

**SECURITIES AND EXCHANGE COMMISSION**  
**(Release No. 34-49611; File No. SR-BSE-2004-10)**

**April 23, 2004**

**Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change by the Boston Stock Exchange, Inc., and Notice of Filing and Granting Accelerated Approval to Amendment No. 1 to Permit the Separation of the Chairman and Chief Executive Officer Positions**

**I. Introduction**

On March 2, 2004, the Boston Stock Exchange, Inc. (“BSE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend its Constitution to permit the separation of the functions of Chairman and of Chief Executive Officer (“CEO”). The proposed rule change was published for comment in the Federal Register on March 17, 2003.<sup>3</sup> The Commission received no comments on the proposal.

Subsequently, on April 14, 2004, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>4</sup> In Amendment No. 1, the Exchange proposes several changes to the original filing. Amendment No. 1 clarifies the duties the Chairman and the CEO would perform when those positions are held by the same person or by different persons. Amendment No. 1 also incorporates a provision governing executive sessions of the Board, and bars the CEO from

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<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. 49434, 69 FR 13922 (March 24, 2004).

<sup>4</sup> See letter from John Boese, Vice President, Legal and Compliance, BSE, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated April 13, 2004 (“Amendment No. 1”). Amendment No. 1 superceded and replaced the original filing in its entirety.

attending all such executive sessions and the Chairman from attending such executive sessions relating to personnel or compensation issues of the Chairman.

This order approves the proposed rule change, as amended; grants accelerated approval to Amendment No. 1; and solicits comments from interested persons on Amendment No. 1.

## **II. Description of Proposed Rule Change**

The BSE proposes to amend its Constitution to permit the separation of the Chairman and CEO positions. The separation would not be mandatory but, according to the Exchange, would be an option to be utilized by the Exchange's Board as deemed necessary and/or prudent to enhance the governance of the Exchange. The Exchange proposes the flexibility to separate the Chairman and CEO positions in the event the BSE's Board determines such a separation to be practical, in light of current or external events. The Exchange represents that any such separation also would allow for the independence of the Exchange's regulatory function from its marketplace function.<sup>5</sup>

To implement the possible separation of the two roles, the proposed changes to the BSE's Constitution would delineate the duties and functions of the Chairman and of the CEO in the event two individuals or the same individual should hold these positions. If the Chairman and CEO are not the same person, then according to the proposed revisions to the Constitution, the Chairman, as an executive officer of the Exchange, among other duties, would: (1) preside over all meetings of the Board; (2) be responsible to the Board for the management of the BSE's regulatory affairs; (3)

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<sup>5</sup> The Exchange noted in its filing that it did not submit this proposal in response to any internal issues arising from its current governance structure. Rather, the Exchange stated that it sought to be proactive in concert with changes occurring in the control mechanisms of other market centers, particularly the New York Stock Exchange ("NYSE"). The Exchange noted that it was not implementing all of the changes recently put in place by the NYSE because the Exchange's size would make such a governance structure unwieldy and unworkable.

be responsible for management of the regulatory affairs of all exchange facilities, subsidiaries, or other legal entities to which the Exchange is a party; and (4) act as Board liaison to the Exchange's CEO and management.<sup>6</sup> Similarly, if the Chairman and CEO positions are held by different individuals, then the CEO, among other duties, would: (1) be responsible for the management and administration of the affairs of the Exchange's marketplace functions; (2) not participate in executive sessions of the Board; and (3) be subject to the authority of the Board.

If the Chairman and CEO are the same person, the proposal provides that the combined Chairman/CEO, among other duties, would: (1) preside over all meetings of the Board; (2) be responsible to the Board for the management of the BSE's regulatory affairs; (3) be responsible for the management of the regulatory affairs of all Exchange facilities, subsidiaries, or other legal entities to which the Exchange is a party; (4) be responsible for the management and administration of the affairs of the Exchange's marketplace functions; and (5) be subject to the authority of the Board.

To further separate the CEO role from the regulatory functions of the Exchange, the Exchange also proposes that if a single individual serves as both the Chairman and CEO, the Board must designate a lead director to preside over executive sessions of the Board. The Chairman/CEO would not be permitted to participate in executive sessions of the Board. In addition, the Board would publicly disclose the lead director's name and a means by which interested parties may communicate with the lead director.

The Exchange further proposes to clarify when an executive session of the Board would

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<sup>6</sup> The Exchange also proposes a Constitutional provision to clarify that the general powers of the Board also would include the administration of the regulatory function of the Exchange. Thus, while the person serving in the capacity of Chairman or Chairman/CEO would be responsible for the management of the Exchange's regulatory affairs, the Exchange's Board would continue to have ultimate oversight responsibility for the Exchange's regulatory functions.

be called. The Exchange proposes to add a provision to the Constitution noting that the Board will have the power to determine when to conduct proceedings in executive session, and that executive session proceedings will be commenced for matters involving the regulation of the Exchange, the compensation of the Chairman, Exchange staff personnel matters, or any other matter that the Board determines to require confidential and sensitive treatment. The proposal requires that the Chairman recuse himself from any executive session proceedings involving personnel or compensation issues of the Chairman. Additionally, the CEO would not be permitted to attend any executive sessions of the Board.

### **III. Discussion**

The Commission has reviewed carefully the proposed rule change, as amended, and finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange and, in particular, the requirements of Section 6(b) of the Act.<sup>7</sup> Specifically, the Commission finds that the proposed rule change, as amended, is consistent with Section 6(b)(1) of the Act,<sup>8</sup> which requires that the exchange be “so organized and [have] the capacity to carry out the purposes of [the Act].” The Commission also finds that the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act<sup>9</sup> in that it is designed, among other things 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.

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<sup>7</sup> 15 U.S.C. 78f.

<sup>8</sup> 15 U.S.C. 78f(b)(1).

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

In the Commission's view, the Exchange has taken an initial step toward strengthening its governance structure by providing itself with the flexibility to separate the functions of Chairman and CEO.<sup>10</sup> According to the Exchange, any such separation would allow for greater independence of the Exchange's regulatory function from its marketplace function. Although the Exchange has retained the ability to have the functions of Chairman and CEO reside in a single individual, the Commission notes that the Exchange's proposal has incorporated several features that are designed to help protect the integrity of the Exchange's regulatory function.

The Commission notes that the proposal sets forth the respective duties of the Chairman and the CEO in the event two individuals hold these positions. In this situation, the Exchange's proposal clarifies that the Chairman is responsible for the management of the BSE's regulatory function, while the CEO is responsible for the management and administration of the Exchange's marketplace function. In the Commission's view, the proposed rule change is designed to help improve the governance structure of the Exchange by ensuring that the Exchange's regulatory function is cordoned off from management of the marketplace function when two individuals hold the positions of Chairman and CEO.

In addition, the Exchange proposes to implement other revisions to its Constitution that are designed to reduce any potential conflicts of interest between its regulatory responsibilities and its marketplace functions, in the event a single individual holds the positions of Chairman and CEO. In this case, the Chairman/CEO would not be permitted to participate in Board executive sessions and a lead director would be appointed to preside over such sessions. Moreover, the Board must disclose the lead director's name and a means by which interested

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<sup>10</sup> The Commission is in the process of reviewing a range of governance issues relating to self-regulatory organizations ("SROs") and, depending on the results of that review, may determine further steps designed to strengthen the governance of SROs are necessary.

parties may communicate with the lead director. The proposed changes to the Constitution would require executive sessions to be commenced for matters involving the regulation of the Exchange, the compensation of the Chairman, Exchange staff personnel matters, or any other matter that the Board determines requires confidential and sensitive treatment. The Chairman would be recused from sessions involving personnel or compensation issues relating to the Chairman. The Commission believes that these additional safeguards proposed by the Exchange are designed to further the goal of independence of the Exchange's regulatory duties from its business functions.

In light of the foregoing reasons, the Commission finds that the proposed rule change, as amended, is consistent with the Act.<sup>11</sup>

#### **IV. Accelerated Approval of Amendment No. 1**

The Commission finds good cause for approving Amendment No. 1 prior to the thirtieth day after the date of publication of notice of filing thereof in the Federal Register.

Amendment No. 1 clarifies the proposed changes to the BSE's Constitution by setting forth expressly the duties of the Chairman and the CEO in the instances when those positions are held by the same individual or by two individuals. In addition, Amendment No. 1 incorporates provisions relating to executive sessions of the Board and specified that when the same individual serves as both Chairman and CEO, a lead director must be designated to preside over such sessions. Amendment No. 1 also specifies the kinds of matters, i.e., the regulation of the Exchange, the compensation of the Chairman, Exchange staff personnel matters, or any other matter that the Board determines to require confidential and sensitive treatment, for which the Board must commence executive session proceedings. The proposed revisions in Amendment

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<sup>11</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

No. 1 were made for the purposes of clarifying the duties of Chairman and CEO, whether the same individual or two individuals hold those positions, and for clarifying the separation between the Exchange's regulatory and market functions. Amendment No. 1 raises no new issues.

Accordingly, the Commission finds good cause, consistent with Sections 6(b)(1),<sup>12</sup> 6(b)(5)<sup>13</sup> and 19(b)(2)<sup>14</sup> of the Act, to accelerate approval of Amendment No. 1 to the proposed rule change.

#### **V. Solicitation of Comments**

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether Amendment No. 1 is consistent with the Act. 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 E-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-BSE-2004-10 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

All submissions should refer to File Number SR-BSE-2004-10. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your

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<sup>12</sup> 15 U.S.C. 78f(b)(1).

<sup>13</sup> 15 U.S.C. 78f(b)(5).

<sup>14</sup> 15 U.S.C. 78s(b)(2).

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 inspection and copying in the Commission's Public Reference Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of the BSE. 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-BSE-2004-10 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

## **VI. Conclusion**

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>15</sup> that the proposed rule change (SR-BSE-2004-10) be, and it hereby is, approved, and that Amendment No. 1 to the proposed rule change be, and hereby is, approved on an accelerated basis.

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

Margaret H. McFarland  
Deputy Secretary

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

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