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Vanessa Countryman
Secretary
United States Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Executive Compensation Roundtable
Comment Letter

Dear Ms. Countryman:

We welcome Chairman Atkins’s invitation to submit comments regarding the current disclosure regime applicable to executive compensation and the upcoming “Executive Compensation Roundtable” that the Securities and Exchange Commission (the “Commission”) will hold to discuss these matters. We believe that while the current disclosure regime provides useful information to investors and is well intentioned, there are certain areas where the rules may be unduly complex and costly and can be improved. In this letter, we discuss certain specific areas where we believe the rules should be re-examined and potentially revised. We are pleased to contribute to this important project and, again, applaud the Commission’s endeavor to revisit this area to strike the right balance between providing material, useful and easily understood information for investors and appropriately considering the compliance burdens for public issuers and companies considering new listings.

1. Reported Value of Granted Equity Awards

The Summary Compensation Table is the “linchpin” of the Item 402 disclosure regime.¹ In the words of the original Item 402 adopting release, the Summary Compensation Table was meant to provide “an easily understood overview of executive compensation in a single location

¹ Executive Compensation Disclosure, Release No. 33-6962 (Oct. 16, 1992).

within the proxy or information statement”.² The table as originally conceived required issuers to show the amount of salary and bonuses earned during the year, the value of “other compensation” received by the executive and information about equity and long-term incentive awards received by the executive, in certain cases based on the number of shares received and in others based on the value of the award. Under the rules initially adopted in 1992, issuers were not required to present a sum “total” of the compensation for the year. As reflected in Alan Beller’s famous “all means all” speech in 2004, the original framework was not ultimately satisfactory to the Commission or to investors³, but one of the reasons a dollar total was not required may have been that equity awards and long-term incentives were not all shown as dollar figures (but rather as a number of shares) and also because the valuation of those awards with respect to a particular year is not a straightforward exercise and any valuation prior to actual payment is merely an estimate given inherent price fluctuations.

Following the Commission’s 2006 amendments to Item 402, issuers were required to present a sum “total” of the compensation for a particular year. Significantly, that required the specification of a methodology for valuing equity awards. The 2006 rules, which still apply today, required that the *full grant date fair value* of an award granted within the year (as measured for financial accounting purposes) be shown as compensation for the year of grant. For example, the entire grant date fair value of an award granted in 2025 must be included in compensation for 2025, regardless of the conditions to actual vesting of the award, which may not be met until several years in the future (if ever).

As a result, the “total” figure that is presented to investors represents an aggregation of certain types of compensation that were actually earned and received in cash in the relevant year and other types of compensation that were not earned in the relevant year but may be earned in the future or, in some cases, may never be earned at all. Furthermore, since these awards are in the form of equity, which by nature fluctuates in value, the actual value received by an executive may be more or less (in some cases by significant amounts) than the amounts shown as compensation in the year of grant.

The “front loaded” reporting of equity awards is consistently confusing to, and misunderstood by, external audiences. The financial media frequently uses the Summary Compensation Table “total” figure to report on “amounts paid to” or “amounts earned by” executives without explanation of the fact that a significant portion of the amounts (equity being the largest component of many executives’ and almost all CEOs’ pay) may not be earned for several years or at all and will likely have a far different ultimate value than reported.

We suggest that the Commission revisit the current requirement that equity awards be reported based on their full grant date fair value in the year of grant. An alternative approach may include valuing awards at their actual value at the time of vesting. This approach would harmonize the most significant columns of the Summary Compensation Table with amounts shown representing the true economic value of the relevant compensation at the time received. It could also lead to an overall simplification of the tabular disclosures by eliminating, at least in part, the need for the separate “Option Exercises and Stock Vested” table required by Item 402(g). Another potential approach could be to spread the reported value of awards over the vesting period of the award to more accurately portray the value attributable to specific

² *Id.*

³ SEC Speech: Remarks Before Conference of the NASPP, the Corporate Counsel and the Corporate Executive: Oct. 20, 2004 (Alan L. Beller).

service periods. This may also more accurately reflect the manner in which the awards are reflected for financial statement reporting purposes.

2. Reported Value of Modified Equity Awards

Similar to the issue discussed above, the Summary Compensation Table rules require that the full “incremental value” of stock options or stock appreciation rights that have been modified in the relevant year be shown as compensation. This is true even though the original award may have already been shown as compensation under the principle discussed above. Again, the “incremental value” of the modified award shown in the Summary Compensation Table covering the period of the modification is entirely unrelated to the timing of an executive’s receipt of value from an award or its ultimate value. As a result, the Summary Compensation Table is again mixing the cash value of compensation when received (as is the case for salary and bonuses) with a financial statement measurement of the hypothetical value of equity awards. Because of this approach, external audiences are often confused and believe that the incremental value reflects true economic value received by the executive. This issue could be mitigated by one or more of the approaches to equity valuation discussed above.

3. Harmonizing Certain Outdated Instructions Relating to Options/SARs and Full Value Awards

The current version of Item 402 was adopted at a time when stock options and stock appreciation rights were the predominant form of equity compensation. Understandably, certain instructions in the rules are limited by their terms to those types of instruments. For example, the rule regarding reporting the value of award modification is set out below:

Instruction 2 to Item 402(c)(2)(v) and (vi). If at any time during the last completed fiscal year, the registrant has adjusted or amended the exercise price of options or SARs previously awarded to a named executive officer, whether through amendment, cancellation or replacement grants, or any other means (“repriced”), or otherwise has materially modified such awards, the registrant shall include, as awards required to be reported in column (f), the incremental fair value, computed as of the repricing or modification date in accordance with FASB ASC Topic 718, with respect to that repriced or modified award.

The rule by its terms only requires information as to modifications of “options and stock appreciation rights”, but practitioner practice is generally to apply this rule to all forms of equity awards. Given that stock options and SARs no longer represent the predominant form of equity compensation in many cases (as opposed to restricted stock units and similar instruments), it would be beneficial if the Commission could clarify whether or not rules that apply to stock options and SARs are applicable to other forms of awards and amend and clarify the instructions accordingly. This type of revision would clarify application of relevant rules and ensure consistent application.

4. Determination of Equity Award Grant Date

The valuation of an equity award and certain elements of disclosure in the compensation tables called for by Item 402 depend on a determination of the “grant date” of the award. It would be logical for investors to believe that the grant date is the date that an executive is awarded a particular incentive; however, Item 402 again ties the determination of the grant date to the specific financial accounting requirements of FASB ASC Topic 718. The accounting rules

require that all material terms and conditions of an award be determined before an award is considered granted for financial accounting purposes. Item 402's reliance on ASC Topic 718 rules can result in cases where an award has been granted in legal form but is not considered granted for accounting purposes. This can be the case, for example, when an equity award has been granted subject to shareholder approval or performance conditions that have not yet been finalized. In such a case, the award may be held by an executive but not yet considered granted for financial statement purposes. We would suggest that this result may be unintentional and that the Commission consider decoupling the determination of grant date for Item 402 purposes from the separate financial accounting rules.

5. Disclosure of Termination Scenarios that Can Never Actually Occur

Item 402(j) requires detailed disclosure of information as to the termination-related benefits that may be payable to named executive officers upon various termination events if a termination had occurred at the end of the relevant year. In certain cases, the executive for whom this disclosure is required may have retired or otherwise separated from employment by the time the proxy statement is filed. The rules nevertheless require detailed disclosure of hypothetical termination benefits. There is guidance from the Commission that provides relief in this scenario, but it is very limited.⁴ We suggest that the Commission clarify that in the event that a named executive officer has departed by the time of the filing of this information (whether before or after the end of the fiscal year), disclosure under Item 402(j) is limited to disclosure regarding the termination event that actually occurred, and that disclosure of other hypothetical scenarios that can no longer occur and are not relevant to investors is no longer required.

6. Simplifying Required Historical Compensation Information for Initial Public Offerings and Spin-Off Transactions

Capital market participants frequently discuss the perceived need to simplify the registration process for companies that are candidates for a new listing (most commonly initial public offerings or spin-off transactions). While this would be a larger project, streamlining the disclosure requirements relative to executive compensation could aid in that overall simplification endeavor.

Under the current rules, new registrants are required to provide anywhere from zero to three years of historical compensation information in the assorted executive compensation tables (depending, in part, on whether the registrant has been operated as a standalone business).⁵ There are several issues with this approach. First, there is a disparate requirement among issuers entering our capital markets for the first time (some are required to present three years of information and others are required to present none). Second, historical compensation information will usually have little to no relevance to the issuer's future life as a public company because public companies typically have inherently different compensation programs, which in any event will be established by the issuer's new board of directors and/or compensation committee. Third, companies often retain new management in the context of initial public offerings and/or spin-offs, so historical information is sometimes presented for individuals who will not serve the new registrant.

⁴ Compliance and Disclosure Interpretation 226.02 (Aug. 8, 2007).

⁵ Compliance and Disclosure Interpretation 217.03 (Jan. 24, 2007).

Relatedly, because under current rules compensation information must be refreshed at the beginning of each calendar year, there is often a practical delay in the finalization of registration statements when a transaction straddles a calendar year until compensation outcomes are finalized for the prior year (for example, board determination of annual bonuses for the prior year). This is different from the timeline applicable to existing registrants who are afforded a grace period (generally until April 30) before compensation information for the prior year is required to be publicly disclosed.

We suggest that the Commission consider streamlining and harmonizing these rules such that new registrants are required either to present only qualitative information as to their future compensation program or to provide only one year of historical information in the Summary Compensation Table in all circumstances. The Commission should also consider whether issuers filing a registration statement early in a calendar year should be afforded a grace period before the compensation information in the registration statement is required to be refreshed.

7. Forward Disclosure of Performance Metrics

It is common for issuers to grant incentive awards subject to performance-based metrics. As a timing matter, issuers are sometimes reluctant to disclose the future performance measures relevant to an award at the time it is granted out of concern that such disclosure would disclose proprietary or confidential business information. Instruction 4 to Item 402(b) provides limited relief in these situations if the issuer can meet a relatively high standard for withholding such information under standards applicable for other purposes.

Registrants are not required to disclose target levels with respect to specific quantitative or qualitative performance-related factors considered by the compensation committee or the board of directors, or any other factors or criteria involving confidential trade secrets or confidential commercial or financial information, the disclosure of which would result in competitive harm for the registrant. The standard to use when determining whether disclosure would cause competitive harm for the registrant is the same standard that would apply when a registrant requests confidential treatment of confidential trade secrets or confidential commercial or financial information pursuant to Securities Act Rule 406 (17 CFR 230.406) and Exchange Act Rule 24b-2 (17 CFR 240.24b-2), each of which incorporates the criteria for non-disclosure when relying upon Exemption 4 of the Freedom of Information Act (5 U.S.C. 552(b)(4)).

The standard that must be satisfied to withhold performance-related metrics is not well understood or consistently applied. It is our experience that it has become commonplace for issuers to withhold disclosure of performance-related measures at the outset of any award and to disclose them only for the time period when the award is earned (backward-looking disclosure rather than forward-looking disclosure). We encourage the Commission to clarify the standards under which issuers can withhold confidential business-related measures from their executive compensation disclosures and to require such disclosure only at the time that the award is actually earned.

8. Pay Versus Performance and Compensation “Actually Paid”

Section 953 of the Dodd-Frank Act required the Commission to adopt rules that clearly showed the relationship between compensation actually paid to executives and company

performance. The Commission adopted final rules under the statute in 2022. The adopted rules require issuers to recalculate and repackage the compensation information shown in the Summary Compensation Table. Most significantly, while, as discussed above, the Summary Compensation Table requires equity awards to be shown at their full grant date fair value, Item 402(v) essentially requires the issuer to mark to market the awards held by executives during multi-year vesting periods before they have vested and been paid to the executives. This approach again leads to a presentation to investors that combines certain elements of compensation that have actually been paid to executives (for example, salary and bonus compensation) with a hypothetical estimate of the current fair value of equity awards that have not yet been paid and may not be paid for some time or ever. We believe that this mix and match of information under a rule intended to present “actually paid” compensation results in confusion and is of questionable utility to investors when compared with the associated compliance burden. While we recognize that the pay versus performance rules were mandated by statute, we would encourage the Commission to revisit the rules in an effort to find a formulation that truly presents compensation actually paid to executives rather than mid-period measurement of awards that may never be received.

In addition, in the brief period that pay versus performance disclosure has been required, it has become one of the more time-consuming and resource-intensive portions of proxy statements to prepare. Furthermore, the proxy advisory firms have their own proprietary methodologies for calculating pay versus performance, so this new disclosure may not be providing a benefit to investors commensurate with the burden to investors. We encourage the Commission to seek investor input as to whether this disclosure is serving its intended goals.

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We reiterate our appreciation and support for the Commission taking on this important project and would be happy to discuss any of the areas above with members of the Commission or its staff at your convenience. Please direct any inquiries to our attention: Jonathan Katz (212-474-1538), Eric Hilfers (212-474-1352), Amanda Gold (212-474-1110) or Matthew Bobby (212-474-1128).

Sincerely,

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