

MEMORANDUM

TO: Our Clients and Friends

FROM: Godfrey & Kahn, S.C.

DATE: April 24, 2003

RE: SEC Final Rules Relating to Listed Company Audit Committees

As mandated by the Sarbanes-Oxley Act of 2002, the SEC recently adopted rules directing the self-regulatory organizations (SROs) to prohibit the listing of any security of a company that is not in compliance with the audit committee requirements established by Sarbanes-Oxley. The SROs must adopt final listing standards implementing these requirements no later than December 1, 2003.

Listing Requirements

Sarbanes-Oxley required the SEC to direct the SROs (NYSE, Nasdaq, and AMEX, among others) to prohibit the listing of any security of an issuer that is not in compliance with several enumerated standards regarding audit committees. In accordance with Sarbanes-Oxley, new Rule 10A-3 under the Securities Exchange Act of 1934 provides that the SROs will be prohibited from listing any security of a company that is not in compliance with the following standards:

- All audit committee members must be “independent,” meaning:
 - an audit committee member may not accept, directly or indirectly, any consulting, advisory or other compensatory fee from the company or any subsidiary other than in his or her capacity as a member of the board of directors or any board committee, and

- an audit committee member may not be an “affiliated person” of the company or any subsidiary, apart from being a member of the board or any board committee. “Affiliated person” is defined consistent with other securities law definitions to mean “a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with,” the company. The rule includes a safe harbor from the definition of “affiliated person” which provides that a person who is not an executive officer or 10% shareholder will be deemed not to control the company;
- The audit committee must be directly responsible for the appointment, compensation, retention and oversight of the independent auditor, which must report directly to the audit committee;
- The audit committee must establish formal procedures for the receipt, retention, and treatment of complaints received by the company regarding accounting, internal accounting controls, or auditing matters, including procedures for the confidential, anonymous submission by employees of concerns regarding questionable accounting or audit matters;
- The audit committee must have the authority to engage independent counsel and other advisors, as it determines necessary to carry out its duties; and
- The company must provide for appropriate funding, as determined by the audit committee, for payment of (1) compensation to any registered public accounting firm for preparing or issuing an audit report or performing other audit, review or attest services for the company, (2) compensation to any advisers employed by the audit committee and (3) ordinary administrative expenses of the audit committee that are necessary or appropriate in carrying out its duties.

Disclosure Changes

The SEC also adopted changes to the current disclosure requirements related to audit committees, as follows:

- Companies that rely on any of the independence exemptions provided in Rule 10A-3 must disclose their reliance on the exemption and their assessment of whether, and if so, how, such reliance will materially adversely affect the ability of the audit committee to act independently and to satisfy its required duties. This disclosure must be included in the proxy statement and included or incorporated by reference in the Form 10-K.
- The names of the members of the audit committee must be included or incorporated by reference in the Form 10-K.

- Because all SROs will need to have independence standards under the new rules, existing proxy statement disclosure regarding the independence of audit committee members has been updated to reflect the new SRO rules.

Implementation and Effectiveness

The SROs must now propose listing standards that comply with the final SEC rules, and then the SEC must approve those listing standards. The SROs must submit proposed listing standards no later than July 15, 2003. The SEC must approve final listing standards that comply with the requirements of new Exchange Act Rule 10A-3 no later than December 1, 2003.

Subject to certain exceptions for foreign companies and small business issuers, listed companies must be in compliance with the new listing standards by the earlier of (1) their first annual shareholders meeting after January 15, 2004 or (2) October 31, 2004.

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We will continue to monitor the SROs as they propose new listing standards and will keep you apprised of any developments. In the meantime, please do not hesitate to contact us if you have any questions.

Godfrey & Kahn Securities Team

Kenneth C. Hunt, kchunt@gklaw.com
Christopher B. Noyes, cbnoyes@gklaw.com
Larry D. Lieberman, llieber@gklaw.com
Pamela M. Krill, pmkrill@gklaw.com
Dennis F. Connolly, dconnoll@gklaw.com

Ellen Drought, edrought@gklaw.com
Michelle M. Nelson, mnelson@gklaw.com
Jake C. Blavat, jblavat@gklaw.com
C.J. Wauters, cwauters@gklaw.com

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