. However, with respect, specifically, to the enhanced standards of independence for compensation committees (concerning fees received by members and their affiliations) BX proposes that, if a listed company follows its home country practice, it must additionally disclose in its annual report filed with the Commission the reasons why it does not have an independent compensation committee as set forth in these standards.<sup>75</sup>

#### 5. Transition to the New Rules for Companies Listed as of the Effective Date<sup>76</sup>

The proposed rule change, as amended, provides that certain of the new requirements for listed companies will be effective on July 1, 2013.<sup>77</sup> Specifically, as of that date, listed companies will be required to comply with the provisions of the proposed rule change relating to the authority of a compensation committee to retain compensation consultants, legal counsel, and other compensation advisers; the authority to fund such advisers; and the responsibility of the committee to consider independence factors before selecting such advisers.<sup>78</sup> To the extent a company does not yet have a compensation committee by that

<sup>74</sup> A Foreign Private Issuer that is not required to file its annual report with the Commission on Form 20–F may make this disclosure only on its Web site.

<sup>75</sup> As stated by BX, this proposed condition adopts the requirements of Rule 10C–1(b)(1)(iii)(A)(4), which provides an exemption from the independence requirements of Rule 10C–1 for a "foreign private issuer that discloses in its annual report the reasons that the foreign private issuer does not have an independent compensation committee."

<sup>76</sup> During the transition periods described herein, until a company is required to comply with a particular provision of the new rules, the company must continue to comply with the corresponding provision, if any, in the current rules, which are re-designated as Rule 5605A(d) and IM–5605A–6 ("Sunsetting Provisions"). See Amendment No. 1, which added this clarification as a preamble to the new Rule 5605(d). The addition mirrors a similar statement already included in the original proposal as a preamble to the Sunsetting Provisions.

<sup>77</sup> See proposed Rule 5605(d)(6), as modified by Amendment No. 1 to the proposed rule change. The original proposal provided that these provisions were to be effective immediately.

<sup>78</sup> *Id.*

date,<sup>79</sup> these provisions will apply to the Independent Directors who determine, or recommend to the board for determination, the compensation of the CEO and all other executive officers of the company.<sup>80</sup>

Regarding the remaining new provisions for compensation committees, the proposed rule change, as amended, provides that, in order to allow listed companies to make necessary adjustments in the course of their regular annual meeting schedule, they will have until the earlier of their first annual meeting after January 15, 2014, or October 31, 2014,<sup>81</sup> to comply with these remaining provisions.<sup>82</sup> A listed company must certify to BX, no later than 30 days after the final implementation deadline applicable to it, that it has complied with Rule 5605(d).

#### 6. Phase-In Schedules: IPOs; Companies that Lose their Exemptions; Companies Transferring From Other Markets

BX's existing rules permit a company listing in connection with its initial public offering ("IPO") to phase in its compliance with the Exchange's independence requirements for compensation and nominations committees,<sup>83</sup> as follows: Each such committee must have one independent member at the time of listing; a majority of members must be independent within 90 days of listing; and all members of such committees must be independent within one year of listing. The same

phase-in schedule is permitted for companies emerging from bankruptcy.<sup>84</sup> BX proposes that this schedule continue to apply and that it remain the same with respect to the new compensation committee composition requirements set forth in the proposed rule change.<sup>85</sup>

As stated by BX, this would mean that a company listing on the Exchange in connection with its IPO or a company emerging from bankruptcy would be permitted to phase in its compliance with the requirements that a compensation committee have at least two members, that these members be Independent Directors as defined in BX's rules, and that they meet the enhanced standards of independence for compensation committees (concerning fees received by members and their affiliations) adopted pursuant to Rule 10C-1.<sup>86</sup>

Since BX is proposing to add to its rules an exemption for controlled companies, as discussed above, BX also proposes to add a phase-in schedule for companies ceasing to be controlled companies. This proposed phase-in schedule is modeled after the similar phase-in schedule in Nasdaq's rules.<sup>87</sup>

In addition, BX proposes minor clarifying changes to the phase-in schedule in its current listing rules for companies transferring from other markets, which will now applied to the new compensation-related rules under the proposal.<sup>88</sup> Under this schedule, companies transferring from another national securities exchange with a substantially similar requirement shall be immediately subject to the compensation committee requirement, provided that such companies will be afforded the balance of any grace period afforded by the other market. Companies that are not subject to a substantially similar requirement at the time of listing on BX, such as a company quoted in the over-the-counter market, will be permitted to phase in compliance with the compensation committee composition requirements in Rule 5605(d)(2)(A), including the requirement that compensation committee members be Independent

Directors, the minimum size requirement and the additional eligibility requirements adopted pursuant to Rule 10C-1, on the same schedule as companies listing in connection with an initial public offering.

For a company that was, but has ceased to be, a Smaller Reporting Company, the proposed rule change, as modified by Amendment No. 1, establishes a phase-in schedule based on certain dates relating to the company's change in status.<sup>89</sup> Pursuant to Rule 12b-2 under the Act, a company tests its status as a Smaller Reporting Company on an annual basis as of the last business day of its most recently completed second fiscal quarter (the "Determination Date"). A company with a public float of \$75 million or more as of the Determination Date will cease to be a Smaller Reporting Company as of the beginning of the fiscal year following the Determination Date. Under BX's proposal, the day of this change in status is the beginning of the phase-in period ("Start Date").<sup>90</sup>

By six months from the Start Date, the company will be required to comply with Rule 5605(d)(3), which sets forth the provisions described above relating to authority of a compensation committee to retain compensation advisers, the requirement that the company fund such advisers, and the requirement that the committee consider independence factors before selecting such advisers. By six months from the Start Date, the company will also be required to certify to BX (i) that it has complied with the requirement in Rule 5605(d)(1) to adopt a formal written compensation committee charter including the content specified in Rule 5605(d)(1)(A)-(D);<sup>91</sup> and (ii) that it has complied, or within the applicable phase-in schedule will comply, with the additional requirements in Rule

<sup>79</sup> A listed company that does not currently have a compensation committee is not required to meet the requirement to have such a committee until the earlier of its first annual meeting after January 15, 2014, or October 31, 2014. See *infra* note 81 and accompanying text.

<sup>80</sup> While the provisions of the proposed rule change relating to the authority of a compensation committee to retain compensation advisers, the company's obligation to fund such advisers, and the responsibility of the committee to consider independence factors before selecting such advisers must be assigned to the committee or Independent Directors acting in lieu of a committee by July 1, 2013, the requirement that they be included in a written committee charter does not apply until a later date, as it is one of the remaining provisions of the new compensation committee rule subject to the transition period discussed below. Rule 5605(d)(6) states that companies should consider under state corporate law whether to grant the specific responsibilities and authority referenced through a charter, resolution or other board action.

<sup>81</sup> See proposed Rule 5605(d)(6), as modified by Amendment No. 1 to the proposed rule change. The original proposal had required these provisions to be implemented by the company's second annual meeting after the proposal was approved, but no later than December 31, 2014.

<sup>82</sup> The remaining provisions subject to this schedule include IM-5605-6, which is new interpretive material to be included in the text of BX's rules that elaborates on the compensation committee requirements.

<sup>83</sup> See Rule 5615(b)(1).

<sup>84</sup> See Rule 5615(b)(2).

<sup>85</sup> Specifically, the phase-in schedule would apply to proposed Rule 5605(d)(2).

<sup>86</sup> See Notice for an illustration provided by BX of how the compensation committee composition requirement will interact with the minimum size requirement.

<sup>87</sup> See Nasdaq Rule 5615(c)(3).

<sup>88</sup> See Rule 5615(b)(3). For example, BX proposes to delete the sentence in this provision stating that companies may choose not to adopt a compensation committee and may instead rely upon a majority of the Independent Directors to discharge these responsibilities, as BX has eliminated the Alternative Option.

<sup>89</sup> See proposed Rule 5605(d)(4), as amended. In the proposal as originally submitted, the phase-in schedule was to be the same as the phase-in schedule for a company listing in conjunction with an IPO, and was to start to run on the due date of the filing with the Commission in which the company is required to report that it is an issuer other than a Smaller Reporting Company. In Amendment No. 1, BX states that while the revised phase-in schedule is different from what it originally proposed, the amended version will allow companies sufficient time to adjust to the differences.

<sup>90</sup> See Amendment No. 1.

<sup>91</sup> See *supra* notes 26-29. This includes the provisions with which the company is now required to comply relating to authority of a compensation committee to retain compensation advisers, the requirement that the company fund such advisers, and the requirement that the committee consider independence factors before selecting such advisers.

5605(d)(2)(A) regarding compensation committee composition.

Under the proposal, as amended, a company that has ceased to be a Smaller Reporting Company will be permitted to phase in its compliance with the enhanced independence requirements for compensation committee members (relating to compensatory fees and affiliation) as follows: (i) One member must satisfy the requirements by six months from the Start Date; (ii) a majority of members must satisfy the requirements by nine months from the Start Date; and (iii) all members must satisfy the requirements by one year from the Start Date.<sup>92</sup>

However, because a Smaller Reporting Company is required to have a compensation committee and such committee is required to be comprised of at least two Independent Directors, a company that has ceased to be a Smaller Reporting Company will not be permitted to use the phase-in schedule for these requirements.

#### 7. Conforming Changes and Correction of Typographical Errors

Finally, BX proposes to make minor conforming changes to its requirements relating to audit and nominations committees and to correct certain typographical errors in its current corporate governance requirements.<sup>93</sup>

### III. Discussion

After careful review, the Commission finds that the BX proposal, as amended, is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>94</sup> In particular, the Commission finds that the amended proposed rule change is consistent with the requirements of Section 6(b) of the Act,<sup>95</sup> as well as with Section 10C of the Act<sup>96</sup> and Rule 10C-1 thereunder.<sup>97</sup> Specifically, the Commission finds that the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act,<sup>98</sup> which requires that the rules of a national securities exchange be designed, among other things, 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 not be designed to permit, among other things, unfair discrimination between issuers.

The development and enforcement of meaningful listing standards for a national securities exchange is of substantial importance to financial markets and the investing public. Meaningful listing standards are especially important given investor expectations regarding the nature of companies that have achieved an exchange listing for their securities. The corporate governance standards embodied in the listing rules of national securities exchanges, in particular, play an important role in assuring that companies listed for trading on the exchanges' markets observe good governance practices, including a reasoned, fair, and impartial approach for determining the compensation of corporate executives. The Commission believes that the BX proposal will foster greater transparency, accountability, and objectivity in the oversight of compensation practices of listed issuers and in the decision-making processes of their compensation committees.

In enacting Section 10C of the Act as one of the reforms of the Dodd-Frank Act,<sup>99</sup> Congress resolved to require that "board committees that set compensation policy will consist only of directors who are independent."<sup>100</sup> In June 2012, as required by this legislation, the Commission adopted Rule 10C-1 under the Act, which directs the national securities exchanges to prohibit, by rule, the initial or continued listing of any equity security of an issuer (with certain exceptions) that is not in compliance with the rule's requirements regarding issuer compensation committees and compensation advisers.

In response, BX submitted the proposed rule change, which includes rules intended to comply with the requirements of Rule 10C-1 and additional provisions designed to strengthen the Exchange's listing standards relating to compensation committees. The Commission believes that the proposed rule change, as amended, satisfies the mandate of Rule 10C-1 and otherwise will promote effective oversight of its listed issuers'

executive compensation practices, for the following reasons:

#### A. Compensation Committee Composition and Charter

The Commission believes that it is reasonable for BX to require each company listed on its market to have a compensation committee. Although the Alternative Option to a formal committee in the Exchange's current rules could be useful to a small number of companies, the Commission agrees that the heightened importance of compensation decisions and oversight of executive compensation in today's environment, as well as the benefits that can result for investors of having a standing committee overseeing compensation matters, makes it appropriate and consistent with investor protection and the public interest under Section 6(b)(5) of the Act for BX to raise its standards in this regard. In making this determination the Commission is aware that Rule 10C-1 does not require listed companies of national securities exchanges to have a committee dedicated to compensation matters. Nevertheless, it is consistent with Section 6(b)(5) of the Act for BX to require all its listed companies to have an independent compensation committee overseeing executive compensation matters because of the importance and accountability to investors that such a formal structure can provide.<sup>101</sup> The Commission also notes that some of the other requirements of Rule 10C-1 apply only when a company has a committee overseeing compensation matters.<sup>102</sup> Thus, the requirement to have a compensation committee will trigger the additional protections for shareholders created by these requirements.

Similarly, the Commission believes that it is appropriate for BX to raise its standards to require the compensation committee of each issuer to have at least two members, instead of permitting a sole individual to be responsible for compensation policy, and that this furthers investor protection and the public interest in accordance with Section 6(b)(5). In light of the importance of compensation matters, the added thought and objectivity that is

<sup>92</sup> During the phase-in schedule, a company that has ceased to be a Smaller Reporting Company will be required to continue to comply with the rules previously applicable to it.

<sup>93</sup> See Exhibit 5 of the proposed rule change.

<sup>94</sup> In approving the BX proposed rule change, as amended, the Commission has considered its impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

<sup>95</sup> 15 U.S.C. 78f(b).

<sup>96</sup> 15 U.S.C. 78j-3.

<sup>97</sup> 17 CFR 240.10C-1.

<sup>98</sup> 15 U.S.C. 78f(b)(5).

<sup>99</sup> See *supra* note 7.

<sup>100</sup> See H.R. Rep. No. 111-517, Joint Explanatory Statement of the Committee of Conference, Title IX, Subtitle E "Accountability and Executive Compensation," at 872-873 (Conf. Rep.) (June 29, 2010).

<sup>101</sup> See, e.g., Section 303A.05 of the New York Stock Exchange ("NYSE") Listed Company Manual, which does not provide for an Alternative Option as is currently allowed under BX rules.

<sup>102</sup> Under Rule 10C-1, the provisions of Rule 10C-1(b)(2)(i) (concerning the authority to retain or obtain the advice of a compensation adviser) and Rule 10C-1(b)(3) (concerning funding for compensation advisers) do not apply to members of the board of directors who oversee executive compensation matters on behalf of the board of directors outside a committee structure.

likely to result when two or more individuals deliberate over how much a listed company should pay its executives, and what form such compensation should take, is consistent with the goal of promoting more accountability to shareholders on executive compensation matters. Moreover, given the complexity of executive compensation packages for corporate executives, it is reasonable for BX to require listed companies to have the input of more than one committee member on such matters. The Commission believes that the two-member requirement will not be an onerous burden for companies and should actually strengthen their review of compensation matters.

The proposal by the Exchange to require a compensation committee to have a written charter detailing the committee's authority and responsibility is also consistent with Section 6(b)(5) of the Act and will help listed companies to comply with the rules being adopted by BX to fulfill its mandate under Rule 10C-1. For example, as noted above, under BX's proposal the charter must set forth the compensation committee's responsibilities as well as the specific authority concerning compensation advisers as required under Rule 10C-1.<sup>103</sup> A written charter will also provide added transparency for shareholders regarding how a company determines compensation and may clarify and improve the process itself. In this regard, the Commission notes that BX's requirement that listed companies review and reassess the adequacy of the compensation's committee charter on an annual basis will also help to ensure accountability and transparency on an on-going basis. The Commission also notes that several exchanges already require their compensation committees to have written charters.<sup>104</sup>

As discussed above, under Rule 10C-1 the exchanges must adopt listing standards that require each member of a compensation committee to be independent, and to develop a definition of independence after considering, among other relevant factors, the source of compensation of a director, including any consulting, advisory or other compensatory fee paid by the issuer to the director as well as

<sup>103</sup> The Commission notes that the provision that is required in the charter regarding the authority of the committee to retain compensation advisers, the requirement that the company fund such advisers, and the requirement that the committee consider independence factors before selecting such advisers does not apply under the BX proposal to Smaller Reporting Companies. See *supra* notes 62–65 and accompanying text.

<sup>104</sup> See, e.g., NYSE Listed Company Manual, Section 303A.05.

whether the director is affiliated with the issuer or any of its subsidiaries or their affiliates.

The Commission notes, however, that Rule 10C-1 leaves it to each exchange to formulate a final definition of independence for these purposes, subject to review and final Commission approval pursuant to Section 19(b) of the Act. As the Commission stated in the Rule 10C-1 Adopting Release, "given the wide variety of issuers that are listed on exchanges, we believe that the exchanges should be provided with flexibility to develop independence requirements appropriate for the issuers listed on each exchange and consistent with the requirements of the independence standards set forth in Rule 10C-1(b)(1)."<sup>105</sup> This discretion comports with the Act, which gives the exchanges the authority, as self-regulatory organizations, to propose the standards they wish to set for companies that seek to be listed on their markets, consistent with the Act and the rules and regulations thereunder, and, in particular, Section 6(b)(5) of the Act.

As noted above, in addition to retaining its existing independence standards that currently apply to board and compensation committee members, which include certain bright-line tests, BX has determined to adopt a definition that prohibits a director who receives compensation or fees from a listed company (other than, among other things, director compensation) from serving on the company's compensation committee.<sup>106</sup>

As the Exchange noted in its proposal, under the bright-line tests of its general rules for director independence, directors can still be considered independent and serve on listed companies' compensation committees if they receive fees that do not exceed certain thresholds.<sup>107</sup> This is in contrast to BX's requirements to serve on a listed company's audit committee, which bar a director who receives any compensatory fees from the company. In considering the Fees Factor under Rule 10C-1, BX stated that it did not see any compelling justification to set a different standard with respect to the acceptance of compensatory fees for members of the compensation committee than for members of audit committees.

The Commission believes that the Exchange has complied with Rule 10C-

<sup>105</sup> As explained further in the Rule 10C-1 Adopting Release, prior to final approval, the Commission will consider whether the exchanges' proposed rule changes are consistent with the requirements of Section 6(b) and Section 10C of the Exchange Act.

<sup>106</sup> See *supra* note 33–36 and accompanying text.

<sup>107</sup> See BX Listing Rules 5605(a)(2)(B) and (D).

1 and Section 10C and that the proposed compensatory fee restriction, which is designed to protect investors and the public interest, is consistent with the requirements of Section 6(b)(5) of the Act. The Commission notes that the compensatory fee restriction will help to ensure that compensation committee members cannot receive directly or indirectly fees that could potentially influence their decisions on compensation matters.<sup>108</sup>

With respect to the Affiliation Factor of Rule 10C-1, BX has concluded that an outright bar from service on a company's compensation committee of any director with an affiliation with the company, its subsidiaries, and their affiliates is inappropriate for compensation committees. BX's existing independence standards will also continue to apply to those directors serving on the compensation committee. BX maintains that it may be appropriate for certain affiliates, such as representatives of significant stockholders, to serve on compensation committees "since their interests are likely aligned with those of other stockholders in seeking an appropriate executive compensation program." The Commission believes that BX's approach of requiring boards only to consider such affiliations, rather than an outright ban on them, is reasonable and consistent with the requirements of the Act.

The Commission notes that Congress, in requiring the Commission to direct the exchanges to consider the Affiliation Factor, did not declare that an absolute bar was necessary. Moreover, as the Commission stated in the Rule 10C-1 Adopting Release, "In establishing their independence requirements, the exchanges may determine that, even though affiliated directors are not allowed to serve on audit committees, such a blanket prohibition would be inappropriate for compensation committees, and certain affiliates, such as representatives of significant shareholders, should be permitted to serve."<sup>109</sup> In determining that BX's

<sup>108</sup> See Nasdaq Approval Order, *supra* note 5, for a discussion of the comments received on Nasdaq's substantially similar proposal on compensatory fees for compensation committee members.

<sup>109</sup> Rule 10C-1 Adopting Release. At the same time, the Commission noted that significant shareholders may have other relationships with the listed company that would result in such shareholders' interests not being aligned with those of other shareholders and that the exchanges may want to consider these other ties between a listed issuer and a director. While the Exchange did not adopt any additional factors, the current affiliation standard would still allow a company to prohibit a director whose affiliations "impair the director's judgment" as a member of the committee.



affiliation standard is consistent with Sections 6(b)(5) and 10C under the Act, the Commission notes that BX's proposal requires a company's board, in selecting compensation committee members, to consider whether any such affiliation would impair a director's judgment as a member of the compensation committee. We believe that this should give companies the flexibility to assess whether a director who is an affiliate, including a significant shareholder, should or should not serve on the company's compensation committee, depending on the director's particular affiliations with the company.

As to consideration by BX of whether it should adopt any additional relevant independence factors, the Exchange stated that it reviewed its rules in the light of Rule 10C-1, but concluded that its existing rules together with its proposed rules are sufficient to ensure committee member independence. The Commission believes that, through this review, the Exchange has complied with the requirement that it consider relevant factors, including, but not limited to, the Fees and Affiliation Factors in determining its definition of independence for compensation committee members.

The Commission notes that BX discussed in its proposal why it did not include, specifically, personal and business relationships as a factor. BX cites its standards for Independent Directors, generally, which require the board of directors of a listed issuer to make an affirmative determination that each such director has no relationship that, in the opinion of the board, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.<sup>110</sup> All compensation committee members must meet the general independence standards under BX's rules in addition to the two new criteria being adopted herein. The Commission therefore expects that boards, in fulfilling their obligations, will apply this standard to each such director's individual responsibilities as a board member, including specific committee memberships such as the compensation committee. The Commission further notes that compliance with BX's rules and the provision noted above would demand that a board consider personal and business relationships and related party transactions, among other factors that may be relevant, when evaluating the independence of compensation

committee members and, for that matter, all Independent Directors on the board.

BX proposes that the "Exceptional and Limited Circumstances" provision in its current rules, which allows one director who fails to meet the Exchange's Independent Director definition to serve on a compensation committee under certain conditions, apply to the enhanced independence standards discussed above that the Exchange is adopting to comply with Rule 10C-1. The Commission believes that the discretion granted to each exchange by Rule 10C-1, generally, to determine the independence standards it adopts to comply with the Rule includes the leeway to carve out exceptions to those standards, as long as they are consistent with the Act. BX also cites, in justifying the exception, the provision of Rule 10C-1 that permits an exchange to exempt a particular relationship with respect to members of the compensation committee as the exchange determines is appropriate, taking into consideration the size of an issuer and any other relevant factors. In this respect, BX states that the flexibility afforded by the exception is particularly important for a smaller company.

Moreover, the Commission approved as consistent with the Act the same exception and concept in the context of BX's current rules requiring each member of a compensation committee to be an Independent Director under Exchange Rule 5605(a)(2), as well in the context of the independence requirements for nominations committees and audit committees. Although the additional independence standards required by Rule 10A-3 for audit committees are not subject to this exception, the Commission notes that Rule 10C-1 grants exchanges more discretion than Rule 10A-3 when considering independence standards for compensation committee membership. The Commission also notes that a member appointed under the Exceptional and Limited Circumstances provision may not serve longer than two years. As BX notes, the additional change to allow a company to rely on the exception for a non-Independent Director who is a family member of a non-executive employee of the company—which the Exchange is proposing to adopt with respect to the Exceptional and Limited Circumstances provisions in both its compensation and audit committee rules—has already been approved by the Commission for the Nasdaq market as an allowance in the corporate governance listing standards of that exchange for both

types of committees.<sup>111</sup> The Commission therefore finds that applying this additional change in the BX rules for both committees is consistent with Section 6(b)(5).

#### *B. Authority of Committees to Retain Compensation Advisers; Funding; and Independence of Compensation Advisers and Factors*

As discussed above, BX proposes to set forth explicitly in its rules the requirements of Rule 10C-1 regarding a compensation committee's authority to retain compensation advisers, its responsibilities with respect to such advisers, and the listed company's obligation to provide appropriate funding for payment of reasonable compensation to a compensation adviser retained by the committee.<sup>112</sup> As such, the Commission believes these provisions meet the mandate of Rule 10C-1 and are consistent with the Act.

As discussed above, the proposed rule change requires the compensation committee of a listed company to consider the six factors relating to independence that are enumerated in the proposal before selecting a compensation consultant, legal counsel or other adviser to the compensation committee. The Commission believes that this provision is consistent with Rule 10C-1 and Section 6(b)(5) of the Act.

The Commission notes that Rule 10C-1 includes an instruction that specifically requires a compensation committee to conduct the independence assessment with respect to "any compensation consultant, legal counsel or other adviser that provides advice to the compensation committee, other than

<sup>111</sup> Nasdaq's rules regarding the independence of audit, nominations, and compensation committee members have included an allowance for Exceptional and Limited Circumstances when a member ceases to be independent since 2003. See Securities Exchange Act Release No. 48745 (November 4, 2003), 68 FR 64154 (November 12, 2003). (The allowance did not apply to the audit committee standards required by Rule 10A-3. See *id.*) In June 2012, when Nasdaq amended its rules to allow the provision to be used when a family member of the director is an employee of the company, as long as the family member is not an executive officer, see *supra* note 48, the change was made to the rules for compensation committees in tandem with the similar change for the other two committees and the Commission found these changes consistent with Section 6(b)(5) of the Act. The Commission notes that, when Nasdaq recently proposed additional independence standards for compensation committees to comply with Rule 10C-1, it proposed to extend the Exceptional and Limited Circumstances allowance, including the change regarding family members of non-executive officers, to the new requirements.

<sup>112</sup> The Commission notes that, in Amendment No. 1, BX revised its proposed rule text to set forth these requirements in full.

<sup>110</sup> See BX Rule 5605(a)(2).

in-house counsel,”<sup>113</sup> and thus requires an independence assessment with respect to regular outside legal counsel. To avoid any confusion, BX, in Amendment No. 1, added rule text that reflects this instruction in its own rules.<sup>114</sup>

In approving this aspect of the proposal, the Commission notes that compliance with the rule requires an independence assessment of any compensation consultant, legal counsel, or other adviser that provides advice to the compensation committee, and is not limited to advice concerning executive compensation. However, BX has proposed, in Amendment No. 1, to add language to the provision regarding the independence assessment of compensation advisers<sup>115</sup> to state that the compensation committee is not required to conduct an independence assessment for a compensation adviser that acts in a role limited to the following activities for which no disclosure is required under Item 407(e)(3)(iii) of Regulation S-K: (a) Consulting on any broad-based plan that does not discriminate in scope, terms, or operation, in favor of executive officers or directors of the company, and that is available generally to all salaried employees; and/or (b) providing information that either is not customized for a particular issuer or that is customized based on parameters that are not developed by the adviser, and about which the adviser does not provide advice. BX states that this exception is based on Item 407(e)(3)(iii) of Regulation S-K, which provides a limited exception to the Commission’s requirement for a registrant to disclose any role of compensation consultants in determining or recommending the amount and form of a registrant’s executive and director compensation.<sup>116</sup>

The Commission views BX’s proposed exception as reasonable, as the Commission determined, when adopting the compensation consultant disclosure requirements in Item 407(e)(3)(iii), that the two excepted categories of advice do not raise conflict of interest concerns.<sup>117</sup> The Commission

also made similar findings when it noted it was continuing such exceptions in the Rule 10C-1 Adopting Release, including excepting such roles from the new conflict of interest disclosure rule required to implement Section 10C(c)(2). The Commission also believes that the exception should allay some of the concerns raised by the commenters on other filings regarding the scope of the independence assessment requirement.<sup>118</sup> Based on the above, the Commission believes these limited exceptions are consistent with the investor protection provisions of Section 6(b)(5) of the Act.

As already discussed, nothing in the proposed rule prevents a compensation committee from selecting any adviser that it prefers, including ones that are not independent, after considering the six factors. In this regard, the Commission notes that, in Amendment No. 1, BX added specific rule language to clarify, among other things, that the rule does not require a compensation adviser to be independent, only that the compensation committee must consider the six independence factors before selecting or receiving advice from a compensation adviser.<sup>119</sup>

As previously stated by the Commission in adopting Rule 10C-1, the requirement that compensation committees consider the independence of potential compensation advisers before they are selected should help assure that compensation committees of affected listed companies are better informed about potential conflicts, which could reduce the likelihood that they are unknowingly influenced by conflicted compensation advisers.<sup>120</sup> The changes to BX’s rules on compensation advisers should therefore benefit investors in BX listed companies and are consistent with the requirements in Section 6(b)(5) of the Act that rules of the exchange further investor protection and the public interest.

Finally, one commenter on the substantially similar proposal relating to the Rule 10C-1 requirements submitted by Nasdaq<sup>121</sup> requested guidance “on how often the required independence assessment should occur.”<sup>122</sup> This commenter observed that it “will be extremely burdensome and disruptive if prior to each compensation committee

meeting, the committee had to conduct a new assessment.” The Commission anticipates that compensation committees will conduct such an independence assessment at least annually.<sup>123</sup>

### C. Application to Smaller Reporting Companies

The Commission believes that the requirement for Smaller Reporting Companies, like all other listed companies, to have a compensation committee, composed solely of Independent Directors, with at least two members is reasonable and consistent with the protection of investors. The Commission notes that BX’s rules for compensation committees have not made a distinction for Smaller Reporting Companies in the past. However, consistent with the exemption of Smaller Reporting Companies from Rule 10C-1, the Exchange has decided not to require Smaller Reporting Companies to meet its proposed new independence requirements as to compensatory fees and affiliation as well as the requirements concerning compensation advisers.

BX will also require a Smaller Reporting Company to adopt a formal written compensation committee charter or board resolution that specifies the compensation committee’s responsibilities and authority, but the company will not be required to review and reassess the adequacy of the charter or board resolution on an annual basis. This is different from the rules for other listed companies, which will be required to include the committee’s responsibilities and authority specifically in a formal written charter and to review the charter’s adequacy on an annual basis.

The Commission believes that these provisions are consistent with the Act and do not unfairly discriminate between issuers. The Commission believes that, for similar reasons to those for which Smaller Reporting Companies are exempted from the Rule 10C-1 requirements, it makes sense for BX to provide some flexibility to Smaller Reporting Companies regarding whether the compensation committee’s responsibilities should be set forth in a formal charter or through board resolution. Further, because a Smaller Reporting Company does not need to include in its charter or board resolution the additional provisions regarding compensation advisers that BX is requiring all other listed companies to

<sup>113</sup> See Instruction to paragraph (b)(4) of Rule 10C-1.

<sup>114</sup> See *supra* note 54 and accompanying text.

<sup>115</sup> See proposed Rule 5605(d)(3), as amended by Amendment No. 1.

<sup>116</sup> See 17 CFR 229.407(e)(3)(iii).

<sup>117</sup> See Proxy Disclosure Enhancements, Securities Act Release No. 9089 (Dec. 19, 2009), 74 FR 68334 (Dec. 23, 2009), at 68348 (“We are persuaded by commenters who noted that surveys that provide general information regarding the form and amount of compensation typically paid to executive officers and directors within a particular industry generally do not raise the potential

conflicts of interest that the amendments are intended to address.”).

<sup>118</sup> See Nasdaq Approval Order and NYSE Approval Order, *supra* note 5.

<sup>119</sup> See *supra* notes 56–58 and accompanying text.

<sup>120</sup> See Rule 10C-1 Adopting Release, *supra* note 9.

<sup>121</sup> See Nasdaq Approval Order, *supra* note 5.

<sup>122</sup> See *id.*

<sup>123</sup> See *id.*

include to comply with Rule 10C-1,<sup>124</sup> and in view of the potential additional costs of an annual review, it is reasonable not to require a Smaller Reporting Company to conduct an annual assessment of its charter or board resolution.

#### D. Opportunity to Cure Defects

Rule 10C-1 requires the rules of an exchange to provide for appropriate procedures for a listed issuer to have a reasonable opportunity to cure any defects that would be the basis for the exchange, under Rule 10C-1, to prohibit the issuer's listing. Rule 10C-1 also specifies that, with respect to the independence standards adopted in accordance with the requirements of the Rule, an exchange may provide a cure period until the earlier of the next annual shareholders meeting of the listed issuer or one year from the occurrence of the event that caused the member to be no longer independent.

The Commission notes that the cure period that BX proposes for companies that fail to comply with the enhanced independence requirements designed to comply with Rule 10C-1 is not exactly the same as the cure period that the Rule sets forth as an option.<sup>125</sup> The BX proposal adds the proviso that, if the annual shareholders meeting occurs no later than 180 days following the event that caused the noncompliance, the company instead has 180 days from the event to regain compliance.

The Commission believes that, although the cure period proposed by BX gives a company more leeway in certain circumstances than the cure period suggested under Rule 10C-1, the accommodation is fair and reasonable. As a general matter, it allows all companies at least 180 days to cure noncompliance. To give a specific example, the proposal would afford a company additional time to comply, than the Rule 10C-1 option, where a member of the compensation committee ceases to be independent two weeks before the company's next annual meeting. The Commission further notes BX already has a similar cure period

with respect to other BX corporate governance requirements.<sup>126</sup>

The Commission notes that Rule 10C-1 requires that an exchange provide a company an opportunity to cure any defects in compliance with any of the new requirements. The Commission believes that BX's general due process procedures for the delisting of companies that are out of compliance with the Exchange's rules satisfy this requirement.<sup>127</sup> In particular, BX's rules provide that, unless continued listing of the company raises a public interest concern, when a company is deficient in compliance with, among other rules, Rule 5605, which includes the Exchange's standards for compensation committees, the listed company may submit a plan for compliance. The rules permit the Exchange's staff to extend the deadline for regaining compliance, under established parameters, and, if the company does not regain compliance within the time period provided by all applicable staff extensions—at which point the staff will immediately issue a determination indicating the date on which the company's securities will be suspended—a company can still request review by a hearings panel.

The Commission believes that these general procedures for companies out of compliance with listing requirements, in addition to the particular cure provisions for failing to meet the new independence standards, adequately meet the mandate of Rule 10C-1 and also are consistent with investor protection and the public interest since they give a company a reasonable time period to cure non-compliance with these important requirements before they will be delisted.

#### E. Exemptions

As discussed above, asset-backed issuers and other passive issuers, limited partnerships, and registered management investment companies are exempt from BX's existing rules relating to compensation, and BX proposes to extend the exemptions for these entities to the new requirements of the proposed rule change. The Commission notes that Rule 10C-1 allows exchanges to exempt from the listing rules adopted pursuant to Rule 10C-1 certain categories of issuers, as the national securities

exchange determines is appropriate.<sup>128</sup> The Commission believes that, given the specific characteristics of the aforementioned types of issuers,<sup>129</sup> it is reasonable and consistent with Section 6(b)(5) of the Act for the Exchange to exempt them from the new requirements. Similarly, the specific characteristics of cooperatives and controlled companies make it reasonable for BX to adopt the proposed exemptions for these entities.<sup>130</sup> The Commission notes, in addition, that other exchanges already have exemptions for these kinds of issuers.<sup>131</sup>

Specifically with regard to BX's proposed exemption for registered management investment companies, the Commission notes that, although Rule 10C-1 exempts certain entities, including registered open-end management investment companies, from the enhanced independence requirements for members of compensation committees, it does not explicitly exempt other types of registered management investment companies, including closed-end funds, from any of the requirements of Rule 10C-1. Under the BX proposal, both closed-end and open-end funds would be exempt from all the requirements of the rule.

The Commission believes that it is reasonable to extend its exemption to all registered investment companies, including closed-end funds, because the Investment Company Act of 1940 already assigns important duties of investment company governance, such as approval of the investment advisory contract, to independent directors, and because such entities were already generally exempt from BX's existing compensation committee requirements. The Commission notes that almost all registered investment companies do not employ executives or employees or have compensation committees.

The Commission notes that BX proposes, however, to amend its current rule for foreign private issuers, which allows such issuers to follow their home country practice in lieu of the

<sup>128</sup> The Commission notes, moreover, that, in the case of limited partnerships and open-end registered management investment companies, Rule 10C-1 itself provides exemptions from the independence requirements of the Rule.

<sup>129</sup> See *supra* Section II.B.4.

<sup>130</sup> The Commission notes that controlled companies are provided an automatic exemption from the application of the entirety of Rule 10C-1 by Rule 10C-1(b)(5). The additional BX provisions requiring listed companies to have a two-member compensation committee and a written committee charter, will, of course, not apply to the exempted entities, which are currently required to have neither a compensation committee nor the Alternative Option.

<sup>131</sup> See *supra* note 72.

<sup>124</sup> As discussed *supra* notes 64-65 and accompanying text, the charter or board resolution of a Smaller Reporting Company will not be required to include, like the charters of other listed companies, a grant of authority to the committee to retain compensation advisers, a requirement that the company fund such advisers, and a requirement that the committee consider independence factors before selecting such advisers, because Smaller Reporting Companies are not subject to these requirements.

<sup>125</sup> See *supra* notes 42-44 and accompanying text.

<sup>126</sup> See *supra* note 42. The existing and proposed cure provisions in BX's rules mirror similar accommodations in Nasdaq's rules for issuers that lose an independent director or audit committee member. See Securities Exchange Act Release No. 54421 (September 11, 2006), 71 FR 54698 (September 18, 2006) (Commission approval of File No. SR-NASDAQ-2006-011).

<sup>127</sup> See, generally, BX Rule 5810.

Exchange's standards regarding a company's compensation decision-making process. The current rule includes the proviso that the issuer must disclose its reliance on the exemption. BX proposes to conform its rules in this regard with the provision of Rule 10C-1 permitting a foreign private issuer to follow home country practice only when it meets the additional condition that the issuer disclose the reasons why it does not have an independent compensation committee.

#### F. Transition to the New Rules for Companies Listed as of the Effective Date

The Commission believes that the deadlines for compliance with the proposal's various provisions are reasonable and should afford companies that may be listed on BX as of the effective date adequate time to make the changes, if any, necessary to meet the new standards. The Commission notes that the provision in the original proposal requiring companies to comply with certain of the requirements immediately has been revised in Amendment No. 1 to allow companies until July 1, 2013 to satisfy these requirements.<sup>132</sup> The Commission also believes that the revised deadline proposed in Amendment No. 1, which gives companies until the earlier of their first annual meeting after January 15, 2014, or October 31, 2014, to comply with the remaining provisions is more clear-cut than the deadline in the original proposal and also matches the deadline set forth by the New York Stock Exchange in its proposed rule change to comply with Rule 10C-1.<sup>133</sup>

#### G. Phase-In Schedules: IPOs; Companies That Lose Their Exemptions; Companies Transferring From Other Markets

The Commission believes that it is reasonable for BX to allow, with respect to IPOs, companies emerging from bankruptcy, companies ceasing to be controlled companies, and companies transferring from other markets, the same phase-in schedule for compliance with the new requirements as is permitted under its current compensation-related rules.

The Commission also believes that the phase-in schedule for companies that cease to be Smaller Reporting Companies, as revised in Amendment No. 1, affords such companies ample time to come into compliance with the

full panoply of rules that apply to other companies. In the Commission's view, the revised schedule also offers such companies more clarity in determining when they will be subject to the heightened requirements.

#### IV. Accelerated Approval of Amendment No. 1 to the Proposed Rule Change

The Commission finds good cause, pursuant to Section 19(b)(2) of the Act,<sup>134</sup> for approving the proposed rule change, as modified by Amendment No. 1, prior to the 30th day after the date of publication of notice in the **Federal Register**. The change made to the proposal by Amendment No. 1 to set forth in detail the requirements of Rule 10C-1(b)(2)-(4) explicitly in the Exchange's rules, rather than incorporating these details by reference as in the original proposal,<sup>135</sup> is not a substantive one and merely codifies the original intent of that provision. Moreover, the change improves the proposal because it brings together the full set of the Exchange's rules on compensation committees in one place, thereby easing compliance for listed companies and benefiting investors seeking an understanding of an issuer's obligations with regard to determining executive compensation.

The change made by Amendment No. 1 to require companies listed on BX as of the effective date of the proposal to comply with certain of the new rules by July 1, 2013 rather than immediately, as originally proposed,<sup>136</sup> reasonably affords companies more time to take the steps necessary for compliance. The change to require such companies to comply with the remaining provisions by the earlier of their first annual meeting after January 15, 2014, or October 31, 2014, rather than by the deadline originally proposed,<sup>137</sup> still allows ample time for companies to adjust to the new rules, and accords with the deadline set by NYSE in its proposed rule change to comply with Rule 10C-1, which was published at the same time as the BX proposal.<sup>138</sup>

<sup>134</sup> 15 U.S.C. 78s(b)(2).

<sup>135</sup> See *supra* note 49 and accompanying text.

<sup>136</sup> See *supra* note 77 and accompanying text.

<sup>137</sup> See *supra* note 81 and accompanying text.

<sup>138</sup> The Commission received one comment letter relating to this provision in the NYSE proposal, in which the commenter supported this transition period for compliance with the new compensation committee independence standards but believed that a longer period should be provided to implement the other listing standards that NYSE proposed. See Letter to Elizabeth M. Murphy, Secretary, Commission, from Robert B. Lamm, Chair, Securities Law Committee, The Society of Corporate Secretaries & Governance Professionals, concerning File No. SR-NYSE-2012-49, dated December 7, 2012.

The revision made by Amendment No. 1 to the phase-in rules for companies that cease to be Smaller Reporting Companies<sup>139</sup> establishes a schedule that is easier to understand, while still affording such companies adequate time to come into compliance. The Commission notes that the Start Date of the phase-in period for such a company is six months after the Determination Date, and the company is given no less than another six months from the Start Date to gain compliance with the rules from which it had been previously exempt. Moreover, with respect to the enhanced independence standards for compensation committee members (relating to fees and affiliation with the company), only one member must meet these standards within six months after the Start Date. The company is given nine months from the Start Date (*i.e.*, fifteen months from the Determination Date) to have a majority of committee members meeting the standards, and a full year from the Start Date (*i.e.*, eighteen months from the Determination Date) to fully comply with the standards.

The addition by Amendment No. 1 of a preamble to proposed Rule 5605(d) to set forth the obligations of a company during the transition period until the new rules apply introduces no substantive change.<sup>140</sup> It merely mirrors the instructions in the preamble to the Sunset Provisions, providing clarity for listed companies.

The inclusion in Amendment No. 1 of language in BX's rules that requires a compensation committee to conduct the independence assessment with respect to "any compensation consultant, legal counsel or other adviser that provides advice to the compensation committee, other than in-house counsel" merely reflects an instruction in Rule 10C-1 itself.<sup>141</sup> The addition of further guidance by Amendment No. 1 merely clarifies that nothing in the Exchange's rules requires a compensation adviser to be independent, only that the compensation committee consider the independence factors before selecting or receiving advice from a compensation adviser,<sup>142</sup> and is not a substantive change.

Amendment No. 1 also excluded advisers that provide certain types of services from the independence assessment.<sup>143</sup> As discussed above, the Commission has already determined to exclude such advisers from the

<sup>139</sup> See *supra* note 89 and accompanying text.

<sup>140</sup> See *supra* note 76.

<sup>141</sup> See *supra* note 113 and accompanying text.

<sup>142</sup> See *supra* note 56 and accompanying text.

<sup>143</sup> See *supra* notes 59-60 and accompanying text.

<sup>132</sup> See *supra* notes 73-74 for the provisions to which the new transition date applies.

<sup>133</sup> See Securities Exchange Act Release No. 68011 (October 9, 2012), 77 FR 62541 (October 15, 2012) (Notice of File No. SR-NYSE-2012-49).

disclosure requirement regarding compensation advisers in Regulation S-K because these types of services do not raise conflict of interest concerns. For all the reasons discussed above, the Commission finds good cause to accelerate approval of the proposed changes made by Amendment No. 1.

#### V. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing and whether Amendment No. 1 are consistent with the Act. Comments may be submitted by any of the following methods:

##### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-BX-2012-063 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090.

All submissions should refer to File Number SR-BX-2012-063. This file number should be included on the subject line if email is used.

To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). 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 Web site viewing and printing in the Commission's Public Reference Room on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of BX. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-BX-2012-063, and should

be submitted on or before February 12, 2013.

#### VI. Conclusion

In summary, and for the reasons discussed in more detail above, the Commission believes that the rules being adopted by BX, taken as whole, should benefit investors by helping listed companies make informed decisions regarding the amount and form of executive compensation. BX's new rules will help to meet Congress's intent that compensation committees that are responsible for setting compensation policy for executives of listed companies consist only of independent directors.

BX's rules also, consistent with Rule 10C-1, require compensation committees of listed companies to assess the independence of compensation advisers, taking into consideration six specified factors. This should help to assure that compensation committees of BX-listed companies are better informed about potential conflicts when selecting and receiving advice from advisers. Similarly, the provisions of BX's standards that require compensation committees to be given the authority to engage and oversee compensation advisers, and require the listed company to provide for appropriate funding to compensate such advisers, should help to support the compensation committee's role to oversee executive compensation and help provide compensation committees with the resources necessary to make better informed compensation decisions.

For the foregoing reasons, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with Section 6(b)(5) of the Act.<sup>144</sup>

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>145</sup> that the proposed rule change, SR-BX-2012-063, as modified by Amendment No. 1, is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>146</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

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<sup>144</sup> 15 U.S.C. 78f(b)(5).

<sup>145</sup> 15 U.S.C. 78s(b)(2).

<sup>146</sup> 17 CFR 200.30-3(a)(12).

#### SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-68643; File No. SR-BATS-2012-039]

#### Self-Regulatory Organizations; BATS Exchange, Inc.; Notice of Filing of Amendment Nos. 2 and 3, and Order Granting Accelerated Approval of Proposed Rule Change, as Modified by Amendment Nos. 1, 2 and 3, To Amend the Listing Rules for Compensation Committees To Comply With Securities Exchange Act Rule 10C-1 and Make Other Related Changes

January 11, 2013.

#### I. Introduction

On September 25, 2012, BATS Exchange, Inc. ("Exchange" or "BATS") 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 modify the Exchange's rules for compensation committees of listed issuers to comply with Rule 10C-1 under the Act and make other related changes. On October 9, 2012, BATS filed Amendment No. 1 to the proposed rule change.<sup>3</sup> The proposed rule change, as modified by Amendment No. 1, was published for comment in the **Federal Register** on October 15, 2012.<sup>4</sup> The Commission subsequently extended the time period in which to either approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change, to January 13, 2013.<sup>5</sup> The Commission received no comment letters on the proposed rule change.<sup>6</sup> On January 10, 2013, the Exchange filed Amendment No. 2 to the proposed rule change.<sup>7</sup> On

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

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

<sup>3</sup> Amendment No. 1 replaced the proposed rule change in full.

<sup>4</sup> See Securities Exchange Act Release No. 68022 (October 9, 2012), 77 FR 62572 ("Notice").

<sup>5</sup> See Securities Exchange Act Release No. 68313 (November 28, 2012), 77 FR 71853 (December 4, 2012).

<sup>6</sup> The Commission notes that comments were received on substantially similar proposals filed by New York Stock Exchange, LLC and Nasdaq Stock Market LLC. For a synopsis of these comments see Securities Exchange Act Release Nos. 68011 (October 9, 2012) ("NYSE Notice") (File No. SR-NYSE-2012-49); 68013 (October 9, 2012) ("Nasdaq Notice") (File No. SR-NASDAQ-2012-109); 68639 (January 11, 2013), ("NYSE Approval Order"); 68640 (January 11, 2013), ("Nasdaq Approval Order").

<sup>7</sup> In Amendment No. 2 to SR-BATS-2012-039, BATS proposes to: (1) Add additional language to further outline the responsibilities of the compensation committee, as well as to make certain clarifying changes to the compensation committee's