AMERICAN BAR ASSOCIATION
Business Law Section

321 N. Clark Street
Chicago, IL 60654-7598
[redacted]
ababusinesslaw.org

Via Electronic Submission

January 24, 2022

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

Re: File No. S7-12-15
Release No. 33-10998
Comments on Listing Standards for Recovery of Erroneously Awarded Compensation

Dear Ms. Countryman:

This letter is submitted on behalf of the Committee on Federal Regulation of Securities (the "**Committee**" or "**we**") of the Section of Business Law of the American Bar Association (the "**ABA**"), in response to the request for additional public comments by the U.S. Securities and Exchange Commission (the "**Commission**") on the proposed rule entitled "Listing Standards for Recovery of Erroneously Awarded Compensation" as set forth in a release published in the Federal Register on July 14, 2015 (Release Nos. 33-9861; 34-75342) (the "**2015 Proposing Release**"). As set forth in the 2015 Proposing Release, the Commission proposed a new rule and rule and form amendments to implement Section 954 ("**Section 954**") of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "**Dodd-Frank Act**"). Section 954 added Section 10D to the Securities Exchange Act of 1934, as amended (the "**Exchange Act**"), which requires the Commission to adopt rules directing the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance with its requirements for disclosure of the issuer's policy on incentive-based compensation and recovery of incentive-based compensation that is received in excess of what would have been received under an accounting restatement (the "**Proposed Rules**"). On February 11, 2016, the Committee submitted a comment letter on the 2015 Proposing Release (the "**Original Comment Letter**").

On October 21, 2021, the Commission reopened the comment period for its proposal to implement the provisions of Section 954 through a release published in the Federal Register (Release No. 33-10998) (the "**2021 Reopening Release**"). We refer to the original Proposed Rules and the updates contained in the 2021 Reopening Release as the "**Proposals**." We appreciate the additional opportunity to comment on the Proposals, and we respectfully request that the Commission consider, in addition to the concerns and recommendations set forth in the Original Comment Letter, the following concerns and recommendations with respect to the additional requests for comment in the 2021 Reopening Release.

The comments expressed in this letter (this "**Comment Letter**") represent the views of the Committee only and have not been approved by the ABA's House of Delegates or Board of Governors and, therefore, do not represent the official position of the ABA. In addition, this Comment Letter does not represent the official position of the Section of Business Law of the ABA.

Comments on Questions Raised in 2021 Reopening Release

As we noted in the Original Comment Letter, generally we applaud the Commission's efforts in proposing a new rule, and rule and form amendments, to implement the provisions of Section 954 of the Dodd-Frank Act, which added Section 10D to the Exchange Act. These Proposals seek to strike a balance between the objectives of the compensation recovery policy contemplated by Section 954 with the costs and burdens that would be incurred by listed issuers in maintaining and enforcing such a policy. These Proposals also seek to ensure that issuers listed on different exchanges are subject to the same disclosure requirements regarding their compensation recovery policies.

We respectfully request that the Commission consider these additional observations and recommendations when formulating the final rules implementing Section 954. Please note that we have numbered each topic to correspond to the numbering system used by the Commission in the "Request for Comment" section of the 2021 Reopening Release.

2. Should we remove the "reasonably should have concluded" standard in light of concerns that the standard adds uncertainty to the determination?

In our Original Comment Letter, we raised concerns about the element of uncertainty that adding the language "reasonably should have concluded" would impose if included as a concept to the trigger of the three-year lookback period for compensation recovery. As proposed, the trigger would have in part the same standard as that in Item 4.02(a) of Form 8-K, namely that an issuer's

board of directors, a committee of the board of directors, or the officer or officers of the issuer authorized to take such action if board action is not required have concluded that the issuer's previously issued financial statements contain a material error.[1] However, as proposed, the language "or reasonably should have concluded" would be added to that standard, adding subjectivity to the triggering event that differs from Form 8-K. We support aligning this part of the triggering standard with the existing language in Form 8-K and continue to believe that the inclusion of a "reasonably should have concluded" standard would introduce unnecessary subjectivity to the determination on the part of the board of directors or officers. This subjectivity would be open to second-guessing, litigation and could easily become a point of contention among the parties in effectively implementing or exercising a compensation recovery provision.

However, if the Commission were to expand this portion of the triggering standard as proposed in the 2021 Reopening Release, we believe that the appropriate standard would be to use the earlier of (a) the date the issuer's board of directors, a committee of the board of directors, or the officer or officers of the issuer authorized to take such action if board action is not required, concludes that the issuer's previously issued financial statements require a restatement to correct an error in those financial statements that is material to the previously issued financial statements or that would result in a material misstatement if (1) the error was left uncorrected in the current report or (2) the error correction was recognized in the current period, or (b) the date a court, regulator or other legally authorized body directs the issuer to restate its previously issued financial statements to correct a material error.

3. Should the Commission rely on common understanding or specifically delineate the rules without relying on a set of definitions specific to this rule?

We believe that if the Commission adopts the revised clawback trigger it is considering (as described in its initial question in the 2021 Reopening Release) that would specifically refer to all required restatements to previously issued financial statements, including those restatements that were not material to those previously issued financial statements, but would result in a material misstatement if (a) the errors were left uncorrected in the current report or (b) the error correction was recognized in the current period, it would be easier and more streamlined for issuers to rely on existing guidance, literature, and definitions concerning accounting errors rather than define the terms "accounting restatement" and "material noncompliance." Given the broader

[1] As proposed, the lookback period would also be triggered on "the date a court, regulator or other legally authorized body directs the issuer to restate its previously issued financial statements to correct a material error." We support this standard as a secondary triggering event as proposed.

scope of the provision under the revised clawback trigger, such an approach would remain current over time as issuers would be able to assess the materiality of an accounting error and to determine when the final rule would come into play. Consequently, we support the removal of the proposed definitions of "accounting restatement" and "material noncompliance" and, instead, the reliance on existing resources.

4. Should we add check boxes to the cover page of the Form 10-K that indicate separately (a) whether the previously issued financial statements included in the filing include an error correction, and (b) whether any such corrections are restatements that triggered a clawback analysis during the fiscal year?

We support the Commission's suggestion that it add a check box to the cover page of the annual report on Form 10-K to indicate whether the previously issued financial statements included in the filing include an error correction, and whether any such corrections are restatements that triggered a clawback analysis during the fiscal year. We believe that, once the final rule is adopted, this will be an item of great interest to investors and such an approach would make it much easier to locate situations where an issuer had actually conducted a clawback as a result of a financial restatement. While the use of a current report on Form 8-K would be another acceptable method for transmitting this information, given the number of Forms 8-K that an issuer may be required to file over the course of a fiscal year, the Form 10-K would simplify the search to a single document and streamline the research process.

7. Would investors benefit from disclosure of how issuers calculated the recoverable amount, including their analysis of the amount of the executive's compensation that is recoverable under the rule, and/or the amount that is not subject to recovery?

We support the concept of disclosure of how issuers calculated the recoverable amount, including their analysis of the amount of the executive's compensation that is recoverable under the rule, subject to one caveat. However, as we recommended in our Original Comment Letter (and summarize in the section entitled "Incentive-Based Compensation" below, we do not support the inclusion of either an issuer's stock price or its total shareholder return in the definition of the term "financial reporting measure." Further, we believe that inclusion of compensation granted, earned, or vested based on stock price or total shareholder return in the definition of "incentive-based compensation" introduces an unacceptable degree of uncertainty, complexity, and cost into compliance with Section 10D of the Exchange Act. We believe that it is inconsistent with the statutory mandate to include these items in such definition as each measure reflects many factors beyond the issuer's reported financial

information. We are also concerned that the inclusion of these items in the term, coupled with this disclosure requirement under consideration would lead to lengthy and complex disclosures regarding the determination and methodology that an issuer used to estimate the effect of stock price or total shareholder return on the recovery. It may be difficult for investors to understand the nuances in these terms as defined and applied from one issuer to another, potentially leading to such disclosures being more confusing than enlightening. As long as an issuer has such information available for review upon request by the Commission Staff, we do not see a significant benefit to investors from having direct access to such information nor a reason for requiring an issuer to include such information in its disclosure.

9. Would Inline XBRL detail tagging of some or all of the compensation recovery disclosures be valuable to investors?

After careful consideration, we recommend that the final rules not require that specific data points within the new compensation recovery disclosure be separately detail tagged using Inline XBRL. Since disclosure is only required in the event of a material restatement, we expect that the recovery process will vary significantly among issuers, depending on the structure and form of their individual executive compensation program. As a result, we anticipate that issuers will tend to create custom tags, as the standard taxonomy will not provide an appropriate element to tag the recovery disclosure. With this leading to a significant increase in custom tags, we believe requiring XBRL tagging of recovery disclosures will create additional comparability issues (and, thus, provide only limited benefits to investors while unnecessarily burdening issuers).

Transition Period for Compliance to New Rule

As originally set forth in the 2015 Proposing Release, the Commission proposed that each national securities exchange file its proposed listing rules no later than 90 days following publication of the final adopted version of Rule 10D-1 in the Federal Register, and that its rules be effective no later than one year following that publication date, and that each listed issuer must adopt the recovery policy required by this section no later than 60 days following the date on which the exchanges' rules become effective. While we have no questions about the first two deadlines proposed, we are concerned as to whether it is realistic to expect that each issuer will be able to adopt the recovery policy required by Rule 10D-1 no later than 60 days following the date on which the exchanges' rules become effective. We raise this issue because, as the Commission notes in the 2021 Reopening Release, numerous issuers have adopted their own compensation recovery policies over the past six years in the absence of Commission rulemaking. The vast majority of these polices provide for compensation committee discretion in determining whether to recover the

excess compensation, provide for a different (typically, shorter) lookback period, define differently (and, therefore, cover) different groups of executive officers and/or do not specifically address whether compensation granted, earned, or vested based on stock price or total shareholder return is to be included in the definition of "incentive-based compensation." Accordingly, many of these policies will require substantial revision or coordination with the issuer's newly-adopted Rule 10D-1-compliant policy. Consequently, we request that the Commission extend the period for adopting the recovery policy to six months.

Additional Comments

In addition to commenting on several of the specific questions raised by the Commission in the 2021 Reopening Release, we would also like to reiterate the primary recommendations provided in our Original Comment Letter. We respectfully request that the Commission revisit and reconsider these recommendations when crafting the final rule for the benefit of issuer's investors, and other market participants.

While we support many facets of the Proposed Rules, we continue to believe that certain
aspects should be modified or enhanced, either to streamline and simplify the operation of the mandated compensation recovery policy or to reduce the costs and burdens of enforcement by listed issuers.

Issuers Subject to Proposed Exchange Act Rule 10D-1. As we requested in the Original Comments Letter, we believe that the Commission should exercise its authority under the Exchange Act to exempt smaller reporting companies, emerging growth companies, and foreign private issuers from proposed Rule 10D-1 as being necessary or appropriate in the public interest and consistent with the protection of investors. In the case of smaller reporting companies and emerging growth companies, we are concerned that applying proposed Rule 10D-1to such issuers would impose costs and burdens that are disproportionate to the benefits to be obtained by the security holders of such issuers. In the case of foreign private issuers, the Commission has long exempted such issuers from many of the corporate governance and executive compensation-related disclosure requirements of the federal securities laws in recognition of the priority of home country law and local custom. We believe that such deference should be afforded to foreign private issuers with respect to the final version of Rule 10D-1.

Executive Officers Subject to Compensation Recovery Policy. We continue to believe that the mandated compensation recovery policy should apply only to individuals who have a meaningful role in the preparation of an issuer's financial statements, as well as individuals who had a role in the events

leading to the restatement, as identified by an issuer's Board of Directors. Consequently, we continue to recommend that, for purposes of the final version of Rule 10D-1, the term "executive officer" be defined as an issuer's principal executive officer, principal financial officer, and chief accounting officer (or if there is no such accounting officer, the controller) and any vice president in charge of a principal business unit, division, or function or any other officer who performs a policy-making function and whom the Board of Directors determined to have had a significant role in the events leading to the financial restatement.

We also continue to believe that recovery should apply only to incentive-based compensation earned by individuals who were executive officers during the three-year period preceding a restatement and only to the extent such compensation was earned during such portion or portions of the three-year period in which the individual was serving as an executive officer.

"Incentive-Based Compensation." Given the "no-fault" nature of proposed Rule 10D-1, we believe only compensation that is truly "incentive" in nature should be subject to the mandated compensation recovery policy. Accordingly, we continue to recommend that "incentive-based compensation" be defined as compensation of the type that would be reportable in the Grants of Plan-Based Awards Table (specifically, non-equity incentive plan awards as reported in columns (c) through (e) of the table and equity incentive plan awards as reported in columns (f) through (h) of the table) and which is granted, earned, or vested based wholly or in part upon the attainment of a financial reporting measure. We believe that the rule will be difficult to apply without such a limitation, particularly given the "wholly or in part" aspect of the definition.

Further, we recommend that the definition of the term "financial reporting measure" be limited to measures that are determined and presented in accordance with the accounting principles used in preparing the issuer's financial statements and any measures that are derived wholly or in part from such measures. We believe that it is inconsistent with the statutory mandate to include either an issuer's stock price and its total shareholder return in such definition as each measure reflects many factors beyond the issuer's reported financial information, the sole criterion set forth in Section 10D(b)(1) of the Exchange Act. We believe that inclusion of compensation granted, earned, or vested based on stock price or TSR in the definition of "incentive-based compensation" introduces an unacceptable degree of uncertainty, complexity, and cost into compliance with Section 10D of the Exchange Act.

Compensation Recovery Process. We continue to believe the contemplated level of issuer discretion in proposed Rule 10D-1 is problematic and, in our view, represents the single biggest impediment to the effective implementation of Section 10D. An issuer's Board of Directors would have

almost no discretion in determining whether to pursue recovery, as well as how much to recover. Indeed, as proposed, an issuer would be required to recover erroneously-awarded compensation in all instances, with only one limited exception – where recovery is "impracticable." We believe this rigidity, as well as the virtual absence of issuer discretion, invites problems and will inevitably frustrate the objectives of Section 10D – especially when considered in the context of the situations that issuers are likely to encounter in seeking to enforce their compensation recovery policy.

Consequently, we recommend that the Boards of Directors of listed issuers be given broad discretion to assess whether recovery is in the best interests of the issuer and its security holders, and, if so, how much to recover (including less than the full recoverable amount) and how to effect that recovery consistent with the objectives of Section 10D. To provide the necessary oversight of this process, we recommend that the disclosure requirements of proposed Item 402(w) be used to monitor the enforcement decisions and actions of the Board of Directors.

Should the Commission not agree with our recommendations concerning issuer discretion as described above, we recommend that, with respect to the exception where the costs of recovery would exceed the amount to be recovered, the analysis be based on all of the direct costs to be incurred by the issuer, whether or not paid to a third party, as well as any indirect costs that it can reasonably allocate to the recovery process.

Further, we support the proposal to permit foreign issuers to forgo recovery of excess incentive-based compensation if such recovery would violate home county law, with some minor modifications as noted. We also recommend that, in view of the uncertainty as to domestic issuers' ability to recover excess incentive-based compensation in certain states, this exception be extended to domestic issuers as well. Consistent with the foregoing recommendations, we support the proposal to permit an issuer's Board of Directors to exercise discretion in determining the appropriate means of recovery of excess incentive-based compensation. In our view, recovery should be permitted by any method the Board of Directors deems to be appropriate.

Determination of Excess Compensation. Should the Commission not agree with our recommendations concerning issuer discretion as described above, we would support the proposal for calculating the amount of excess incentive-based compensation that listed issuers must recover, subject to one revision. To avoid a punitive and inequitable result, we believe that such amounts should be calculated on a post-tax, rather than a pre-tax, basis. We disagree that the recoverable amount of incentive-based compensation should be calculated on a pre-tax basis "to ensure that the company recovers the full amount of incentive-based compensation that was erroneously awarded." In our

view it would be inequitable to require an executive officer to return incentive-based compensation on a pre-tax basis after the executive has paid taxes on that compensation, resulting in an overcollection when recovering excess compensation from the executive. An executive should not be placed in a position where the executive has less money than before the incentive-based compensation was received by the executive.

Disclosure of Policy. We support the proposal to have the listing standard require issuers to file all disclosures with respect to their compensation recovery policy in accordance with the requirements of the federal securities laws. We see no compelling reason to require this information only through issuer disclosure requirements or, alternatively, solely through a listing standard requirement. Rather than require listed issuers to file their mandated compensation recovery policy as an exhibit to their Exchange Act annual report, however, we recommend that the Commission take an approach similar to the disclosure of committee charters required by Item 407 of Regulation S-K. Under this approach, an issuer would be required to disclose in its definitive proxy or information statement whether a current copy of its compensation recovery policy is available to security holders on the issuer's web site, and if so, provide the issuer's web site address.

While we generally support the content and the timing of the disclosure contemplated by proposed Item 402(w) and the proposed amendment to Item 404 of Regulation S-K, because of the "no fault" nature of the compensation recovery policy trigger we do not support the proposal to require the identification of each individual executive officer from whom a listed issuer decided during the last completed fiscal year not to pursue recovery, or the identification of each individual from whom excess incentive-based compensation has been outstanding for 180 days or longer since the date the issuer determined the amount the individual owed. In the former case, we believe it is sufficient to simply indicate the number of executive officers from whom recovery has been forgone, the aggregate amount forgone, and the reasons why recovery was determined to be impracticable. In the latter case, we believe it is sufficient to simply indicate the number of executive officers from whom excess incentive-based compensation has been outstanding for 180 days or longer, as well as the dollar amount remaining due from each such individual.

Transition and Timing. We recommend that the Commission provide that the mandated compensation recovery policy apply only to erroneously-awarded compensation that is granted or awarded after an issuer adopts such a policy following the effective date of the listing standard of the applicable national securities exchange or association as approved by the Commission. We believe that requiring issuers to apply their mandated compensation recovery policy to erroneously-awarded compensation retroactively; that is, to incentive-

based compensation that is earned or vested as the result of achieving a financial reporting measure based on or derived from financial information for a period or periods that end on or after the effective date of the final version of Rule 10D-1 would be unfair and create needless complexity and uncertainty

* * *

We appreciate the opportunity to continue to participate in this process and respectfully request that the Commission consider our recommendations and suggestions. We are available to meet and discuss these comments or any questions the Commission and its staff may have, which may be directed to the individuals listed below.

Very truly yours,

_____

Jay H. Knight
Chair of the Federal Regulation of Securities Committee

Drafting Committee:

Mark A. Borges
C. Alex Bahn
Martha N. Steinman

32301241.2