Jack Ehnes
Chief Executive Officer

CALSTRS
HOW WILL YOU SPEND YOUR FUTURE?

California State Teachers'
Retirement System
7667 Folsom Boulevard
Post Office Box 15275
Sacramento, CA 95851-0275

916.229.3706 Tel
www.calstrs.com

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Special Committee on Governance
New York Stock Exchange, Inc.
11 Wall Street
New York, NY 10005

Dear Mr. McCall and Mr. Panetta:

This letter is sent to you on behalf of the California State Teachers' Retirement System (CalSTRS). CalSTRS is a public pension fund, established for the benefit of California's public school teachers 90 years ago. As of our fiscal year-end June 30, 2003, the fund's assets totaled $100.2 billion. The portfolio's exposure to the New York Stock Exchange (the Exchange) companies represented $32.2 billion, or approximately 80 percent of our domestic equity exposure.

As you are aware, the last several years have been trying for investors; during this time the usual pillars of the investment process have been examined and, in some cases, altered. We believe that the recent revelations regarding the operation and process of the Exchange's compensation committee in the matter of its senior personnel have opened the investment community up to new criticism and skepticism by the investing public. In light of this, we believe that improvements are needed in the Exchange's governance structure in order to give both the fact and the appearance of alignment of interest between the Exchange and the investing public. The recommendations below focus on reform of the Exchange's current level of board independence, committee structure, regulatory responsibilities and transparency:

Recommendation 1: **Align regulator's interest with investor's interest.** Having a regulatory body that is owned and controlled by the very entities it regulates creates a conflict with investor interest. While we realize that the Exchange is a hybrid of a business and a regulator, we believe separation of the two functions will keep the regulator's interest on investors, and allow the business of the Exchange to be conducted without a need for the delicate balancing of interest that must now occur. It is our recommendation that the regulatory function of the exchange be separated from the business aspect.

Recommendation 2: Require a majority of independent directors. The apparent lack of independence in the Exchange's board runs contrary to current governance standards. We recommend that a majority of independent directors constitute the board; this is the same standard to which the Exchange's own companies adhere and one that the investing public understands and accepts. In order for a director to be designated as an independent director, that director must not come from the ranks of the listed or member firms or from those entities with close affiliations with the Exchange.

Recommendation 3: Set a gold standard for disclosure. The Exchange should serve as the model for openness and transparency. Our suggestions regarding how to improve transparency include, but are not limited to, disclosure of charitable contributions on behalf of indicated members and staff, and disclosure that details the composition, function and processes of key committees, such as the Nominating and Compensation committees. We believe that it is important that the key committees issue an annual report to the public on how well they functioned and executed their duties. We also believe that the Exchange should have a committee of directors who are responsible for succession planning regarding the executive management of the Exchange.

Recommendation 4: Reduce the potential conflicts of interest from cross-directorship on a board. Establish a policy to protect investors by reducing or eliminating cross-directorships and create a Compensation Committee free of interlocks by limiting it to independent directors. A scan of the directorship shows an unusually high number of directors serving on multiple boards in a reciprocal capacity. Not only does this create a barrier to good governance, but it also fosters the image of an insiders' club that is owned and controlled by the very entities it regulates.

Recommendation 5: Establish independent Nominating and Compensation committees. These key committees should be composed entirely of directors who meet the Exchange's definition of independence. We applaud the Exchange's recent decision to appoint and formally name a lead director to guide it through its current difficulties. We believe that this practice should be formally established as part of the governance structure of the Exchange.

Recommendation 6: Separate chairman and chief executive officer. We believe that the chairman of the board and the chief executive officer (CEO) should be two distinct positions, held by separate individuals. Had such a structure been in place during the most recent CEO's tenure, perhaps questions would have come from the Exchange's own governing body, rather than the distracting public inquiry.

Recommendation 7: Annually elect and evaluate directors. The board of directors should be elected annually, rather than on a staggered basis. An essential part of the election process should be an annual evaluation of the directors and board. The board's evaluation should pay close attention to the tenure, the attendance and participation of all the board members, and the governance profiles of the companies that the sitting board members represent.

Recommendation 8: Reduce size of the board. The size of the board should be reduced to a range of between five and 11 members, which we believe would greatly increase its overall effectiveness and accountability.

We would appreciate working closely with you to further refine these ideas. As a large institutional investor, CalSTRS has a vested interest in the success and image of the Exchange. The recent scandals within corporate America and investing challenges in the deep bear markets have deteriorated investor confidence in the U.S. equity markets. Our combined goal should be to restore that confidence through meaningful, profound improvements to show all investors that we are serious about our efforts to make this a level playing field for all.

We would like to join with you to improve the functioning of the Exchange for the benefit of our members and all investors.

Sincerely,

Jack Ehnes

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Chief Executive Officer

cc: William Donaldson, Chairperson
Securities and Exchange Commission