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**Re: Shareholder Approval Requirement for Equity Compensation Plans**

Dear Clients and Other Friends:

Effective June 30, 2003 the Securities and Exchange Commission approved new listing standards for the New York Stock Exchange ("NYSE") and the NASDAQ Stock Market ("NASDAQ"). The new standards require that shareholders approve equity compensation plans and any materials amendments to such plans. Newspapers have reviewed the new standards, but this letter discusses some of the important details.

**Plans subject to voting requirement.** The new NYSE standard requires shareholders to approve all "equity compensation plans" (including individual grants not made under a formal plan) that provide for the delivery of equity securities (whether newly issued or treasury shares) to any employee, director, or service provider as compensation for services. The following equity plans will not require shareholder approval under the NYSE standard if they are approved by a Company's independent compensation committee or a majority of the Company's independent directors[1]:

- Equity grants made to induce a person to become an employee of the Company.

- Employee benefits plans qualified under § 401(a) of the Internal Revenue Code and employee stock purchase plans intended to qualify under Code § 423.

- So-called "parallel excess plans" that provide benefits which cannot be provided under tax qualified plans due to certain limits under the Internal Revenue Code.

- Conversion or adjustment of outstanding options or awards to reflect a corporate acquisition or merger and post acquisition grants to target company employees from a plan previously approved by target company.

The new NASDAQ standard requires shareholders to approve new stock option or purchase plans and other equity compensation arrangements under which equity securities may be issued to officers, directors, employees, or consultants. The NASDAQ standard also requires

[1] The effect may be to require board level consideration of plans and plan amendments that were not considered board level issues in the past.

shareholders to approve individual equity compensation arrangements made outside of a formal plan. Plans covering warrants or rights issued to all shareholders generally or stock purchase plans available on terms equal to all shareholders (such as dividend reinvestment plans) do not require shareholder approval.

The new NASDAQ standard contains exemptions similar to those of the NYSE, provided however, the exemption for new employee awards is not available to former directors of the company. The NASDAQ exemptions for broad based plans and deminimus awards (the lesser of 1% of the outstanding shares or 25,000 shares) have been eliminated.

**Material Amendments.** Both NYSE and NASDAQ now require shareholder approval of "material amendments" or revisions to an equity compensation plan. Material amendments include a material increase in the number of shares available for issuance and expansion of the types of awards available under a Plan, and a material expansion of the eligible participants.

**Stock Option Repricings.** Both NYSE and NASDAQ significantly limit stock option repricings. The NYSE standard provides that any deletion or limitation of a plan provision prohibiting repricing will be considered a material amendment requiring shareholder approval. Further, the NYSE standard provides that plans that do not explicitly allow for repricings will be deemed to prohibit them. The new NASDAQ standard provides that any material increase in benefits to participants, including any material change to permit a repricing of outstanding options will be considered a material amendment requiring shareholder approval.

**Transition Rules.** Most existing equity compensation plans adopted before June 30, 2003 may continue to operate as previously established. However, the NYSE standard has a transition period for so-called formula plans and discretionary plans. Formula plans are plans that provide for automatic increases in the number of shares that can be issued under them (sometimes referred to as "evergreen" plans) or plans that provide for automatic grants under a formula. Discretionary plans are plans with no specific limit on the number of shares that can be issued under them, whether or not such plans have previously been approved by shareholders.

With respect to formula plans, if they either have not been approved by shareholders or have a term of more than ten years, companies can make additional grants without shareholder approval until the earliest of June 30, 2004; the Company's next shareholder's meeting at which directors are elected on or after December 27, 2003; or the plan expiration date.

With respect to discretionary plans, regardless of earlier shareholder approval, additional grants may be made without further shareholder approval only in a manner consistent with past practice and only for the transition period described in the preceding paragraph.

**Discretionary Broker Voting Eliminated.** NYSE rules were also changed to prohibit brokers from giving a proxy to vote on equity compensation plans unless the beneficial owner of the shares has given specific voting instructions. In the past, brokers have given proxies on so-called "uninstructed" shares, but under the revised rule, brokers may no longer do so with respect to a vote on an equity compensation matter. This change is effective for any meeting of shareholders held on or after September 28, 2003. NASDAQ rules already prohibit discretionary

voting by brokers without the beneficial owner's explicit instructions. Commentators believe that this NYSE rule change may dramatically alter the dynamics of the stock plan approval process, shifting voting power to institutional shareholders that tend to always vote their shares.

These new listing standards are significant. Companies will want to review their existing equity compensation plans for compliance, particularly with respect to the transition rules. Also, new proxy voting strategies may have to be implemented to deal with the elimination of broker voting of "uninstructed" shares on equity compensation proposals.

Please call us with any questions.

Very truly yours,

Jule M. Hannaford IV

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