American Stock Exchange Inc.
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Arthur Levitt Jr.
Chairman of the Board

December 21, 1979

The Honorable Harold Williams
Chairman
Securities and Exchange Commission
500 North Capitol Street
Washington, D.C. 20549

Dear Harold:

Knowing of your interest in and concern with the mechanisms of corporate governance, I am pleased to inform you that the Exchange Board of Governors has adopted a recommendation that all Amex listed companies establish audit committees composed of independent directors. In taking this action, I believe the Exchange Board has struck a useful balance between the problems of smaller issuers and the need to strengthen corporate accountability.

The Board's action arose out of its consideration of the recommendations of the Special Advisory Committee on Audit Committees, which was appointed by the Board in November, 1978 to study and formulate recommendations as to whether the Exchange should require all or some of its listed companies to establish audit committees.

The Committee, composed of accountants, lawyers and chief executive officers of listed companies and chaired by Arthur M. Borden, Esq., undertook a comprehensive study of the audit committee question. The Committee studied the available literature on the subject of audit committees, the work of the AICPA, and the experience of the New York Stock Exchange with its audit committee rule. The Committee also considered the relationship of the Amex with its listed companies, its members and the public. In this connection, the Committee solicited the views of listed companies on a variety of issues related to audit committees. The results of that survey were consistent with earlier surveys, which showed that approximately three-quarters of Amex companies have audit committees; that somewhat less than that number are composed solely of independent directors; and that a large number of Amex companies oppose an exchange audit committee requirement, although they favor audit committees generally.

The Committee's report, which was presented to the Board in September, 1979, recommended that the Board adopt a rule requiring all listed companies to establish audit committees composed of a majority of independent directors. The Committee also recommended that the Exchange administration retain authority to grant exemptions from the requirement in cases of hardship or where the protections which an audit committee would confer are in fact provided to a company. The exemptive provisions, and the ability of affiliated directors to serve on audit committees, were recommended by the Committee as a means of alleviating the problems smaller companies may have in establishing audit committees.

While the Exchange Board of Governors strongly supports the concept of audit committees and believes that listed companies should be encouraged to establish them, it found certain aspects of the Committee's proposal troublesome. The Board expressed reservations with respect to a requirement that would mean further intrusion by regulatory organizations into the internal management of listed companies and furthermore, it expressed concern that, in the absence of a similar requirement for over-the-counter companies, an audit committee requirement might place the Exchange at a substantial competitive disadvantage in its ability to attract new listings.

The Board also believes that, while an audit committee that included members of management might have a "cosmetic" value, it would not really be meaningful, since a principal function of an audit committee is to monitor the activities of management. It is also felt that, if an audit committee is to be truly effective, it would not include any persons whose affiliations with the company as major suppliers, customers, or providers of services, might interfere with the exercise of their independent judgment as members of the audit committee.

In view of these concerns the Board believed it appropriate at the present time to strongly recommend, but not require, that any listed company which does not already have an audit committee composed entirely of independent directors establish such a committee. The Exchange will retain its present definition of "independent director," (i.e., a director who is not an officer of the company, and who is neither related to its officers nor represents concentrated or family holdings) except that it would add a provision that an "independent director" would be a person who, in the view of the company's board of directors, is free of any relationship that would interfere with the exercise of independent judgment.

The Board noted the almost total compliance that has been achieved with the Exchange's longstanding recommendation that listed companies have at least two outside directors as precedent for a recommendation in this case.

The Board has directed the Exchange administration to continue to review the audit committee question in light of the experience gained with the above recommendation, and to report to the Board within a year on its effect and the need, if any, for further action.

The rule change will be submitted to the Commission on Form 19b-4 shortly.

With kindest personal regards.

Sincerely,