Council of Institutional Investors®
The voice of corporate governance

Via E-Mail

July 18, 2019

Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: File Number S7-04-19

Dear Madam Secretary:

I am writing in response to the Securities and Exchange Commission's (SEC or Commission) invitation to comment on its semiannual regulatory agenda.[1] We respectfully reiterate our requests that the following two individual agenda items currently listed under the "Division of Corporation Finance—Long Term Actions" be advanced to "Division of Corporation Finance—Final Rule Stage:" "Universal Proxy" and "Listing Standards for Recovery of Erroneously Awarded Compensation."[2]

In addition, we respectfully request that the Commission add to its "Division of Corporation Finance—Long Term Actions" amendments to (1) Rule 10b5-1 trading plans[3] and (2) Item 402(b) of Regulation S-K to improve the information about the pay target metrics presented in the Compensation Discussion & Analysis (CD&A) section of the proxy statement.[4]

Finally, we respectfully request the Commission remove from its "Proposed Rule Stage," amendments to (1) "thresholds for shareholder proposals under Rule 14a-8"[5] and (2)

[1] Regulatory Flexibility Agenda, Securities Act Release No. 10,620, Exchange Act Release No. 85,401, Investment Adviser Act Release No. 5,207, Investment Company Act Release No. 33,428, 84 Fed. Reg. 29,784 (June 24, 2019), https://www.govinfo.gov/content/pkg/FR-2019-06-24/pdf/2019-11690.pdf.
[2] *See, e.g.*, Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Brent J. Fields, Secretary, Securities and Exchange Commission 1 (Dec. 13, 2018), https://www.cii.org/files/issues_and_advocacy/correspondence/2018/December%2013%202018%20SEC%20Reg%20Flex%20Letter.pdf ("We respectfully reiterate our prior requests that the following two individual agenda items currently listed under the "Division of Corporation Finance—Long Term Actions" be advanced to the "Division of Corporation Finance—Final Rule Stage: "Universal Proxy" and "Listing Standards for Recovery of Erroneously Awarded Compensation.").
[3] *See id.* ("In addition, we also respectfully reiterate our request that the Commission add to its 'Division of Corporation Finance—Long-Term Actions' amendments to Rule 10b5-1 trading plans.").
[4] *See, e.g.*, Press Release, Council of Institutional Investors, Leading Investor Group Petitions SEC to Require Clear Disclosure on CEO Pay Targets (Apr. 29, 2019), https://www.cii.org/nongaapdisclosure.
[5] Office of Information and Regulatory Affairs, Office of Management and Budget, Executive Office of the President, View Rule, SEC Title: Rule 14a-8 Amendments (Spring 2019), https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201904&RIN=3235-AM49.

amendments to address certain advisors' reliance on the proxy solicitation exemptions in Rule 14a-2(b).[6]

In making these requests, we are mindful of the Commission's limited resources and believe our requests, the bases for which are described in more detail below, would have a positive impact on long-term investors.

The Council of Institutional Investors ("CII") is a nonprofit, nonpartisan association of public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of approximately $4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families. Our associate members include a range of asset managers with more than $35 trillion in assets under management.[7]

Universal Proxy

CII agrees with most investors and "many panelists" at the SEC's November 15, 2018, public roundtable on the proxy process (Roundtable)[8] who recommended the SEC finalize its 2016 proposal on Universal Proxy (2016 Proposal).[9] The 2016 Proposal was generally consistent with CII's membership approved policies.[10] Those policies state:

> To facilitate the shareholder voting franchise, the opposing sides engaged in a contested election should utilize a proxy card naming all management nominees and all shareholder-proponent nominees, providing every nominee equal prominence on the proxy card.[11]

In our most recent comment letter submitted in response to the SEC's regulatory agenda, we addressed what we view as unconvincing criticisms of the 2016 Proposal raised by a few of the Roundtable panelists (December Letter).[12] Those criticisms focused largely on formatting issues in

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[6] Office of Information and Regulatory Affairs, Office of Management and Budget, Executive Office of the President, View Rule, SEC Title: Rule 14a-2(b) (Spring 2019), https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201904&RIN=3235-AM50.

[7] For more information about the Council of Institutional Investors ("CII"), including its board and members, please visit CII's website at http://www.cii.org.

[8] U.S. Securities and Exchange Commission, Spotlight on Proxy Process, November 15, 2018: Roundtable on the Proxy Process (last visited June 16, 2019), https://www.sec.gov/proxy-roundtable-2018.

[9] Adé Heyliger et al., Key Takeaways from the SEC's Proxy Process Roundtable: Is Proxy Voting Reform on the Horizon?, Weil, Gotshal & Manges LLP 2 (Nov. 20, 2018), https://www.jdsupra.com/legalnews/key-takeaways-from-the-sec-s-proxy-45650/; *see, e.g.*, U.S. Securities and Exchange Commission, Roundtable on the Proxy Process Transcript 70 (Nov. 15, 2018), https://www.sec.gov/files/proxy-round-table-transcript-111518.pdf (panelist Brian L. Schorr recommending "the use of the universal proxy . . . [to] eliminate some of the problems that we're trying to tackle today").

[10] Council of Institutional Investors, Corporate Governance Policies § 2.2 Director Elections (updated Oct. 24, 2018), https://www.cii.org/files/10_24_18_corp_gov_policies.pdf.

[11] *Id.*

[12] *See* Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors to Brent J. Fields, Secretary, Securities and Exchange Commission 3-4 (Dec. 13, 2018),

designing a universal proxy card.[13] In our view, the 2016 Proposal already fully and appropriately addresses those issues.

More specifically, in the December Letter, we detailed the 2016 Proposal's formatting requirements.[14] Those requirements include distinguishing between company and dissident nominees, listing nominees alphabetically in each group, using uniform font styles and sizes, and disclosing the maximum number of electable nominees, among other specifications.[15]

This proxy season provided an example of the benefits of a universal proxy at EQT Corporation, which was the first successfully executed use of a universal proxy for a control slate in the United States (U.S.).[16] While we believe the formatting of the cards was not in compliance with the 2016 Proposal, the ability of EQT shareholders to vote by proxy for exactly the candidates they preferred was clearly positive for shareholders and for the proxy voting process. We, however, note that for reasons explained by the SEC in the 2016 Proposal, relying on an optional system usually will not result in use of a universal proxy.[17] And even in this case, the formatting as prescribed by the Proposal would have improved the process.

CII continues to believe that the SEC should promptly[18] adopt a final rule largely consistent with the 2016 Proposal.[19] A universal proxy will facilitate better proxy voting on the most contested and consequential votes. Allowing investors to split their tickets in proxy contests serves the principle that shareholders voting by proxy should have the same voting privileges as those voting in person.[20]

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https://www.cii.org/files/issues_and_advocacy/correspondence/2018/December%2013%202018%20SEC%20Reg%20Flex%20Letter.pdf.

[13] *See, e.g.*, U.S. Securities and Exchange Commission, Roundtable on the Proxy Process Transcript at 73 (panelist David A. Katz stating: "Universal proxy can be helpful[] [b]ut the truth is really going to be depending on the details, . . . like how you designate who is on which slate and things like that, and whether it's alphabetical or other things or one side bold and -- you know.").

[14] *Id.*

[15] Universal Proxy, Exchange Act Release No. 79,164, Investment Company Act Release No. 32,339, 81 Fed. Reg. 79,122, 79,141 (proposed rule Oct. 2016), https://www.gpo.gov/fdsys/pkg/FR-2016-11-10/pdf/2016-26349.pdf.

[16] *See, e.g.*, Andrew Freedman et al., News & Resources, CLIENT ALERT: Olshan Represents Activist in First Successful Use of a Universal Proxy Card for a Control Slate in the United States, Olshan (July 2019), https://www.olshanlaw.com/resources-alerts-Olshan-Activist-FirstSuccessfulUniversalProxyCard-ControlSlate-US.html.

[17] *See* 81 Fed. Reg. at 79,170-172 (discussing mandatory vs. optional use of universal proxies).

[18] *See, e.g.*, U.S. Securities and Exchange Commission, Roundtable on the Proxy Process Transcript at 77 (panelist Bruce H. Goldfarb stating: "we need to walk and chew gum at the same time[] I think we can do multiple things . . . [a]nd on universal proxy, the SEC put out a very good proposal two years ago, and I think . . . the work has already been done[] [s]o I don't think that needs to derail anything else that's happening").

[19] *See* Letter from Ken Bertsch, Executive Director, Council of Institutional Investors to Brent J. Fields, Secretary, Securities and Exchange Commission 3 (Dec. 28, 2017) (providing extensive comments in response to the 2016 proposal and noting that "[w]ith minor enhancements, the proposed framework will provide for a constructive universal proxy regime that gives greater effect to existing shareholder rights"), https://www.cii.org/files/issues_and_advocacy/correspondence/2016/12_28_16_comment_letter_SEC_universal_proxy.pdf.

[20] *See, e.g.*, Letter from Marcie Frost, Chief Executive Officer, California Public Employees' Retirement System to Mr. Brent J. Fields, Secretary, Securities and Exchange Commission 2 (Dec. 11, 2018), https://www.sec.gov/comments/4-725/472-4765670-176812.pdf ("We have long supported a proxy voting system

Listing Standards for Recovery of Erroneously Awarded Compensation

CII continues to support prompt completed action on the SEC's required response to Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) entitled, "Recovery of Erroneously Awarded Compensation."[21] We note that Section 954 was responsive to the recommendations of the Investors' Working Group (IWG).[22]

In its seminal report on U.S. Financial Regulatory Reform, the IWG concluded:

> **Federal clawback provisions on unearned executive pay should be strengthened**. Clawback policies discourage executives from taking questionable actions that temporarily lift share prices but ultimately result in financial restatements. Senior executives should be required to return unearned bonus and incentive payments that were awarded as a result of fraudulent activity, incorrectly stated financial results or some other cause. The Sarbanes-Oxley Act of 2002 required boards to go after unearned CEO income, but the Act's language is too narrow. It applies only in cases where misconduct is proven—which occurs rarely because most cases result in settlements where charges are neither admitted nor denied—and only covers CEO and CFO compensation. Many courts, moreover, have refused to allow this provision to be enforced via private rights of action.[23]

The SEC's proposed rule to implement Section 954 (2015 Proposal) is generally consistent with CII's membership approved policies.[24] Those policies state:

> The compensation committee should ensure that sufficient and appropriate mechanisms and policies (for example, bonus banks and clawback policies) are in place to recover erroneous bonus and incentive awards paid in cash, stock or any other form of remuneration to current or former executive officers, and to prevent such awards from being paid out in the first instance. Awards can be erroneous due to acts or omissions resulting in fraud, financial results that require restatement or some other cause that the committee believes warrants withholding or recovering incentive pay. Incentive-based compensation should be subject to recovery for a period of time of at least three years following discovery of the fraud or cause

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that works without the need of physical presence to vote for the full slate of director candidates and the current proxy voting process does not provide shareowners with an efficient and cost-effective way to exercise this right.").

[21] Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. § 954 (2010), https://www.gpo.gov/fdsys/pkg/PLAW-111publ203/html/PLAW-111publ203.htm.

[22] S. Rep. No. 111-176, at 136 (Apr. 30, 2010), https://www.congress.gov/111/crpt/srpt176/CRPT-111srpt176.pdf ("The Investor's Working Group wrote 'federal clawback provisions on unearned executive pay should be strengthened.'").

[23] Report of the Investors' Working Group, U.S. Financial Regulatory Reform: The Investors' Perspective 23 (July 2009), http://www.cii.org/files/issues_and_advocacy/dodd-frank_act/07_01_09_iwg_report.pdf.

[24] Listing Standards for Recovery of Erroneously Awarded Compensation, Securities Act Release No. 9,861, Exchange Act Release No. 75,342, Investment Company Act Release No. 31,702, 80 Fed. Reg. 41,144 (proposed rule July 2015), https://www.federalregister.gov/articles/2015/07/14/2015-16613/listing-standards-for-recovery-of-erroneously-awarded-compensation.

> forming the basis for the recovery. The mechanisms and policies should be publicly disclosed.[25]

Consistent with CII policies, we believe the final SEC rule should, as proposed,[26] apply broadly to the compensation of all current or former executive officers, whether or not they had control or authority over the company's financial reporting.[27] As we explained in our comment letter to the SEC in response to the 2015 Proposal:

> In our view, establishment of a broad clawback arrangement is an essential element of a meaningful pay for performance philosophy. If executive officers are to be rewarded for "hitting their numbers"—and it turns out they failed to do so—the unearned compensation should generally be recovered notwithstanding the cause of the revision.[28]

A broad clawback can be "a powerful tool for companies seeking to punish executives for wrongdoing."[29] In addition, we agree with legal experts that broad clawback arrangements may "keep executive officers focused on sound accounting company-wide."[30]

CII believes the Commission should consider empirical studies indicating that the adoption of clawback provisions is generally associated with improved financial reporting quality, enhanced investor and auditor confidence in the quality of financial reporting, and reduced audit fees.[31] We note that one of the more recent studies indicates clawbacks generally protect accounting integrity while maintaining and even enhancing the advantages of performance based Chief Financial Officer pay.[32]

We acknowledge SEC Chairman Clayton's observation that "several companies . . . [have clawback] policies [that] go beyond what would be required under Dodd-Frank."[33] However, we

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[25] Council of Institutional Investors, Corporate Governance Policies § 5.5 Pay for Performance.
[26] *See* 80 Fed. Reg. at 41,153 ("the compensation recovery provisions of Section 10D apply without regard to an executive officer's responsibility for preparing the issuer's financial statements").
[27] *See, e.g.*, Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission 5 (Aug. 27, 2015), http://www.cii.org/files/issues_and_advocacy/correspondence/2015/08_27_15_letter_to_SEC_clawbacks.pdf.
[28] *Id*. (footnotes omitted).
[29] *See, e.g.*, Jef Feeley & Anders Melin, Hertz Seeks $70M in Clawbacks Tied to Accounting Scandal, Acct. Today, Apr. 1, 2019, https://www.accountingtoday.com/articles/hertz-seeks-70m-in-clawbacks-tied-to-accounting-scandal.
[30] *See, e.g.*, Financial CHOICE Act of 2017, Hearing Before the H. Comm. on Fin. Servs., 115th Cong. (Apr. 26, 2017) (Testimony of Michael S. Barr, The Roy F. and Jean Humphrey Proffitt Professor of Law, University of Michigan Law School at 15) (on file with CII).
[31] *See* Gregory L. Prescott & Carol E. Vann, Implications of Clawback Adoption in Executive Compensation Contracts: A Survey of Recent Research, 29 J. Corp. Acct. & Fin. 59, 67 (Jan. 2018), https://onlinelibrary.wiley.com/doi/full/10.1002/jcaf.22312.
[32] *See* Peter Kroos et al., Voluntary Clawback Adoption and the Use of Financial Measures in CFO Bonus Plans, 93(3) Acct. Rev. 213-235 (May 1, 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2312762; *see also* Ben Hiamowitz, Adoption of Clawbacks Means Stronger Link Between Firm Performance and CFO Pay, CPA PracticeAdvisor, June 7, 2018, http://www.cpapracticeadvisor.com/news/12416039/adoption-of-clawbacks-means-stronger-link-between-firm-performance-and-cfo-pay.
[33] U.S. Securities and Exchange Commission, Chairman Jay Clayton, Testimony on "Oversight of the U.S. Securities and Exchange Commission," Before the Comm. on Fin. Servs., U.S. H.R. at n.50 (June 21, 2018),

believe there are a multitude of potential benefits to long-term investors from the SEC requiring *all* companies to adopt,[34] at a minimum, clawback policies consistent with the 2015 Proposal and the Dodd Frank mandate by the U.S. Congress.

Rule 10b5-1 Trading Plans

For the benefit of both institutional and retail investors, CII continues to believe the Commission should make a priority of proposing amendments to improve Rule 10b5-1 trading plans.[35] For years, we have heard and read accounts about corporate insiders violating the spirit of the SEC's Rule 10b5-1,[36] apparently in at least some cases in efforts to provide cover for improper stock trades while possessing material non-public information.[37] *The Wall Street Journal* published a series of articles in 2012 that highlighted suspiciously fortuitous trading patterns under Rule 10b5-1 plans adopted by corporate insiders.[38] Empirical research by academics has

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https://www.sec.gov/news/testimony/testimony-oversight-us-securities-and-exchange-commission; s*ee* Proxy Process and Rules: Examining Current Practices and Potential Changes: Hearing before the S. Comm. on Banking, Hous. & Urban Affairs, 115th Cong. (Dec. 6, 2018) (statement of Michael Garland, Assistant Comptroller, for Corp. Governance and Responsible Inv., In the Office of the N.Y.C. Comptroller Scott Stringer at 8), https://www.banking.senate.gov/imo/media/doc/Garland%20Testimony%2012-6-18.pdf (indicating that the successful negotiation of a broad clawback policy at Wells Fargo "enabled the Wells Fargo Board of directors to announce in September 2016 that it would recoup $60 million from two senior executives in order to hold them financially accountable for the fake account scandal that involved the loss of jobs by 5,300 lower-level employees and cost Wells Fargo $185 million in fines and penalties"); Kathryn Neel et al., The Business Case for Clawbacks, Harv. L. Sch. F. on Corp. Governance & Fin. Reg. (May 6, 2018), https://corpgov.law.harvard.edu/2018/05/06/the-business-case-for-clawbacks/ (listing Cognizant Technology Solutions, Wells Fargo, Zions Bancorp, and eBay as companies that have adopted "detrimental conduct" clawback policies); *see also* Michael S. Melbinger, Update on Clawback Policy Issues, Executive Compensation Blog, Winston & Strawn (Oct. 19, 2017), https://www.winston.com/en/executive-compensation-blog/update-on-clawback-policy-issues.html (recommending that "directors should protect themselves and their companies by adopting a strong policy").

[34] Benjamin Gibbs et al., The State of Play on Clawbacks and Forfeitures Based on Misconduct, Pillsbury (June 12, 2019), https://www.jdsupra.com/legalnews/the-state-of-play-on-clawbacks-and-30672/ (A review of ten major Silicon Valley companies revealing the "*absence of clawbacks at Alphabet and Facebook"*).

[35] *See, e.g.*, Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Brent J. Fields, Secretary, Securities and Exchange Commission 13 (July 11, 2018), https://www.cii.org/files/July%2011%202018%20SEC%20Reg%20Flex%20Letter%20Final.pdf ("Finally, for the benefit of both institutional and retail investors, we continue to believe the Commission should make a priority of proposing amendments to improve Rule 10b5-1 trading plans.").

[36] Trading "On the Basis Of" Material Nonpublic Information in Insider Trading Cases, 17 C.F.R. § 240.10b5-1 (Aug. 2000), *available at* https://www.law.cornell.edu/cfr/text/17/240.10b5-1.

[37] *See, e.g.*, Craig M. Scheer, Rule 10b5-1 Trading Plans in the Current Environment: The Importance of Doing it Right, Bus. Law Today (Sept. 19, 2018) ("Critics have long viewed the rule as creating an opportunity for abuse, claiming that some insiders may in fact be aware of material non-public information at the time plans are established and that the rule can be used to provide cover for improper trades."), http://apps.americanbar.org/buslaw/blt/content/2013/02/article-06-scheer.shtml.

[38] Jean Eaglesham & Rob Barry, Trading Plans Under Fire, Wall. St. J., Dec. 13, 2012 ("the SEC is facing mounting pressure to tighten its rules, following a[n] . . . investigation that found profitable and well-timed trades by more than 1,400 executives"), https://www.wsj.com/articles/SB10001424127887324296604578177734024394950; Justin Lahart, Timing Is Everything for Insider Sales, Wall. St. J., Nov. 28, 2012 ("There is substantial wiggle room within 10b5-1 plans—for example, their existence doesn't have to be disclosed, and they can be canceled or changed without disclosure, as well."), https://www.wsj.com/articles/SB10001424127887324020804578147261230632772; Susan Pulliam & Rob Barry, Executives' Good Luck in Trading Own Stock, Wall. St. J., Nov. 27, 2012 (initial reporting on investigation finding that more than 1,400 executives, including some with 10b5-1 plans, had made usually beneficial trades), https://www.wsj.com/articles/SB10000872396390444100404577641463717344178; *see,*

found similar results[39] suggesting that "trades that should have resulted in insider trading liability have escaped scrutiny."[40]

In December 2012, at the recommendation and with the assistance of a prominent corporate/securities lawyer, CII submitted a rulemaking petition to the SEC recommending improvements to Rule 10b5-1.[41] Those improvements were specifically designed to limit the opportunity for executives to continue to abuse the rule and were derived, in part, from our membership approved policies.[42]

Despite our repeated requests, the common-sense improvements to Rule 10b5-1 that we first recommended in 2012 have not been adopted.[43] As a result, gaping loopholes in the rule remain that we believe will likely continue to be subject to periodic abuse through "successful manipulation of trading plans."[44]

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e.g., Cydney Posner, Blog: New House Bill to Curb Potential Abuse of 10b5-1 Plans, PubCo@Cooley (Jan. 25, 2019) (commenting that the articles "identified a number of problems with 10b5-1 plans, including the absence of public disclosure about the plan or changes to it and the absence of rules about how long the plans must be in place before trading under the plans can begin"), https://www.jdsupra.com/legalnews/blog-new-house-bill-to-curb-potential-19688/.

[39] *See* John Shon & Stanley Veliotis, Insiders' Sales Under Rule 10b5-1 Plans and Meeting or Beating Earnings Expectations, 59(9) Mgmt. Sci. iv (Sept. 2013) ("One interpretation of our results is that CEOs and CFOs who sell under these plans may be more likely to engage in strategic behavior to meet or beat expectations in an effort to maximize their proceeds from plan sales."), https://pubsonline.informs.org/doi/abs/10.1287/mnsc.1120.1669?journalCode=mnsc.; *see also* Cydney Posner ("The problem is—and of course there's a problem—that academic studies uncovered a statistical link between the timing of executive sales under Rule 10b5-1 plans and negative corporate news, finding that executives using 10b5-1 plans generated significantly better returns than other executives at the same company.").

[40] Alfred L. Fatale III & Lisa Strejlau, Analysis, The Time has Come to Address Rule 10b5-1 Trading Plans and Their Shortcomings, N.Y.L.J. (Mar. 6, 2019), https://www.law.com/newyorklawjournal/2019/03/06/the-time-has-come-to-address-rule-10b5-1-trading-plans-and-their-shortcomings/.

[41] Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors to The Honorable Elisse B. Walter, Chairman, U.S. Securities and Exchange Commission (Dec. 28, 2012), http://www.cii.org/files/issues_and_advocacy/correspondence/2012/12_28_12_cii_letter_to_sec_rule%20_10b5-1_trading_plans.pdf.

[42] *Id.* at 3 (proposed improvements include "imposing a minimum period between the adoption of a Rule 10b5-1 plan and the execution of trades pursuant to such plan, . . . restricting plan modifications and cancellations . . . [and] making boards explicitly responsible for the oversight of Rule 10b5-1 plans"); *see* Council of Institutional Investors, Corporate Governance Policies, § 5.15b Stock Sales (updated Oct. 24, 2018) ("10b5-1 program adoptions, amendments, terminations and transactions should be disclosed immediately, and boards of companies using 10b5-1 plans should: (1) adopt policies covering plan practices, (2) periodically monitor plan transactions and (3) ensure that company policies discuss plan use in the context of guidelines or requirements on equity hedging, holding and ownership."), https://www.cii.org/files/10_24_18_corp_gov_policies.pdf.

[43] *See, e.g.*, Cydney Posner ("No action to amend the Rule was taken by the SEC at the time.").

[44] Alfred L. Fatale III & Lisa Strejlau; *see, e.g.*, Ken Kam, 2 CEOs Who Have Not Earned My Trust, Forbes, Feb. 17, 2019, https://www.forbes.com/sites/kenkam/2019/02/17/2-ceos-who-have-not-earned-my-trust/#7a8dbec0337c ("the fact is [in October 2017, after changing his 10b5-1 trading plan, the former chief executive officer of Intel Corp. Brian] Krzanich sold every share [of Intel stock] he could and still remain CEO about a month before the security vulnerabilities of Intel's processors became public knowledge").

CII's recommended improvements to Rule 10b5-1 have been incorporated into the SEC study of Rule 10b5-1 that would be mandated by H.R. 624.[45] H.R. 624 was co-sponsored by Committee on Financial Service Chair Maxine Waters and Ranking Member Patrick T. McHenry.[46]

As you are aware, on January 28, 2019, the U.S. House of Representatives (House) approved H.R. 624 by a vote of 413 to 3. Prior to the vote, Representatives from both parties expressed support for the bill on the House floor. For example, Representative McHenry stated:

> This bipartisan legislation is critical for protecting mom and pop investors from the effects of insider trading, while ensuring that the rules are clear, fair and not unduly burdensome. I want to first thank chairwoman Waters for her sponsorship of this bill and for writing this legislation.[47]

On February 27, 2019, Ranking Member of the Securities Subcommittee of the Committee on Banking, Housing, and Urban Affairs (Banking Committee) Chris Van Hollen and Senator Deb Fischer introduced S. 573, a companion bill to H.R. 624.[48] In explaining her support for S. 573, Senator Fischer stated:

> Nebraskans who are investing to save for retirement or send their kids to college should receive a fair shake. Our bipartisan legislation will increase transparency in corporate trading to help weed out bad actors who take advantage of the current system. This is a common-sense solution that will level the playing field for hardworking American families and businesses on Main Streets.[49]

We noted that in commenting on the bill, SEC Commissioner Robert J. Jackson, Jr. stated:

> I share the bipartisan concern, reflected in a bill recently introduced . . . , that insider trading pursuant to plans under Rule 10b5-1 is associated with unusual insider profits. . . . Academic research identified this concern long ago, but neither Congress nor the SEC has addressed it yet.[50]

We believe the Commission should promptly propose amendments to Rule 10b5-1 along the lines we, the House, and Senators Van Hollen and Fischer have suggested to stop reoccurring and long-standing abuses of the spirit of the rule.

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[45] *See* Promoting Transparent Standards for Corporate Insiders Act, H.R. 624, 116th Cong. § 2(a)(1) (2019), *available at* https://www.congress.gov/bill/116th-congress/house-bill/624/text.
[46] *See* Promoting Transparent Standards for Corporate Insiders Act, H.R. 624, *available at* https://www.congress.gov/bill/116th-congress/house-bill/624/cosponsors.
[47] Promoting Transparent Standards for Corporate Insiders Act, H.R. 624 (statement of Rep. McHenry) (on file with CII).
[48] Promoting Transparent Standards for Corporate Insiders Act, S. 573, 116th Cong. (2019), *available at* https://www.congress.gov/bill/116th-congress/senate-bill/573/cosponsors.
[49] Van Hollen, Fischer Introduce Bi-Partisan Bill to Increase Transparency in Corporate Trading (Feb. 27, 2019), https://www.vanhollen.senate.gov/news/press-releases/van-hollen-fischer-introduce-bipartisan-bill-to-increase-transparency-in-corporate-trading.
[50] Robert J. Jackson, Jr., Letter on Stock Buyback's and Insider Cash Outs, Harv. L. Sch. F. on Corp. Governance & Fin. Reg. n.8 (Mar. 8, 2019), https://corpgov.law.harvard.edu/2019/03/08/letter-on-stock-buybacks-and-insiders-cashouts/.

CD&A Pay Target Metrics

CII believes that the Commission should make a priority of proposing amendments to ensure that public companies explain why and how they use non-standard metrics to determine Chief Executive Officer (CEO) pay.[51]

In April we submitted a rulemaking petition specifically asking the SEC amend Item 402(b) of Regulation S-K[52] to require companies in their proxy statements to (1) explain why they are using metrics other than generally accepted accounting principles (GAAP) in their CD&A for setting executive compensation and (2) provide a quantitative reconciliation of such metrics to their GAAP financials (or hyperlink to such a reconciliation in another document filed with the SEC).[53]

The problem, as MIT Sloan School of Management Senior Lecturer Robert C. Pozen and SEC Commissioner Jackson explain in their April *Wall Street Journal* op-ed: "The SEC's disclosure rules have not kept pace with changes in compensation practices, so investors cannot easily distinguish between high pay based on good performance and bloated pay justified by accounting gimmicks."[54]

It used to be the case that non-GAAP metrics were the exception in compensation committee reports, but now they have become the rule.[55] As recently discussed a blog by Olga Usvyatsky of

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[51] Council of Institutional Investors, Press Releases, Leading Investor Group Petitions SEC to Require Clear Disclosure on CEO Pay Targets (Apr. 29, 2019), https://www.cii.org/nongaapdisclosure ("Institutional investors say it's time for the Securities and Exchange Commission (SEC) to ensure that public companies explain why and how they use non-standard metrics to determine CEO pay.").

[52] Executive Compensation, 17 C.F.R. § 229.402(b) (Sept. 2006), *available at* https://www.law.cornell.edu/cfr/text/17/229.402 (Instruction 5 states: "Disclosure of target levels that are non-GAAP financial measures will not be subject to Regulation G (17 CFR 244.100 - 102) and Item 10(e) (§ 229.10(e)); however, disclosure must be provided as to how the number is calculated from the registrant's audited financial statement.").

[53] Letter from Kenneth A. Bertsch, Executive Director, Council of Institutional Investors et al. to Vanessa Countryman, Acting Secretary Securities and Exchange Commission (Apr. 29, 2019), https://www.cii.org/Files/issues_and_advocacy/correspondence/2019/20190426%20CII%20Petition%20revised%20on%20non-GAAP%20financials%20in%20proxy%20statement%20CDAs.pdf.

[54] Robert J. Jackson Jr. & Robert C. Pozen, Opinion/Commentary, Executive Pay Needs a Transparent Scorecard, Wall St. J, Apr. 10, 2019, https://www.wsj.com/articles/executive-pay-needs-a-transparent-scorecard-11554936540?mod=searchresults&page=1&pos=1; *see* Nicholas M. Guest et al., High Non-GAAP Earnings Predict Abnormally High CEO Pay (Jan. 2, 2019) (unpublished paper), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3030953 ("our evidence suggests large non-GAAP earnings adjustments influence some boards of directors in approving a level of CEO pay that is otherwise not supported by the firm's stock price or GAAP earnings performance."); Robert C. Pozen & S.P. Kothari, Executive Compensation, Decoding CEO Pay, Harv. Bus. Rev. (July-Aug. 2017), https://hbr.org/2017/07/decoding-ceo-pay (research suggesting that companies report inflated pro forma numbers in their proxy statements to rationalize overly generous executive compensation and recommending that "all exclusions of GAAP expenses should be justified and quantified").

[55] *See* Olga Usvyatsky, Pros and Cons of Using Non-GAAP Metrics for Executive Compensation, Including ESG Considerations, Audit Analytics (June 11, 2019), https://blog.auditanalytics.com/pros-and-cons-of-using-non-gaap-metrics-for-executive-compensation-including-esg-considerations/ (identifying a 50% increase in the use of non-

Audit Analytics, there are at least two problems when companies use non-GAAP metrics for compensation purposes:

> First, the figures don't need to be reconciled to GAAP numbers. This means that investors have little visibility into how the metrics are calculated and which expenses were taken out. Second, some firms will double-adjust executive compensation metrics by identically labeling metrics in both earnings releases and executive pay but calculating the metrics differently.
>
> There is limited transparency for investors and analysts when metrics are double-adjusted, and this is especially troubling if companies wouldn't be able to reach their C-suite compensation targets without double-adjusting the numbers. In 2018, about 30% of the S&P500 companies used metrics that were double-adjusted.[56]

We believe there are legitimate reasons for companies to use non-GAAP metrics for executive pay targets, but it is hard to tell unless you have a quantitative reconciliation about what exactly is happening.[57] In our view, the 2019 proxy statement excerpt of the FedEx Corporation attached to this letter provides an example of the type of information the SEC should require to ensure that investors can properly evaluate whether the CEO hit performance targets the board set for incentive pay.[58] Clarity on financial criteria for payouts is critical in the proxy statement because that is what shareholders review when deciding how to cast advisory votes on executive compensation, which occur annually at most companies.[59]

Shareholder Proposal Rule

We believe the current thresholds under SEC Rule 14a-8 for offering and resubmitting a shareholder proposal are well balanced and should not be changed.[60] We share the reported view that "certain Staff members left the [R]oundtable with the impression that stronger arguments were made in favor of keeping the current Rule 14a-8 eligibility requirements and resubmission thresholds."[61]

While CII recognizes that the existing ownership and resubmission thresholds were set long ago, we continue "to believe the current shareholder proposal rules permit investors to express their

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GAAP metrics for executive compensation in proxy statements); Brian Croce, CII Urges SEC to Require Clear Disclosure of Executive Pay, P&I, Apr. 29, 2019, https://www.pionline.com/article/20190429/ONLINE/190429852/cii-urges-sec-to-require-clear-disclosure-on-ceo-pay ("'It used to be case that non-GAAP metrics were the exception in compensation committee reports but now they've become the rule,' said Mr. Pozen").

[56] Olga Usvyatsky.

[57] Brian Croce ("'Sometimes there are legitimate reasons ... but it's hard to tell unless you have a quantitative reconciliation and a good explanation about what exactly is happening,' Mr. Pozen said.").

[58] FedEx Corporation, Definitive Proxy Statement, Appendix C (Aug. 13, 2018), https://www.sec.gov/Archives/edgar/data/1048911/000120677418002406/fedex3330721-def14a.htm#pg32a.

[59] *See* Council of Institutional Investors, Press Releases, Leading Investor Group Petitions SEC to Require Clear Disclosure on CEO Pay Targets.

[60] Shareholder Proposals, 17 C.F.R. § 240.14a-8 (1998), *available at* https://www.law.cornell.edu/cfr/text/17/240.14a-8.

[61] Adé Heyliger et al. at 3.

voices collectively on issues of concern to them, without the cost and disruption of waging proxy contests."[62] And we continue to believe that "the rule works particularly well in granting retail investors—who lack other avenues to meaningfully engage with management—a voice in the companies they own."[63]

CII believes Banking Committee Ranking Member Sherrod Brown fairly summarized the current debate surrounding shareholder proposals at a Banking Committee hearing earlier this year when he stated: "Corporate special interests want to . . . silence the voices of . . . investors by making it harder for shareholders to petition companies to allow all shareholders to vote on issues significant to the company."[64] Last month, Committee on Financial Services Chair Maxine Waters introduced, and the House passed, an amendment to the appropriations bill for the Commission that would restrict the SEC for using funds to revise the threshold for shareholder proposals or resubmissions under Rule 14a-8.[65]

We generally agree that pursuing 14a-8 rulemaking is not an effective use of the SEC's limited resources. Any effort to increase the Rule 14a-8 thresholds would be time-consuming, alienate many retail and institutional investors, and would likely provide limited, if any, reduction in corporate expenditures. As one example, many management-oriented special interest groups complain about the costs "when a failed shareholder proposal is resubmitted year after year."[66] In fact, a recent analysis by Sustainable Investments Institute (Si2) of environmental and social proposals that came to a vote over the last 5 years reveals that only 7% (74 of 1,054) of those proposals had been resubmitted 3 or more times.[67] Similarly, noted governance advocate Nell Minow recently stated that "if shareholder proposals constitute only 4% of proxy items and most companies receive none, resubmissions do not impose a significant burden on issuers."[68]

The attempt to rule certain matters significant to companies and their shareholders as "out of bounds" because they have social and/or political dimensions, or because there are differing views on them, seems perverse. Ironically, these efforts to exclude "politics" are themselves highly political efforts to limit discussion, and we would expect shareholder proposals to highlight matters

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[62] Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to The Honorable Michael D. Crapo, Chairman, Committee on Banking, Housing, and Urban Affairs, United States Senate et al. 12 (Feb. 27, 2019) [hereinafter February Letter], https://www.cii.org/files/issues_and_advocacy/correspondence/2019/February%2027%202019%20Letter%20to%20Senate%20Banking%20Committee.pdf.

[63] *Id*.

[64] Transcript of Senate Banking, Housing and Urban Affairs Committee, Hearing on The Application of Environmental, Social, and Governance Principles in Investing and the Role of Asset Managers, Proxy Advisors, and Other Intermediaries, Bloomberg Gov't 5 (Apr. 3, 2019) (on file with CII).

[65] H.R. Rep. No. 116-126, § 901 (June 24, 2019), https://www.congress.gov/congressional-report/116th-congress/house-report/126 (Amendment # 44).

[66] *See, e.g.*, Letter from Maria Ghazal, Senior Vice President & Counsel, Business Roundtable to Ms. Vanessa Countryman, Acting Secretary, Securities and Exchange Commission 5 (June 3, 2019), https://www.sec.gov/comments/4-725/4725-5619758-185567.pdf.

[67] Email from Heidi Welsh, Executive Director, Sustainable Investments Institute (Si2) to Jeff Mahoney (July 15, 2019) (on file with CII).

[68] Peter Rasmussen, Bloomberg Law Analysis, Analysis: Shutdown & New Legal Bulletin Shape 2019 Proxy Season, Bloomberg L., Apr. 17, 2019, https://news.bloomberglaw.com/bloomberg-law-analysis/analysis-shutdown-new-legal-bulletin-shape-2019-proxy-season.

on which there is some measure of disagreement. Typically, shareholder proposals are not required on matters for which the best path is obvious and universally agreed.

Shareholder proposals are a key tool in the U.S. market not only to communicate to the board and management, but also to other shareholders. For antitrust and other reasons, it is very difficult for shareholders in the U.S. market to communicate on company-specific matters with each other, putting a premium on the shareholder proposal as a tool both to express the collective voice of shareholders and for investors to gain some understanding of the perspective of other investors. We think this aspect of utility in shareholder proposals is entirely lost on management-oriented groups that would like to confine all company/shareholder engagement to one-on-one communications.

Proxy Advisory Firms

We believe that the SEC's new agenda project to propose amendments to Rule 14a-2(b) to add regulations to proxy advisory firms[69] is misguided and is not the best use of the Commission's limited resources.[70]

As you are aware, at the end of the Roundtable an SEC staff member asked: "Is there anyone on the panel that thinks there should be additional regulation?"[71] No panelist—including those speaking on behalf of the corporate community voiced any need for new regulations of proxy advisory firms.[72] One of those panelists was Patti Brammer, Corporate Governance Officer, Ohio Public Employees Retirement System (OPERS). Consistent with her comments at the Roundtable, a follow-up letter to the SEC explained:

> OPERS does not believe additional regulation of proxy advisory firms is warranted. . . . To the extent that a regulatory change increases our costs, delays the information we need, or erodes the confidence we have in the independence of the research reports we receive, there will be a negative impact on our members – the law enforcement officers, university employees, librarians, road workers, and others

[69] S*ee* Commissioner Elad L. Roisman, Speech, Keynote Remarks: ICI Mutual Benefit Funds and Investment Management Conference (Mar. 18, 2019), https://www.sec.gov/news/speech/speech-roisman-031819 (citing Rules 14a-2(b)(1) and 14a-2(b)(3) and stating: "since proxy advisory firms rely on the proxy solicitation exemptions available under certain Exchange Act rules, it may be appropriate for the Commission to reassess whether their current practices fit within the intended scope and purpose of these exemptions"); *see also* Cydney Posner, The SEC's Current End Game on Proxy Advisory Firms, Harv. L. Sch. F. on Corp. Governance & Fin. Reg. (Apr. 26. 2019), https://corpgov.law.harvard.edu/2019/04/26/the-secs-current-end-game-on-proxy-advisory-firms/ ('"It is . . . possible that the SEC could move forward with a regulatory proposal imposing tougher restrictions on proxy advisers [including] [t]he agency could require proxy advisers to provide draft recommendation reports to companies before publication for clients, so that businesses can submit comments and criticism, to accompany the initial recommendation report publication.'").

[70] Office of Information and Regulatory Affairs, Office of Management and Budget, Executive Office of the President, View Rule, SEC Title: Rule 14a-2(b).

[71] U.S. Securities and Exchange Commission, Roundtable on the Proxy Process Transcript at 250 (SEC Staff Michelle Anderson).

[72] *See id.* at 250-57; *see generally* Matt Egan, Corporate America Loves Deregulation. Then Why Is It Pushing For These Rules?, CNN Bus., Mar. 29, 2019, https://www.cnn.com/2019/03/29/investing/regulation-proxy-advisory-reform-sec/index.html (commenting that some market participants "say business groups are going after proxy advisers to silence shareholders by cutting them off from rigorous research needed to scrutinize gaudy pay packages and evaluate complicated proposals on topics such as climate change and minimum wage hikes").

> who depend on us for their retirement security. We respectfully request that the SEC preserve our access to efficient, timely, and independent information from our proxy advisory firm.[73]

Another of those panelists was former Banking Committee Chair Phil Gramm. Many of our members share the view expressed by Senator Gramm at a post-Roundtable Banking Committee hearing on the topic: "[M]y dealings with proxy advisors basically have been good. I think they listen [and] . . . the problem is not proxy advisors."[74]

We also note that in a December letter to the SEC, T. Rowe Price Associates, Inc. stated: "We . . . would have significant concerns with any regulatory changes that would sacrifice the objectivity of proxy advisor reports or introduce delays in the proxy voting process that, in an already compressed and intensely seasonal voting cycle, could result in missed vote deadlines."[75]

We acknowledge that SEC Commissioner Elad L. Roisman and some others have raised some legitimate issues regarding conflicts of interest, accuracy and completeness, pre-populating votes, and overly standardized voting guidelines.[76] While we concede that there is room for improvement, we believe there are other more cost-effective avenues that do not require additional regulation.

More specifically, CII believes that the Commission could encourage private sector solutions. In particular, we support strengthening of the Best Practice Principles for Shareholder Voting Research, a global proxy advisory industry effort to improve standards.[77]

We also note that Glass Lewis (GL) recently announced that it has established a Report Feedback Statement (RFS).[78] In response to concerns about accuracy and completeness of information, the RFS provides an opportunity for public companies and shareholder proposal proponents to express their differences of opinion with GL analysis, and then have those comments delivered to 3000+

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[73] Letter from Karen Carraher, Executive Director, Ohio Public Employees Retirement System et al. to Brent J. Fields, Secretary, Securities and Exchange Commission 4 (Dec. 13, 2018), https://www.sec.gov/comments/4-725/4725-4767821-176841.pdf.

[74] Transcript of Senate Banking, Housing and Urban Affairs Committee, hearing on The Application of Environmental, Social, and Governance Principles in Investing and the Role of Asset Managers, Proxy Advisors, and Other Intermediaries, Bloomberg Gov't 14 (on file with CII).

[75] Letter from Donna F. Anderson, Head of Corporate Governance, T. Rowe Price Associates, Inc. et al. to Brent J. Fields, Esq., Secretary, Securities and Exchange Commission 3 (Dec. 13, 2018), https://www.sec.gov/comments/4-725/4725-4792350-176928.pdf.

[76] *See, e.g.*, Commissioner Elad L. Roisman, Speech, Keynote Remarks: ICI Mutual Benefit Funds and Investment Management Conference.

[77] *See* The BPPG, Best Practices Principles for Shareholder Voting Research (last visited July 17, 2019), https://bppgrp.info/.

[78] Katherine Rabin, CEO, Glass Lewis, Glass Lewis' Report FeedBack Service: Direct, Unfiltered Commentary from Issuers and Shareholder Proponents, Harv. L. Sch. F. on Corp. Governance & Fin. Reg. (Mar. 31, 2019), https://corpgov.law.harvard.edu/2019/03/31/glass-lewis-report-feedback-service-direct-unfiltered-commentary-from-issuers-and-shareholder-proponents/.

individuals who subscribe to GL's research and voting services.[79] An analysis by Bloomberg Law indicated that the RFS "would be beneficial for the industry and the marketplace."[80]

In addition, CII believes the Commission could consider improving the oversight of its existing guidance. SEC Staff Legal Bulletin No. 20 (SLB 20), in our estimation, already appropriately provides that investment advisors ensure that voting recommendations are based on current and accurate information and to identify and address conflicts of interest.[81] If the SEC has evidence that the provisions of SLB 20 regarding proxy advisory firms are not being complied with or are otherwise misunderstood by investment advisors, we would support more effective SEC oversight and of the guidance and, if deemed necessary, clarification of the requirements.

We note that the SEC's new agenda project to propose amendments to Rule 14a-2(b) appears to be in direct conflict with the recommendations of the SEC's own Investor Advocate Rick Fleming.[82] In an April speech Mr. Fleming stated:

> I sincerely hope that the Commission will not prioritize a rulemaking that could impair the independence of proxy advice or lead to even greater inefficiencies in proxy voting. As a practical matter, it is hard to imagine, based on the feedback I've seen to date, that a serious economic analysis could justify a rulemaking to cure a purported harm when the investors—the supposed victims of the harm—have denied that a significant problem exists.
>
> Again, no one is claiming that proxy advisors are perfect, but in light of all the important things that the Commission could spend its time on—including the initiatives I highlighted earlier—I would respectfully suggest that imposing new regulations on proxy advisers should be given a low priority.[83]

Given Mr. Fleming's comments and the overwhelming opposition of investors to additional regulation of proxy advisory firms, it is not surprising that the Committee on Financial Services Chair introduced, and the House passed, an amendment to the appropriations bill for the Commission that would prohibit the SEC "from proposing, implementing, administering, or enforcing any rule that would revise the reliance of certain advisors on the proxy solicitation exemption under 240.14a-2(b)."[84] As indicated, we agree that pursuing rulemaking to further regulate proxy advisory firms is not an effective use of the SEC's limited resources, particularly when the SEC could, among other things, use its limited resources to ensure investor confidence in

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[79] *Id*. ("The Report Feedback Statement service provides a unique opportunity for public companies and shareholder proposal proponents—the subjects of Glass Lewis research—to express their differences of opinion with Glass Lewis' analysis, and then have those comments delivered through a unique, focused channel to 3,000+ individuals who subscribe to Glass Lewis' research and voting services.").
[80] Peter Rasmussen.
[81] *See, e.g.*, February Letter, *supra* note 62, at 13 ("While we concede that there is room for improvement, SEC Staff Legal Bulletin No. 20, in our estimation, already effectively requires investment advisors to ensure that voting recommendations are based on current and accurate information and to identify and address conflicts of interest.").
[82] *See* Rick Fleming, Speech at The SEC Speaks in 2019: Important Issues for Investors in 2019 (Apr. 8, 2019), https://www.sec.gov/news/speech/fleming-important-issues-investors-2019.
[83] *Id*.
[84] H.R. Rep. No. 116-126, § 901 (Amendment # 43).

proxy voting is improved through an effective system of vote confirmation, and completing its rulemaking on universal proxy as an interim step to improving proxy plumbing.[85]

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Thank you for consideration of our views. If we can answer any questions or provide additional information on the Commission's regulatory agenda, please do not hesitate to contact me at [redacted] or [redacted].

Sincerely,

Jeffrey P. Mahoney
General Counsel

Attachment

[85] *See, e.g.*, February Letter, *supra* note 62, at 10-12 (discussion of long-term and interim improvements to proxy plumbing).

FedEx 2019 proxy Appendix C

https://www.sec.gov/Archives/edgar/data/1048911/000120677418002406/fedex3330721-def14a.htm#pg32a

Appendix C

Reconciliations of Non-GAAP Measures

We report our financial results in accordance with accounting principles generally accepted in the United States ("GAAP" or "reported"). We have supplemented the reporting of our financial information determined in accordance with GAAP with certain non-GAAP (or "adjusted") financial measures.

We believe these adjusted financial measures facilitate analysis and comparisons of our ongoing business operations because they exclude items that may not be indicative of, or are unrelated to, the company's and our business segments' core operating performance, and may assist investors with comparisons to prior periods and assessing trends in our underlying businesses. These adjustments are consistent with how management views our businesses. Management uses these non-GAAP financial measures in making financial, operating, compensation and planning decisions and evaluating the company's and each business segment's ongoing performance.

Our non-GAAP measures are intended to supplement and should be read together with, and are not an alternative or substitute for, and should not be considered superior to, our reported financial results. Accordingly, users of our financial statements should not place undue reliance on these non-GAAP financial measures. Because non-GAAP financial measures are not standardized, it may not be possible to compare these financial measures with other companies' non-GAAP financial measures having the same or similar names.

See our earnings releases, which are available in the News & Events section of the Investor Relations page of our website at http://investors.fedex.com, for additional details regarding the reconciliation of GAAP and non-GAAP financial measures below.

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Fiscal 2018 Reconciliations for Fiscal 2018 AIC Plan and FY2016–FY2018 and Active LTI Plans

As described in "Executive Compensation — Compensation Discussion and Analysis," the Board of Directors, upon the recommendation of the Compensation Committee, designed or later adjusted the fiscal 2018 AIC plan and the FY2016–FY2018, FY2017–FY2019, FY2018–FY2020 and FY2019–FY2021 LTI plans to exclude from fiscal 2018 earnings the following items (as applicable to each plan), in order to ensure that payouts under the plans more accurately reflect core financial performance in fiscal 2018: (i) the annual mark-to-market ("MTM") retirement plans accounting and other pension adjustments; (ii) fiscal 2018 TNT Express integration expenses (including any restructuring charges at TNT Express); (iii) expenses in connection with certain pending U.S. Customs Border and Protection matters involving FedEx Trade Networks; (iv) the cost of accelerated 2018 annual pay increases for certain hourly team members to April 2018 from October 2018, following the passage of the Tax Cuts and Jobs Act of 2017 (the "TCJA"); (v) goodwill and other asset impairment charges at FedEx Supply Chain; and (vi) the provisional benefit from the remeasurement of the company's net U.S. deferred tax liability following the passage of the TCJA. The table below presents a reconciliation of our presented fiscal 2018 non-GAAP measures to the most directly comparable GAAP measures.

FISCAL 2018

	FedEx Corporation			
Dollars in millions, except EPS	**Operating Income**	**Income Taxes[1][2]**	**Net Income[2][3]**	**Diluted Earnings Per Share**
GAAP measure	**$4,870**	**$(219)**	**$4,572**	**$16.79**
FedEx Supply Chain goodwill and other asset impairment charges[4]	380	1	379	1.39
TNT Express integration expenses[5]	477	105	372	1.36
FedEx Trade Networks legal matters	8	2	6	0.02
MTM retirement plans accounting and other pension adjustments[6]	(10)	(1)	(9)	(0.03)
Net U.S. deferred tax liability remeasurement	—	1,150	(1,150)	(4.22)
Accelerated 2018 annual pay increases	55	11	44	0.16
Non-GAAP measure for FY16–FY18, FY17–FY19, FY18–FY20 and FY19–FY21 LTI plans and fiscal 2018 AIC plan[7]	*$5,780*	$1,050	$4,213	*$15.47*

(1) Income taxes are based on the company's approximate statutory tax rates applicable to each transaction and give consideration to the effects of the TCJA on the fiscal 2018 rates.
(2) Does not sum to total due to rounding.
(3) Effect of "Total other (expense) income" on net income amount not shown.
(4) Goodwill impairment charges are not deductible for income tax purposes.
(5) These expenses, including restructuring charges at TNT Express, were recognized at FedEx Corporate and FedEx Express.
(6) MTM retirement plans accounting adjustments reflect the year-end adjustment to the valuation of the company's defined benefit pension and other postretirement plans. MTM retirement plans accounting and other pension adjustments include the one-time $210 million charge recognized in the fourth quarter of fiscal 2018 related to the previously announced transfer of approximately $6 billion of FedEx Corporation's tax-qualified U.S. domestic pension plan obligations to Metropolitan Life Insurance Company.
(7) Fiscal 2018 adjusted EPS of $15.47 is used for purposes of calculating actual aggregate EPS under the FY16–FY18, FY17–FY19 and FY18–FY20 LTI plans and is the base-year EPS for the FY19–FY21 LTI plan. Adjusted consolidated operating income of $5,780 is used for purposes of the fiscal 2018 AIC plan.

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Fiscal 2017 Reconciliations for FY2016–FY2018, FY2017–FY2019 and FY2018–FY2020 LTI Plans

As described in "Executive Compensation — Compensation Discussion and Analysis," the Board of Directors, upon the recommendation of the Compensation Committee, designed or later adjusted the FY2016–FY2018, FY2017–FY2019 and FY2018–FY2020 LTI plans to exclude from fiscal 2017 earnings the following items, in order to ensure that payouts under the plans more accurately reflect core financial performance in fiscal 2017: (i) the annual mark-to-market ("MTM") retirement plans accounting adjustments; (ii) TNT Express integration expenses (including any restructuring charges at TNT Express); (iii) expenses related to the settlement of and certain expected losses relating to independent contractor litigation matters involving FedEx Ground; and (iv) charges accrued in connection with pending U.S. Customs and Border Protection matters involving FedEx Trade Networks. Additionally, the Board approved adjustments to the FY16–FY18 and FY17–FY19 LTI plans to exclude the impact in fiscal 2017 of stock repurchase activity (net of interest expense on debt issued to fund a portion of the applicable stock repurchase program). The table below presents a reconciliation of our presented fiscal 2017 non-GAAP measures to the most directly comparable GAAP measures.

FISCAL 2017

	FedEx Corporation			
Dollars in millions, except EPS	**Operating Income**	**Income Taxes[1]**	**Net Income[2][3]**	**Diluted Earnings Per Share[3]**
GAAP measure	**$5,037**	**$1,582**	**$2,997**	**$11.07**
MTM retirement plans accounting adjustments[4]	(24)	(18)	(6)	(0.02)
TNT Express integration expenses[5]	327	82	245	0.91
FedEx Trade Networks legal matters	39	15	24	0.09
FedEx Ground legal matters	22	9	13	0.05
Non-GAAP measure for FY18–FY20 LTI plan[6]	$5,401	$1,670	$3,273	*$12.09*
EPS impact of stock repurchases	—	—	—	(0.40)
Interest expense[7]	—	52	89	0.33
Non-GAAP measure for FY16–FY18 LTI and FY17–FY19 LTI plans[8]	$5,401	$1,722	$3,361	*$12.02*

(1) Income taxes are based on the company's approximate statutory tax rates applicable to each transaction.
(2) Effect of "Total other (expense) income" on net income amount not shown.
(3) Does not sum to total due to rounding.
(4) MTM retirement plans accounting adjustments reflect the year-end adjustment to the valuation of the company's defined benefit pension and other postretirement plans.
(5) These expenses, including restructuring charges at TNT Express, were recognized at FedEx Corporate and FedEx Express.
(6) Fiscal 2017 adjusted EPS of $12.09 is the base-year EPS for the FY18–FY20 LTI plan.
(7) Represents the income tax and net income impact of $141 million of interest expense on debt issued to fund a portion of the applicable stock repurchase program.
(8) Fiscal 2017 adjusted EPS of $12.02 (adjusted to reflect the stock repurchase impact) is used for purposes of calculating actual aggregate EPS under the FY16–FY18 and FY17–FY19 LTI plans.

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APPENDIX C RECONCILIATIONS OF NON-GAAP MEASURES – FISCAL 2016 RECONCILIATIONS

Fiscal 2016 Reconciliations for FY2016–FY2018 and FY2017–FY2019 LTI Plans

As described in "Executive Compensation — Compensation Discussion and Analysis," the Board of Directors, upon the recommendation of the Compensation Committee, designed or later adjusted the FY2016–FY2018 and FY2017–FY2019 LTI plans to exclude from fiscal 2016 earnings the following items (as applicable to each plan), in order to ensure that payouts under the plans more accurately reflect core financial performance in fiscal 2016: (i) the annual MTM retirement plans accounting adjustments; (ii) expenses in connection with the settlement of and certain expected losses relating to independent contractor litigation matters involving FedEx Ground, net of recognized immaterial insurance recovery; (iii) expenses related to the settlement of a U.S. Customs and Border Protection matter involving FedEx Trade Networks, net of recognized immaterial insurance recovery; (iv) expenses associated with the acquisition, financing and integration of TNT Express, net of any tax impact, and TNT Express's fiscal 2016 financial results; (v) the favorable tax impact from an internal corporate legal entity restructuring to facilitate the integration of FedEx Express and TNT Express; and (vi) the EPS impact of stock repurchase activity (net of interest expense on debt issued to fund a portion of the applicable stock repurchase program). The table below presents a reconciliation of our presented fiscal 2016 non-GAAP measures to the most directly comparable GAAP measures.

FISCAL 2016

	FedEx Corporation			
Dollars in millions, except EPS	**Operating Income[1]**	**Income Taxes[1][2]**	**Net Income[3]**	**Diluted Earnings Per Share**
GAAP measure	**$3,077**	**$920**	**$1,820**	**$6.51**
MTM retirement plans accounting adjustments[4]	1,498	552	946	3.39
TNT expenses and financial results[5]	115	6	125	0.45
Tax impact — legal entity restructuring for TNT integration	—	76	(76)	(0.27)
FedEx Ground legal matters[6]	256	97	158	0.57
FedEx Trade Networks legal matter[6]	69	26	43	0.15
Non-GAAP measure for FY17–FY19 LTI plan[7]	$5,014	$1,678	$3,016	*$10.80*
EPS impact of stock repurchases	—	—	—	(0.32)
Interest expense[8]	—	19	32	*0.12*
Non-GAAP measure for FY16–FY18 LTI plan[9]	$5,014	$1,697	$3,048	*$10.60*

(1) Does not sum to total due to rounding.
(2) Income taxes are based on the company's approximate statutory tax rates applicable to each transaction.
(3) Effect of "Total other (expense) income" on net income amount not shown.
(4) MTM retirement plans accounting adjustments reflect the year-end adjustment to the valuation of the company's defined benefit pension and other postretirement plans.
(5) TNT Express's financial results are immaterial from the time of acquisition (May 25, 2016).
(6) Net of recognized immaterial insurance recovery.
(7) Fiscal 2016 adjusted EPS of $10.80 is the base-year EPS for the FY17–FY19 LTI plan.
(8) Represents the income tax and net income impact of $51 million of interest expense on debt issued to fund a portion of the applicable stock repurchase program.
(9) Fiscal 2016 adjusted EPS of $10.60 (adjusted to reflect the stock repurchase impact) is used for purposes of calculating actual aggregate EPS under the FY16–FY18 LTI plan.

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Fiscal 2015 Reconciliations for FY2016–FY2018 LTI Plan

As described in "Executive Compensation — Compensation Discussion and Analysis," the Board of Directors, upon the recommendation of the Compensation Committee, designed or later adjusted the FY2016–FY2018 LTI plan to exclude from fiscal 2015 earnings the following items, in order to ensure that payouts under the plan more accurately reflect core financial performance in fiscal 2015: (i) the net impact of the company's adoption of MTM accounting for its defined benefit pension and other postretirement plans, including the impact of lowering the expected return on plan assets ("EROA") assumption from 7.75% to 6.5% in the presentation of segment results for all prior periods; (ii) aircraft impairment and related charges; and (iii) a charge to increase the legal reserve associated with the settlement of a legal matter at FedEx Ground to the amount of the settlement. The table below presents a reconciliation of our presented fiscal 2015 non-GAAP measures to the most directly comparable GAAP measures.

FISCAL 2015

Dollars in millions, except EPS	FedEx Corporation			
	Operating Income	**Income Taxes[1][2]**	**Net Income[3]**	**Diluted Earnings Per Share**
GAAP measure	**$1,867**	**$577**	**$1,050**	**$3.65**
Segment reporting change[4]	(266)	(98)	(168)	(0.58)
MTM retirement plans accounting adjustments[5]	2,190	808	1,382	4.81
Aircraft impairment and related charges	276	101	175	0.61
FedEx Ground legal matter	197	64	133	0.46
Non-GAAP measure	$4,264	$1,451	$2,572	$8.95
Segment elimination of pension amortization expense and recast of EROA, net	(36)	(13)	(23)	(0.08)
Non-GAAP measure for FY16–FY18 LTI plan[6]	$4,228	$1,438	$2,549	*$8.87*

(1) Does not sum to total due to rounding.
(2) Income taxes are based on the company's approximate statutory tax rates applicable to each transaction.
(3) Effect of "Total other (expense) income" on net income amount not shown.
(4) Represents the adjustment in "Corporate, other and eliminations" resulting from the change in recognizing EROA for our defined benefit pension and other postretirement plans at the segment level associated with the adoption of MTM accounting.
(5) MTM retirement plans accounting adjustments reflect the year-end adjustment to the valuation of the company's defined benefit pension and other postretirement plans.
(6) Fiscal 2015 adjusted EPS of $8.87 is the base-year EPS for the FY16–FY18 LTI plan.