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Via Electronic Submission

February 11, 2016

Mr. Brent J. Fields
Secretary

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

**Re: File No. S7-12-15
Release Nos. 33-9861; 34-75342; IC-31702
Listing Standards for Recovery of Erroneously Awarded
Compensation**

Dear Mr. Fields:

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 comments by the U.S. Securities and Exchange Commission (the "**Commission**") in the proposing release referenced above (the "**Proposing Release**"). As set forth in the Proposing Release, the Commission has 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 (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 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.

The Committee thanks the Commission for this opportunity to comment on the Proposing Release and the proposed amendments to its rules relating to the implementation of Section 954 of the Dodd-Frank Act.

Summary of Our Comments

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, which direct the national securities exchanges and associations to prohibit the listing of any security of an issuer that is not in compliance with the requirements of Section 10D(b), seek to strike a balance between the objectives of the compensation recovery policy contemplated by that provision 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.

While we support many facets of the proposals, we also 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. Before responding in detail to the questions posed in the Proposing Release, we summarize the key comments and recommendations set forth in this Comment Letter.¹

- **Issuers Subject to Rule.** We request the Commission 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-1 to 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.
- **Restatements Triggering Application of Policy.** We recommend that, for purposes of the final version of Rule 10D-1, the definition of an "accounting restatement" expressly state that the "process of revising

¹ Please note that while we provide responses to most of the questions set forth in the Proposing Release, we have not provided comment on each and every question. The Commission may assume that, in the case of these omitted questions, we intended not to provide a response to such question.

previously issued statements" is that process as required under applicable accounting standards. We believe this clarification is important because in the context of GAAP it will help ensure that the definition of a restatement in the relevant accounting standards does not apply to immaterial items.

While we support the proposal to treat the earlier of (i) the date an issuer's Board of Directors, a board committee, or the issuer's officers concludes that the issuer's previously issued financial statements contain a material error or (ii) 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 as "the date on which an issuer is required to prepare an accounting restatement," we do not support the inclusion within the description of the first of the two dates the phrase "or reasonably should have concluded." We believe that the use of this clause would add an element of subjectivity to the rule that would give rise to an unacceptable degree of uncertainty as to when an accounting restatement was required.

- **Executive Officers Subject to Policy.** We 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 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 believe that recovery should apply only to incentive-based compensation earned by individuals who were executive officers (as described in the preceding paragraph) 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 the proposed rule, we believe only compensation that is truly "incentive" in nature should be subject to the mandated compensation recovery policy. Accordingly, we 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.

- **Time Period Covered by Policy.** We support the proposal to define the three-year “look-back” period specified in Section 10D(b)(2) as the “three completed fiscal years immediately preceding the date that the issuer is required to prepare a restatement of its previously issued financial statements to correct a material error.”
- **Compensation Recovery Process.** We 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 country 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.
- **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.

Discussion

Generally, we support the use of a compensation recovery policy as a means of promoting corporate accountability, as well as ensuring that an issuer's executive officers are only paid amounts that have been actually earned. We believe that a well-designed compensation recovery policy is an important feature of a responsible corporate governance program. Since the enactment of the Sarbanes-Oxley Act of 2002,² the adoption of compensation recovery policies has increased almost every

² See Section 304 of the Sarbanes-Oxley Act of 2002, Pub. L. 107-204, 116 Stat. 745 (2002) (the "Sarbanes-Oxley Act").

year.³ While variations exist, the vast majority of these policies have been designed to extend the Sarbanes-Oxley Act model to a broader group of individuals and situations.

We believe that there are several key principles that should guide the design and operation of a compensation recovery policy:

- **Reinforce corporate objectives** – The mission of a corporation is to create long-term value for its owners and other stakeholders, primarily through sustained economic performance, effective risk management, and responsible leadership. A compensation recovery policy should reinforce the pursuit of each of these objectives.
- **Minimize risk of manipulation** – The financial and operational results of a corporation should not be susceptible to manipulation, particularly through the corporation's compensation program. A compensation recovery policy can mitigate this risk by providing for a right to recovery if these results have been manipulated as the result of misconduct or other deleterious behavior.
- **Ensure accountability for inappropriate behavior** – While appropriate sanctions should be imposed for any act (or omission) that damages the welfare or reputation of the organization, recovery of previously-paid amounts is a particularly effective way to hold individuals accountable in the event of malfeasance unrelated to a financial restatement, such as a violation of policy or a breach of an employment or post-employment covenant.
- **Prevent unjust enrichment** – A compensation recovery policy enables a corporation to recover amounts paid without regard to conduct if there is a financial restatement, and, as a result, more compensation was paid than otherwise would have been paid had the correct financial results been originally reported.

We further believe that these principles are best achieved by a “principles-based,” rather than a prescriptive, approach to the features of the mandated compensation recovery policy. However, as discussed in more detail in the body of this Comment Letter, under this approach, there should be sufficient latitude for an issuer’s Board of Directors to determine whether certain individuals should be subject to the compensation recovery policy, as well as the amount, timing, and means of recovery. We believe the Board of Directors, the members of which are elected to use their best judgment and act in the best interest of shareholders, is well-suited to carry out these

³ See, for example, Equilar, Inc., *Compensation & Governance Outlook 2016* (2015), at page 16: “From 2011 to 2015, the percentage of S&P 500 company proxies disclosing a clawback policy increased significantly, from 50.4% to 77.1%.”; The Clearbridge 100 Report, *Executive Compensation Policies* (Oct. 2014), at page 11: “91% of companies disclosed a clawback policy in 2014 which is a slight increase from 2013 (87%).”

responsibilities in a manner that is consistent with the purpose of Section 10D of the Exchange Act. In this regard, to ensure full transparency, we recommend that an issuer be required to disclose and explain each exercise of discretion so that shareholders can evaluate how a Board of Directors has chosen to address each situation involving potential recovery.

In our view, such an approach would provide the necessary flexibility to enforcing a mechanism that will, undoubtedly, have repercussions on multiple levels. In our experience, there will be numerous competing interests that will need to be addressed in any situation that ultimately leads to the recovery of previously-granted, earned, or paid compensation. The inevitable real-world variation in situations that may trigger a compensation recovery policy warrant a rule that ensures that the Board of Directors retains broad discretion to address the circumstances that led to the financial restatement (thereby triggering the policy) and fashion a remedy that both furthers the principles summarized above and Congress' objectives.⁴

In this Comment Letter, we provide our comments and other observations on the proposed rules, recommend several alternatives which we believe are consistent with the foregoing discussion, and respond to the Commission's request for comments.

A. Issuers and Securities Subject to Proposed Exchange Act Rule 10D-1

1. General

1. Should the listing standards and other requirements of the proposed rule and rule amendments apply generally to all listed issuers, as proposed? If not, what types of issuers should be exempted, and why? Please explain the rationale that justifies exempting any particular category of issuer.

The Commission is proposing to apply proposed Rule 10D-1 to smaller reporting companies,⁵ emerging growth companies,⁶ and foreign private issuers.⁷ In the

⁴ We note that many existing compensation recovery policies empower the Board of Directors with broad discretion to determine whether recovery is in an issuer's best interests and, if so, to determine the amount, timing, and means of recovery.

⁵ Exchange Act Rule 12b-2 [17 CFR 240.12b-2] defines the term "smaller reporting company" as "an issuer that is not an investment company, an asset-backed issuer . . ., or a majority-owned subsidiary of a parent that is not a smaller reporting company and that: (1) had a public float of less than \$75 million as of the last business day of its most recently completed second fiscal quarter, computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates by the price at which the common equity was last sold, or the average of the bid and asked prices of common equity, in the principal market for the common equity; or (2) in the case of an initial registration statement under the Securities Act or Exchange Act for shares of its common equity, had a public float of less than \$75 million as of a date within 30 days of the date of the filing of the registration statement, computed by multiplying the aggregate worldwide number of such shares held by non-affiliates before the registration plus, in the case of a Securities Act registration statement, the number of such shares included in the registration statement by the estimated public offering price of the shares; or (3) in the case of an issuer whose public float as calculated under paragraph (1) or (2) of this definition

Proposing Release, the Commission states that it chose not to exempt categories of listed issuers, such as emerging growth companies, smaller reporting companies, and foreign private issuers "because we believe the objective of recovering excess incentive-based compensation is as relevant for these categories of listed issuers as for any other listed issuer."⁸

Notwithstanding the Commission's belief that that shareholders of smaller reporting companies, emerging growth companies, and foreign private issuers that are listed on a national securities exchange or association would benefit from a policy to recover erroneously-awarded compensation and that applying the proposed rule to these issuers will further the statutory goal of assuring that executive officers do not retain incentive-based compensation that they received erroneously, we do not support the application of proposed Rule 10D-1 to such issuers. Accordingly, we request the Commission exercise its general exemptive authority under the Exchange Act⁹ to exempt such 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 extending proposed Rule 10D-1 to such issuers would impose costs and burdens that are disproportionate to the benefits to be obtained from extending the recovery and disclosure requirements of the proposed rule to such issuers.¹⁰ The Commission has a long history of sensitivity to the costs and burdens faced by smaller reporting companies in complying with the federal securities laws. Most recently, to encourage capital formation and stimulate the U.S. economy, Congress

was zero, had annual revenues of less than \$50 million during the most recently completed fiscal year for which audited financial statements are available."

⁶ Section 2(a)(19) of the Securities Act of 1933 (the "Securities Act") [15 U.S.C. 77b(a)19] and Section 3(a)(80) of the Exchange Act [15 U.S.C. 78c(a)(80)] define the term "emerging growth company" as "an issuer that had total annual gross revenues of less than \$1,000,000,000 . . . during its most recently completed fiscal year." An issuer continues to be deemed an emerging growth company until the earliest of (i) the last day of the fiscal year during which it had total annual gross revenues of \$1 billion; (ii) the last day of the fiscal year following the fifth anniversary of the first sale of its common equity securities; (iii) the date on which it has issued more than \$1 billion in non-convertible debt during the previous three years; or (iv) the date on which it is deemed a large accelerated filer.

⁷ Exchange Act Rule 3b-4(c) [17 CFR 240.3b-4(c)] defines the term "foreign private issuer" as "any foreign issuer other than a foreign government except for an issuer meeting the following conditions as of the last business day of its most recently completed second fiscal quarter: (1) more than 50 percent of the issuer's outstanding voting securities are directly or indirectly held of record by residents of the United States; and (2) (i) the majority of the executive officers or directors are United States citizens or residents, (ii) more than 50 percent of the assets of the issuer are located in the United States, or (iii) the business of the issuer is administered principally in the United States." Exchange Act Rule 3b-4(b) defines "foreign issuer" as "any issuer which is a foreign government, a national of any foreign country or a corporation or other organization incorporated or organized under the laws of any foreign country."

⁸ See the Proposing Release, at Section II.A.1.

⁹ See Section 36(a)(1) of the Exchange Act [15 U.S.C. 78mm(a)(1)].

¹⁰ We note that the Commission itself acknowledges that the proposed listing standards could, in certain respects, impose a disproportionate burden on, among others, smaller reporting companies and emerging growth companies. See the Proposing Release, at Section II.A.1.

has seen fit to exempt an entire category of companies – emerging growth companies – from many of the registration and reporting requirements of the federal securities laws pursuant to The Jumpstart Our Business Startups (“JOBS”) Act.¹¹ As the Commission recognizes in the Proposing Release, the JOBS Act expressly exempts emerging growth companies from several, although not all, of the provisions of Title IX of the Dodd-Frank Act, of which Section 954 is a part.¹²

In our experience, the majority of both smaller reporting companies and emerging growth companies eligible for the scaled disclosure requirements of Item 402 of Regulation S-K have taken advantage of this privilege when it comes to the disclosure of their executive compensation policies and practices.¹³ Accordingly, very few of these issuers provide a Compensation Discussion and Analysis. And, concomitantly, such issuers rarely, if ever, address the subject of their policy regarding the recovery of erroneously-paid compensation. In fact, it is entirely likely that many of these issuers may not even have a formal compensation recovery policy.

For this reason, as the Commission acknowledges in the Proposing Release,¹⁴ to the extent that implementation of proposed Rule 10D-1 entails fixed costs (which we believe they will), smaller reporting companies and emerging growth companies will incur a proportionally larger compliance burden than other issuers. Moreover, smaller reporting companies and emerging growth companies are less likely to be in the financial position to bear these costs. Further, depending on the vitality of their internal controls, the nature of their incentive-based compensation arrangements, the financial reporting measures used in these arrangements,¹⁵ and the number and situation of its executive officers subject to the compensation recovery policy, smaller reporting companies and emerging growth companies are likely to bear significant costs in enforcing a mandatory compensation recovery policy. In our view, imposing such costs and the associated regulatory burden on smaller reporting companies and emerging growth companies is at direct odds with the legislative purposes of the JOBS Act.¹⁶

¹¹ Pub. L. No. 112-106, 126 Stat. 306 (2012).

¹² Among these provisions are Section 951, the security holder vote on executive compensation disclosures, and Section 953(b), the Chief Executive Officer pay ratio disclosure. See Section 102(a)(1) of the JOBS Act.

¹³ In this regard, we note that the proposed rules do not provide any form of relief for smaller reporting companies or emerging growth companies, whether it be scaled disclosure, a “phase-in” period, or any other accommodation.

¹⁴ See the Proposing Release, at Section III.B.3.

¹⁵ Particularly if the financial performance measure involves stock price or total shareholder return. See the Proposing Release, at Section III.B.2.

¹⁶ We note that the Advisory Committee on Small and Emerging Companies has recommended that the Commission (i) revise the definition of “smaller reporting company” to include companies with a public float of up to \$250 million and (ii) revise its rules to provide smaller reporting companies with the same disclosure accommodations that are available to emerging growth companies. See the Letter from the Securities and Exchange Commission Advisory Committee on Small and Emerging Companies to the Honorable Mary Jo White, Chair, U.S. Securities and Exchange Commission dated September 23, 2015.

We also note that newly-public issuers, which encompasses most emerging growth companies as well as many smaller reporting companies tend to have fairly simple long-term incentive compensation arrangements and, often, grant few, if any, performance-based compensation awards. We believe that requiring such issuers to comply with the proposed rule may discourage them from introducing such awards into their executive compensation program to minimize the impact of their mandated compensation recovery policy. Even where not so discouraged, we believe that these awards will incent such issuers to use performance measures that minimize the impact of the mandated policy. As the Commission notes in the Proposing Release, any such behavior may result in the executive compensation packages of such issuers' executive officers becoming less sensitive to their financial performance, creating a divergence in the interests of such individuals from those of the issuers' shareholders.¹⁷

For these reasons, we believe that subjecting smaller reporting companies and emerging growth companies to the listing standards contemplated by proposed Rule 10D-1 would impose unreasonable costs on such companies and potentially undermine the Congressional objective underlying JOBS Act disclosure relief for emerging growth companies.

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.¹⁸ We agree with other commenters that such deference should be afforded to foreign private issuers in the case of the proposed rule.¹⁹ In other words, we believe that the general presumption against the extra-territorial application of United States law absent an express statutory directive, as well as the general principle of international comity, should be extended to proposed Rule 10D-1.²⁰ Although proposed Rule 10D-1 does contain exemptive relief for foreign private

¹⁷ See the Proposing Release, at Section III.A. Further, to the extent that executive officers respond negatively to the expected effects of the mandated compensation recovery policies, the proposed rules may cause affected issuers to be less able to attract and retain executive talent, a particularly acute need for smaller reporting companies and emerging growth companies.

¹⁸ Such exemptions cover, for example, the proxy and information statement requirements of Section 14 of the Exchange Act (see Exchange Act Rule 3a12-3(b) [17 CFR 240.3a12-3(b)]), the shareholder advisory vote on named executive officer compensation requirement of Section 14A of the Exchange Act (see Exchange Act Rule 14a-21 [17 CFR 240.14a-21]), and the final CEO pay ratio rule and the proposed pay versus performance rules under Section 953 of the Dodd-Frank Act (see Pay Ratio Disclosure, 80 Fed. Reg. at 50104 (August 18, 2015) and Pay Versus Performance, 80 Fed. Reg. at 26330 (May 7, 2015)). We note that foreign private issuers are not required to provide the CEO pay ratio disclosure under Item 402(u) of Regulation S-K and, as proposed, would not be required to provide pay versus performance disclosure under proposed Item 402(v)[, in each case, because securities registered by such issuers are not subject to the proxy statement requirements of the Exchange Act].

¹⁹ See the Letter of Sullivan & Cromwell LLP dated September 22, 2015, at page 4: "[A] adopting prescriptive rules relating to a foreign private issuer's clawback policies could affect the governance structures of foreign entities by 'injecting US corporate governance theory into foreign countries via a US listing standard.'"

²⁰ We note that foreign private issuers are also exempt from several of the corporate governance-related listing standards of the national securities exchanges provided that they disclose the significant

issuers, that relief is available only in a very narrowly prescribed situation and within the overall framework of applying the mandatory compensation recovery policy to such issuers.²¹

Alternatively, should the Commission ultimately decide to apply proposed Rule 10D-1 to all listed issuers, we request that it provide additional time for smaller reporting companies, emerging growth companies, and foreign private issuers to adopt a compliant compensation recovery policy. Specifically, instead of the 60-day period from the effective date of the applicable listing standard as currently proposed, we recommend that such issuers be given at least two years from the effective date of the applicable listing standard within which to adopt the policy required by proposed Rule 10D-1.

2. Should we distinguish among listed issuers based on the types of securities listed? Please explain the rationale for any such exemption. For example, do issuers with listed non-convertible debt or preferred stock that do not have listed common equity raise the same concerns as issuers with listed common equity? For listed issuers that do not have listed common equity, do the different residual claims against the cash flows of the issuer warrant a different treatment?

We recommend that the Commission exempt from the required listing standards issuers that have only non-convertible debt listed on a national securities exchange or association and that do not also have listed equity securities. In our experience, holders of listed non-convertible debt assume the risk of a financial restatement when making their investment decision (which is reflected in the bond's rating and coupon). Further, unless the information is expressly set forth in the indenture, they may not even be aware of the design, terms, or conditions of the issuer's executive compensation arrangements; matters over which they have no control or influence.²²

On a more practical level, we also note that issuers that have only non-convertible debt listed on a national securities exchange or association and that do not also have listed equity securities are not subject to Section 16 of the Exchange Act.²³ Consequently, these issuers have not necessarily designated their executive officers using the approach required by Exchange Act Rule 16a-1(f).²⁴ In our view, they would

differences, if any, in which their corporate governance practices differ from those applicable to domestic U.S. issuers listed on these exchanges.

²¹ Proposed Rule 10D-1(b)(1)(iv) provides that foreign private issuers may forgo recovery of erroneously-awarded compensation if recovery would violate home country law.

²² See the Letter of The Society of Corporate Secretaries & Governance Professionals dated September 18, 2015, at page 11: "Requiring debt-only issuers to recoup incentive compensation upon a restatement, as proposed, is tantamount to adding a contractual provision for which the issuer does not receive consideration."

²³ 15 U.S.C. 78p.

²⁴ 17 CFR 240.16a-1(f).

face novel challenges in identifying their executive officers for purposes of proposed Rule 10D-1. Under these circumstances, we believe that it is neither necessary nor appropriate to subject issuers of listed non-convertible debt securities whose equity securities are not also listed to the proposed listing standards to the final version of Rule 10D-1.

3. Would the proposed listing standards conflict with any home country laws, stock exchange requirements, or corporate governance arrangements that apply to foreign private issuers? If so, please explain the nature of those conflicts. Should the proposed rule and rule amendments allow exchanges to permit foreign private issuers to forego recovery of erroneously awarded compensation if recovery would violate the home country's laws and certain conditions were met, as proposed? Is such an exception necessary or appropriate? If no, why not? If not are there more appropriate or effective means to address such conflicts?

While, as discussed in our response to Question 1 above, we recommend that foreign private issuers be exempted from the final version of Rule 10D-1 entirely, should the Commission decide that such a blanket exemption is unwarranted, we support its proposal to permit foreign private issuers to forego recovery of erroneously-awarded compensation if recovery would violate an issuer's home country laws.²⁵ Where recovery would subject a foreign private issuer to litigation, either by the applicable regulator or the subject executive officer, we believe that it is not in the best interests of the issuer or its shareholders to compel the issuer to pursue such recovery or risk its listing status. While the number of jurisdictions with such laws at any particular point in time may be small, over time changes in local laws or regulations may create substantial impediments to the enforcement of a compensation recovery policy in jurisdictions outside the United States.

We believe that foreign private issuers should have the certainty of knowing whether the location of an executive officer in a foreign country will affect the enforceability of their compensation recovery policy so that this can be taken into consideration when determining the compensation arrangements for such executive officer, as well as assessing the potential compliance costs associated with the policy.

However, we do not support the proposal that would limit the use of the home country laws exemption to situations where the subject law was in effect as of July 14, 2015.²⁶ We are not persuaded by the Commission's concern that, absent such a limitation, foreign countries will be motivated by the exemption to change their laws, presumably to entice issuers to relocate in that jurisdiction based solely on the

²⁵ See proposed Rule 10D-1(b)(1)(iv). As the Commission notes in the Proposing Release, certain exchange listing standards already permit foreign private issuers to follow home country practice in lieu of certain corporate governance requirements (see, for example, New York Stock Exchange Rule 303A.00 and NASDAQ Stock Market LLC Rule 5615(a)(3)). See the Proposing Release, at footnote 34 and the accompanying text.

²⁶ See the Proposing Release, at Section II.C.3.b.

opportunity to avoid having to adopt the mandated compensation recovery policy. Given that many jurisdictions follow the lead of the United States in the development and adoption of appropriate corporate governance standards, we believe that it is unfair to penalize an issuer because it happens to be located in a jurisdiction that has not had the foresight to adopt a law or regulation governing the recovery of erroneously-awarded compensation ahead of the Commission's own timetable from implementing such a requirement.

4. In the event that a foreign private issuer's home country has a law that like Section 10D requires the issuer to disclose its policies on incentive-based compensation and recover erroneously awarded incentive-based compensation from current or former executive officers, should the foreign private issuer be permitted to comply with its home country law instead of complying with the listing standard of the U.S. exchange that lists the foreign private issuer's securities? Please explain why or why not.

While, as discussed in our response to Question 1 above, we recommend that foreign private issuers be exempted from the final version of Rule 10D-1 entirely, should the Commission decide that such a blanket exemption is unwarranted, we support the concept of permitting a foreign private issuer to comply with any home country law that is similar to Section 10D of the Exchange Act that requires the issuer to disclose its policies on incentive-based compensation and recover erroneously-awarded incentive-based compensation from current or former executive officers instead of complying with the listing standard of the national securities exchange or association on which its securities are listed. To do otherwise would result in an unreasonable lack of comity towards the home country laws of the issuer²⁷ and could serve as a disincentive for foreign private issuers to seek the listing of a class of their securities in the United States.

Equally important, since foreign private issuers generally adhere to the accounting requirements set forth in the International Financial Reporting Standards, which, as the Commission notes in the Proposing Release, set forth criteria for determining when an accounting restatement is required that differ from generally accepted accounting principles in the United States, the application of proposed Rule 10D-1 to such issuers may lead to inconsistent treatment among issuers and likely investor confusion.

* * *

²⁷ We are concerned that the application of a compensation-related policy to an issuer domiciled in a foreign jurisdiction through a United States-based listing standard may be perceived as an inappropriate extension of the standard.

2. Securities Futures Products and Standardized Options

6. Are our proposed exemptions for listing securities futures products and standardized options appropriate? Why or why not?

We support the Commission's proposed exemption for securities futures products that are cleared by a clearing agency that is registered pursuant to Section 17A of the Exchange Act²⁸ or that are exempt from the registration requirements of Section 17A(b)(7)(A)²⁹ and standardized options (as defined in Exchange Act Rule 9b-1(a)(4)),³⁰ which are issued by a clearing agency that is registered pursuant to Section 17A.³¹ As the Commission notes in the Proposing Release, the purchaser of security futures products and standardized options does not, except in the most formal sense, make an investment decision regarding the clearing agency. As a result, information about the clearing agency's business, its executive officers and directors and their compensation, and its financial statements is less relevant to investors in these securities than information about the issuer of the underlying security.³²

In addition, the investment risk in security futures products and standardized options is largely determined by the market performance of the underlying security rather than the performance of the clearing agency.³³ For the reasons that these securities have been exempted from Exchange Act Rules 10A-3³⁴ and 10C-1,³⁵ and because any relationship between any incentive-based compensation that the clearing agency pays its executive officers and its financial statements would not be significant to investors in these futures and options, they should be similarly exempted from the final version of Rule 10D-1.

* * *

B. Restatements

1. Restatements Triggering Application of Recovery Policy

12. For purposes of proposed Rule 10D-1, an accounting restatement would be defined as the result of the process of revising previously issued financial statements to correct errors that are material to those financial statements.

²⁸ 15 U.S.C. 78q-1.

²⁹ 15 U.S.C. 78q-1(b)(7)(A).

³⁰ 17 CFR 240.9b-1(a)(4).

³¹ See proposed Rule 10D-1(b)(2).

³² See the Proposing Release, at Section II.A.2.

³³ *Id.*

³⁴ See Exchange Act Rules 10A-3(c)(4) and (5) [(17 CFR 240.10A-3(c)(4) and (5))].

³⁵ See Exchange Act Rules 10C-1(b)(5)(iii) and (iv) [(17 CFR 240.10C-1(b)(5)(iii) and (iv))].

Rather than including this definition in our proposed rule, should we refer to the definition of “restatement” in GAAP? If we do not refer to the definition in GAAP, is it appropriate to include in the proposed definition the phrase “errors that are material” or might it be confusing or redundant? Is our proposed approach the appropriate means to implement Section 10D, including its “material noncompliance” provision?

As proposed, an accounting restatement would be defined as “the result of the process of revising previously issued financial statements to reflect the correction of one or more errors that are material to those financial statements.”³⁶ We believe that, for purposes of the final version of Rule 10D-1, this definition should expressly state that the “process of revising previously issued statements” is that process *as required under applicable accounting standards*. Although the concept that a restatement is to occur in accordance with applicable accounting standards is present in the Proposing Release,³⁷ we believe it should be set forth in the definition itself for sake of clarity. We believe this clarification is important because in the context of generally accepted accounting principles in the United States (“GAAP”), for example, it will help ensure that the definition of a restatement in ASC 250-10-20 is read together with ASC 105-10-05-6, the provision in the Codification which makes clear that the application of ASC 250-10-20 does not apply to immaterial terms. Accordingly, we recommend that the definition of “accounting restatement” in the final version of Rule 10D-1(c)(1) should read as follows:

(1) Accounting restatement. For purposes of this rule, an accounting restatement occurs when the issuer is required by applicable accounting standards to issue restated financial statements to correct one or more errors that are material to those previously issued financial statements.

We also note that, in the Proposing Release, the Commission states that “issuers should consider whether a series of immaterial error corrections, whether or not they resulted in filing amendments to previously filed financial statements, could be considered a material error when viewed in the aggregate.”³⁸ To avoid any uncertainty with respect to when the accumulation of such errors would be considered a material error requiring an accounting restatement that will trigger the compensation recovery policy, as well as potential uncertainty regarding its timing, we recommend that the Commission clarify the circumstances in which a restatement would be required for purposes of the final version of Rule 10D-1. Specifically, we recommend that the Commission expressly confirm that compensation recovery is triggered only if, following the aggregation of a series of immaterial errors, an issuer is required, under GAAP, to

³⁶ Proposed Rule 10D-1(c)(1).

³⁷ See the Proposing Release, at Section II.B.1.

³⁸ *Id.*

prepare a financial restatement to correct a material error of the type required to be reported under Item 4.02(a) of Form 8-K.³⁹

Finally, we recommend that the Commission confirm in the final version of Rule 10D-1 that:

- Certain accounting restatements may not always require a recovery of incentive-based compensation based on stock price or total shareholder return ("TSR"). We note that at least one major United States accounting firm has observed that certain restatements may not affect stock price or TSR.⁴⁰ In the event that an issuer reasonably concludes that incentive-based compensation based on stock price or TSR would not have been affected by an accounting restatement, we believe that it should be clear that it is not required to recover any excess incentive-based compensation (since there was no such compensation).
- In the case where a relative financial reporting measure is used to determine the amount of incentive-based compensation that is granted, earned, or vested, a financial restatement by a member of the comparator group does not trigger recovery.

13. If an issuer evaluates whether certain errors are material, and concludes that such errors are immaterial or are not the result of material noncompliance, should the issuer disclose its evaluation? If so, what should be disclosed and where should such disclosure be required?

We believe that no issuer should be required to disclose its evaluation of any errors which it has concluded are not material or are not the result of material noncompliance. Issuers are required to make determinations of materiality in connection with many of their ongoing public disclosure obligations under the Exchange Act. As a general matter, issuers are not required to disclose, nor should they be required to disclose, their analyses on matters it has determined to be immaterial and, thus, not disclosed. Since immaterial data should be of no consequence to an investment decision, the inclusion of any such analysis would not be useful to investors.

Further, to require such disclosure would subject issuers to potential second-guessing of their determinations and, potentially, to costly and protracted litigation to

³⁹ As noted in the proposed rule itself in the case of when it is determined that an issuer's previously-issued financial statements contain a material error, this approach would be consistent with the date that is generally expected to coincide with the occurrence of the event described under Item 4.02(a) of Form 8-K [17 CFR 249.308]. See the Note to proposed Rule 10D-1(c)(2).

⁴⁰ See the letter of Ernst & Young LLP dated September 14, 2015, at page 3: "For example, restatements related to the measurement and recognition of financial assets and liabilities, the measurement of asset impairments and classification errors in the statement of cash flows often have limited if any impact on stock price or TSR."

defend their conclusions against spurious claims by plaintiffs.⁴¹ Any potential benefit to be obtained from such disclosure is grossly outweighed by the cost of defending against such claims and the preemptive need to prepare detailed and defensible summaries of such analysis. Instead, we believe the existing anti-fraud provisions of the Exchange Act provide sufficient impetus to issuers to disclose all material information, and to the extent that any prior financial reporting error is material, an issuer is thereby required to provide the appropriate disclosure including any restatement required by applicable GAAP. To require issuers to disclose their evaluation of errors they believe to be immaterial would be unduly burdensome and inconsistent with the existing practice under the federal securities laws.

14. Should any revision to previously issued financial statements that results in a reduction in incentive-based compensation received by an executive officer always trigger application of an issuer's recovery policy under the proposed listing standards? Why or why not?

An accounting restatement of previously-issued financial statements to correct one or more material errors in those financial statements is required by GAAP. Such a restatement will trigger application of an issuer's compensation recovery policy. Under Section 10D of the Exchange Act, this would result in a reduction of incentive-based compensation during the preceding three fiscal years. We believe that our responses to Questions 12 and 13 above are also instructive to this question. To the extent that an issuer revises financial statements to correct an error that it has concluded is immaterial, this revision should not result in application of the recovery policy. Application of the recovery policy to such revisions would be inconsistent with Section 10D and would impose burdens on management that would be disproportionate to any benefits of such an expansion of the recovery requirement, particularly given that the analysis of the materiality of an error takes into account the impact of the error on executive compensation.

15. As noted above, certain changes to the financial statements would not trigger recovery because they do not represent error corrections under the accounting standards. Are there any other types of changes to an issuer's financial statements that should not be deemed to trigger application of the issuer's recovery policy?

⁴¹ While it may be an open question as to whether the compensation recovery policy required by Section 10D of the Exchange Act may be enforced only by the Commission or by the issuer itself (directly or by a private plaintiff), if a court were to find a private right of action, issuers would likely encounter a wide range of litigation from private plaintiffs challenging various aspects of the operation of the policy, such as, for example, a Board of Directors' decision that recovery is "impracticable" or its calculation of the amount of erroneously-awarded compensation. Based on the language of Section 10D providing that "the issuer will recover" any excess incentive-based compensation, we read the statute to permit derivative litigation.

In the Proposing Release,⁴² the Commission lists six types of “changes” that do not represent corrections of errors and, thus, would not trigger application of an issuer’s compensation recovery policy. A GAAP change in an accounting estimate is defined as an “Accounting Change” in ASC 250-10-20, but was not included in this list of “changes.” A change in an accounting estimate (which is not a correction of an error under ASC 250-10-20 and ASC 250-10-45-17 through 20) may never cause a restatement of financial statements, and, accordingly, should be included in the list of “changes” to an issuer’s financial statements that will not be deemed to trigger application of the issuer’s compensation recovery policy.

16. Should the proposed listing standards contain any anti-evasion language regarding the circumstances in which recovery would be triggered? If so, what should the language provide?

We have not identified any “anti-evasion” language that we believe would improve or otherwise clarify the accounting treatments addressed in our responses to Questions 12 through 15 above.

2. Date the Issuer Is Required to Prepare an Accounting Restatement

17. Is it appropriate to treat the earlier of the two proposed dates as “the date on which an issuer is required to prepare an accounting restatement” for purposes of triggering the Section 10D recovery obligation? If not, why not? Would using these dates provide sufficient certainty and transparency for issuers, investors and exchanges to determine when recovery would be triggered for purposes of compliance with the proposed listing standards? Are there additional triggers we should consider including?

The Commission has proposed that the date on which an issuer is required to prepare an accounting restatement will be the earlier to occur of:

- “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, or reasonably should have concluded, that the issuer’s previously issued financial statements contain a material error; or
- 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.”⁴³

The Commission’s proposal to treat the earlier of such two dates as “the date on which an issuer is required to prepare an accounting restatement” (for purposes of this

⁴² See the Proposing Release, at Section II.B.1.

⁴³ See proposed Rule 10D-1(c)(2)(i) and (ii).

response, the "Trigger Date") is (subject to our comment below with regard to the description of the first of such two dates) appropriate as it allows the recovery to be triggered by events that most closely approximate the date such restatement has objectively been determined to be required. We also concur with the Commission's rationale for rejecting other proposed triggering dates, such as the date on which the erroneous filing is made and the date the issuer files the accounting restatement.

We believe, however, that it is inappropriate to include within the description of the first of the two dates the phrase "or reasonably should have concluded." By inserting that clause, the proposal has injected an element of subjectivity into the concept of the Trigger Date, which will give rise to the very uncertainty that the rule is intended to avoid. The Commission indicates in the Proposing Release that:

In considering how best to craft a trigger for recovery under the proposed listing standards, we have sought to define the date on which an accounting restatement is required in a way that provides reasonably certain for issuers, shareholders and exchanges while not permitting issuers to avoid recovery when a material error has occurred.⁴⁴

If that phrase were, as we hereby urge, to be deleted from the first of the two dates above, we believe the rule would then set forth two alternative, objective standards for the Trigger Date that help to assure certainty in the application of the requirement. As proposed, however, we anticipate that the inclusion of such language in the first alternative (that is, the date that the Board of Directors, committee of the Board of Directors, or officers "reasonably should have concluded" that the issuer's prior financial statements contain a material error) could render the second alternative date (that is, 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) irrelevant, as the first alternative would likely always be deemed to precede any date that would otherwise arise under the second alternative. Further, the phrase would, we believe, act to ensure significant uncertainty about the applicable date as the decision by an issuer, its Board of Directors, or committee of the Board of Directors, or relevant officers would be subject to claims that such decision should have been made before or after the actual occurrence of such decision.

We also note that other existing laws, including the certification requirements and anti-fraud provisions of the Exchange Act as well as applicable corporate law, provide the appropriate incentives to an issuer, its Board of Directors, and relevant officers to make timely financial reporting determinations in connection with SEC filings, including with respect to the materiality of error corrections.

18. Should receipt of a notice from a company's independent auditor that previously issued financial statements contain a material error constitute a date when the issuer "reasonably should have concluded" that such

⁴⁴ See the Proposing Release, at Section II.B.2.

statements contain a material error? Why or why not? What if the issuer disagrees with the auditor's conclusion?

The receipt of a notice from an issuer's independent auditor that previously issued financial statements contain a material error should not constitute a date when the issuer "reasonably should have concluded" that such statements contain a material error. In our view, to treat any such notice or similar auditor communication to trigger the required look-back period would be premature. The financial statements, although audited by an independent auditor, remain the financial statements of the relevant issuer, and not the auditor. Consequently, while any such notice or other communication from an issuer's auditor is part of the process in evaluating the magnitude of an error and, of course, should be considered carefully by the issuer, the ultimate determination of the need for a restatement to correct a material error should be made by the issuer.

19. Are there other means of defining the date on which an issuer is required to prepare an accounting restatement that would provide clear benchmarks that do not inject subjectivity into when recovery would be triggered? If so, how should the date on which the issuer is required to prepare a restatement be defined?

Subject to our responses to Questions 17 and 18 above with regard to the phrase "or reasonably should have concluded" within the first alternative date, we believe that the earlier of the two alternative dates within the proposed definition of the date on which an issuer is required to prepare an accounting restatement is the most objective date that is consistent with the plain meaning of the language of Section 954.

C. Application of Recovery Policy

1. Executive Officers Subject to Recovery Policy

20. Consistent with the Rule 16a-1(f) definition of "officer", should we define "executive officers" to expressly include the principal financial officer and the principal accounting officer (or if there is no such accounting officer, the controller), as proposed?

Please see our response to Question 23 below.

21. Are there any other officers, such as the chief legal officer, chief information officer, or such other officer, who by virtue of their position should be specifically named as executive officers subject to the issuer's recovery policy? If so, which additional officers should be subject to the issuer's recovery policy and why?

Please see our response to Question 23 below.

22. Are there any other officers who should be included in the group of executive officers subject to the issuer's recovery policy, but who may not fall within the proposed definition? Is the definition of executive officer appropriate? If not, how else should executive officer be defined?

Please see our response to Question 23 below.

23. Alternatively, is the proposed definition of "executive officer" too broad? Should we instead limit the recovery policy to "named executive officers," as defined in Items 402(a)(3) and 402(m)(2) of Regulation S-K or otherwise define a more narrow set of officers subject to recovery?

If proposed Rule 10D-1 is adopted in its current form, the required compensation recovery policy would apply on a "no-fault" basis to all current and former executive officers who served in such a capacity at any time during the proposed three-year look-back period. For this purpose, the Commission is proposing to define the term "executive officer" in a manner that is substantively consistent with the definition of the term "officer" in Exchange Act Rule 16a-1(f).⁴⁵ We believe that the combination of the "no-fault" basis for the recovery trigger and the expansive scope of the proposed definition of who should be subject to the compensation recovery policy is inconsistent with the purpose of Section 954 and would lead, in many instances, to unfair and inappropriate results.

As proposed, the mandated compensation recovery policy would apply to individuals who undoubtedly play a significant role in, or have responsibility for, the preparation of an issuer's financial statements, such as its president, principal financial officer, and principal accounting officer (or the controller, if there is none). As to these individuals, proposed Rule 10D-1 would clearly serve the objectives of Section 954 by promoting the preparation of complete and accurate financial statements, eliminating any incentive to manipulate financial results, and penalizing bad behavior.

As proposed, however, the definition of the term "executive officer" would also include individuals who may have no meaningful role in the preparation of an issuer's financial statements, such as a vice-president in charge of a principal business unit, division, or function.⁴⁶ While a vice-president in charge of administration may be a very important role within an issuer's business and while it may be entirely appropriate to have such a position be subject to Section 16, it is questionable whether the individual serving in such a role has any meaningful impact on the preparation of the issuer's financial statements. Accordingly, applying the mandated compensation recovery policy to an individual whose functional responsibility or business unit has no influence or

⁴⁵ See proposed Rule 10D-1(c)(3).

⁴⁶ This aspect of the proposed definition could encompass individuals in such areas as administration, human resources, marketing, investor relations, information technology, legal and compliance, research and development, and other areas that do not directly involve financial reporting and/or the maintenance of internal controls over financial reporting.

basis regarding the financial reporting error which has led to the need for a financial restatement would result in compensation forfeitures that could deprive these individuals of earned compensation merely because they have access to the type of information that makes them a “corporate insider.” Thus, except as explained hereafter, we believe the purpose of Section 10D would not be furthered by applying proposed Rule 10D-1 to individuals whose roles are divorced from the preparation of – or responsibility for – the issuer’s financial statements.

Consequently, we believe it is most appropriate for the term “executive officer” in proposed Rule 10D-1 to cover those officers of an issuer who have had a role in preparing the issuer’s financial statements or who played a significant role in the events leading to the restatement. Consequently, we propose to define the term “executive officer” to include an issuer’s principal executive officer, principal financial officer, and chief accounting officer (or if there is no such accounting officer, the controller). In addition, we recommend that individuals who are executive officers of the issuer and who also played a significant role in the events leading to the financial restatement also be subject to the final version of Rule 10D-1. Specifically, we recommend the Commission define the term “executive officer” to include the individuals identified above as well as 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.⁴⁷

We believe this definition would focus the compensation recovery policy on those individuals who are expected to have the greatest impact on the preparation of the issuer’s financial statements. We believe that using clearly identifiable titles will assist issuers in ensuring they are able to track and monitor the individuals from whom recovery may be required, including the amounts that are paid over the possible recovery period.

This approach would ensure that these individuals would not escape responsibility when their actions (or failure to act) may have contributed to the underlying events that ultimately led to the material error that resulted in the financial restatement. We believe that including these individuals within the ambit of the final version of Rule 10D-1 would serve the objectives of Section 10D by penalizing bad behavior (to the extent that their actions were culpable) and preventing the realization of unearned benefits at the expense of shareholders. Since this category of executive officers necessarily would cover individuals who do not, by virtue of their position or title, play a significant role in, or have responsibility for, the preparation of an issuer’s financial statements, their identification would have to be conducted by the issuer’s Board of Directors, based on all the relevant facts and circumstances. We believe that, consistent with its fiduciary obligations, the Board of Directors should be permitted the

⁴⁷ For additional support for this recommendation, see the letter of The Society of Corporate Secretaries & Governance Professionals dated September 18, 2015.

discretion to assume this responsibility.⁴⁸ Further, we believe that such a role would not be inconsistent with the mandatory nature of Section 10D as the Board of Directors would be required to enforce the issuer's compensation recovery policy, but only against individuals who bore an actual nexus to the financial restatement.

Finally, we do not support limiting the definition of the term "executive officer" to only an issuer's "named executive officers." As provided in Item 402 of Regulation S-K, the determination of an issuer's named executive officers (other than its principal executive officer and principal financial officer) relies entirely on the amount of total compensation of the issuer's executive officers who were serving as executive officers at the end of the last completed fiscal year.⁴⁹ Such a definition bears no rational link to an issuer's financial functions and, accordingly, would be as arbitrary a standard as the current proposed definition.

24. Will the scope of the term "executive officer" for purposes of Section 10D affect issuers' practices in identifying executive officers for other purposes? If so, how, and what if anything should we do to address that? Are there other means of simplifying the identification of "executive officers" for purposes of Rule 10D-1 that would promote consistency with identifying executive officers for other purposes, such as Item 401(b) of Regulation S-K? Is there another, more appropriate definition?

In our experience, for purposes of compliance with Exchange Act Rule 3b-7⁵⁰ and Section 16 of the Exchange Act,⁵¹ most Boards of Directors make an annual determination of the individuals who should be considered "executive officers" and that determination creates a presumption for purposes of Section 16.⁵² We note that proposed Rule 10D-1(c)(3)⁵³ is intended to create a similar presumption with respect to the individuals identified as executive officers in an issuer's annual report on Form 10-K or its proxy or information statement.⁵⁴ We believe that the proposed definition of

⁴⁸ While we recognize that the use of the term "significant" introduces a degree of subjectivity into a Board of Directors determination of whether an executive officer's actions would be sufficient to subject him or her to potential recovery of incentive-based compensation, we note that proposed Rule 10D-1 itself (by referencing the Section 16 approach) includes a similar degree of subjectivity within the context of determining whether an officer is a "policy maker" who would be subject to the issuer's compensation recovery policy. See the Note to proposed Rule 10D-1(c)(3): "Policy-making function is not intended to include policy-making functions that are not significant." Thus, we believe that issuers have sufficient experience in applying the "significant" standard in other contexts that may be helpful in making determinations for purposes of Rule 10D-1.

⁴⁹ See Item 402(a)(3)(iii) of Regulation S-K [17 CFR 229.402(a)(3)(iii)].

⁵⁰ 17 CFR 240.3b-7.

⁵¹ 15 U.S.C. 78p.

⁵² See the Note to Exchange Act Rule 16a-1(f) [17 CFR 240.16a-1(f) Note].

⁵³ See the Note to proposed Rule 10D-1(c)(3).

⁵⁴ See Item 401(b) of Regulation S-K [17 CFR 229.401(b)].

“executive officer” is likely to impact issuers’ practices in identifying their executive officers.

By employing a definition that parallels an issuer’s determination of its executive officers who are subject to Section 16, we are concerned that some issuers would have an incentive to reevaluate the previous identification of their “corporate insiders” to see whether they should reduce the number of individuals subject to those rules – particularly where the individual has little or no responsibility for accounting and finance matters. In our experience, some issuers have tended to be liberal in identifying the individuals who will be subject to Section 16, thus resulting in a larger group of Section 16 officers than had an issuer taken a more conservative view. Frequently, familiarity with the reporting and liability requirements of Section 16 have outweighed any concerns about an inadvertent “short-swing profits” disgorgement and have resulted in the identification of a larger group of “corporate insiders” than may otherwise have been necessary. We are concerned that the potential broad application of the mandated compensation recovery policy may give issuers a more substantive reason to reevaluate their Section 16 determinations.

25. Is it consistent with the purposes of Section 10D to apply recovery to any incentive-based compensation earned during the three completed fiscal years immediately preceding the date that the issuer is required to prepare a restatement if that person served as an executive officer at any time during the performance period? Alternatively, should an individual be subject to recovery only for incentive-based compensation earned during the portion of the performance period during which the individual was serving as an executive officer? Should an individual who is an executive officer at the time recovery is required be subject to recovery even if that individual did not serve as an executive officer of the issuer at any time during the performance period for the affected incentive-based compensation? If a different standard should govern the circumstances when an executive officer or former executive officer is subject to recovery, what should that standard be, and why should it apply?

We do not support the Commission’s proposal to require recovery of any incentive-based compensation earned during the three completed fiscal years immediately preceding the date that an issuer is required to prepare a financial restatement (the “Look-Back Period”) from any individual who served as an executive officer of the issuer *at any time* during the performance period. We believe that such a requirement is overly broad.

We believe that the final version of Rule 10D-1 should require recovery of incentive-based compensation that was earned during the Look-Back Period, but only during such portion or portions of the period in which the individual served as an executive officer. For example, if an individual were designated an executive officer during the second year of the Look-Back Period, but was not an executive officer of the issuer at any time during years one or three, we believe that it would be inappropriate

to require recovery of any portion of the incentive-based compensation that was earned in years one and three, as the compensation earned in those years was not earned in the individual's capacity as an executive officer.

We believe that such a result is consistent with a careful reading of Section 10D of the Exchange Act. While we acknowledge Section 10D(b)(2) refers to recovery from "any current or former executive officer . . . during the 3-year period preceding" the financial restatement that triggered the compensation recovery policy, we believe the reference to "former" is not intended to mean that incentive-based compensation earned at any point during the performance period is subject to recovery. Rather, we believe the reference to "former" is simply intended to capture individuals who earned incentive-based compensation in their capacity as an executive officer during the Look-Back Period, even if the individual is no longer serving as an executive officer of the issuer at the time of recovery.

In addition, we believe that the final version of Rule 10D-1 should apply only to an individual who served as an executive officer during the applicable Look-Back Period, even if that individual is serving as an executive officer of the issuer at the time recovery is required. We believe this position is consistent with the language of Section 10D(b)(2), which requires recovery of incentive-based compensation that is "in excess of what would have been paid to the executive officer under the accounting restatement." We interpret this language to mean that if the incentive-based compensation at issue was not paid to an individual who was an "executive officer" during the Look-Back Period, recovery should not be compelled from that individual.

2. Incentive-Based Compensation

a. Incentive-Based Compensation Subject to Recovery Policy

26. Is the scope of incentive based compensation subject to recovery under Section 10D(b) properly defined by reference to compensation that is granted, earned or vested based wholly or in part upon attainment of any measure that is determined or presented in accordance with applicable accounting principles? If not, please explain what other forms of compensation should be covered and why.

For purposes of Section 10D of the Exchange Act, proposed Rule 10D-1 would define the term "incentive-based compensation" as "any compensation that is granted, earned or vested based wholly or in part upon the attainment of any financial reporting measure."⁵⁵ Given the "no-fault" nature of the proposed rule and its complexity in implementation, we find the scope of this proposed definition to be overly broad.

⁵⁵ Proposed Rule 10D-1(c)(4).

As a threshold matter, we believe that only compensation that is truly “incentive” compensation should be subject to the mandated compensation recovery policy. Further, we believe that, for this purpose, recoverable compensation should be limited to incentive-based compensation of the type that would be reportable in the Grants of Plan-Based Awards Table⁵⁶ and which is earned or vests based on the attainment of a financial reporting measure (as discussed in our response to Question 29 below). A principles-based approach to applying the rule will be difficult without such a limitation, particularly given the “wholly or in part” aspect of the definition.⁵⁷

In our view, the present disclosure requirements under Item 402 of Regulation S-K adequately define the types of compensation that should be considered “incentive-based compensation” for purposes of Section 10D: non-equity incentive plan awards as reported in columns (c) through (e) of the Grants of Plan-Based Awards Table pursuant to Item 402(d)(2)(iii) and equity incentive plan awards as reported in columns (f) through (h) of that table pursuant to Item 402(d)(2)(iv). In effect, only those awards “granted, earned or vested based wholly or in part upon any financial reporting measure” would be subject to recovery.

We believe defining the scope of “incentive-based compensation” in this manner is consistent with the language of Section 10D(b)(1). Further, it enhances principles-based implementation. Using the existing framework for the disclosure of executive compensation information would enable issuers to use their current processes for identifying such compensation. To satisfy their disclosure obligations, issuers currently articulate the basis for the decisions of their Board of Directors (or Compensation Committee) with respect to the grant of incentive awards and the vesting or earning and amounts payable upon the settlement of such awards, as well as the underlying rationale for such decisions. This creates a record upon which the assessment of whether, and if so what, incentive-based compensation has been granted, earned, or vested in whole or in part based on financial reporting measures may be made.

27. Is the proposed definition of “incentive-based compensation” the best means to capture all forms of compensation that could be subject to reduction if recalculated based on an accounting restatement? If not, please explain what other forms of compensation, which would not be covered by the proposed definition, should be covered.

Please see our response to Question 26 above.

28. Are there circumstances in which compensation that is received upon completion of a specified employment period or upon the attainment of any

⁵⁶ See Item 402(d) of Regulation S-K [17 CFR 229.402(d)].

⁵⁷ For example, as suggested in footnote 132 of the Proposing Release, base salary could be “incentive-based compensation” if the executive officer was awarded a raise wholly or in part based on attainment of a financial reporting measure. The Commission also suggests that the rule could apply to pension or other retirement plans if the benefits are calculated using incentive-based compensation as defined. See the Proposing Release, at Section II.C.3.a. at Question 47.

other goal that is not covered by our proposed definition should be considered incentive-based compensation subject to recovery? Why or why not? If so, how would an issuer calculate the recoverable amounts in the event of an accounting restatement? Are there any other measures of compensation that should be included in the definition of incentive-based compensation? If so, which ones and why?

Please see our response to Question 26 above. We do not believe there are other circumstances in which compensation that is received upon completion of a specified employment period or upon the attainment of any other non-financial goal should be considered "incentive-based compensation" for purposes of Section 10D.

29. Should compensation that is based upon stock price performance or total shareholder return be considered incentive-based compensation subject to recovery? If not, please explain why not. If compensation that is based on stock price performance or total shareholder return is included as incentive-based compensation subject to recovery, what calculations would need to be made to determine the recoverable amount? What are the costs and technical expertise required to prepare these calculations? Who would make these calculations for issuers? Would the costs be greater than for calculations tied to other financial reporting measures, which would be subject to mathematical recalculation directly from the information in an accounting restatement? Would the exchanges be able to efficiently assess these calculations for purposes of enforcing compliance with their listing standards? Why or why not? Should we require an independent third party to assess management's calculations?

We do not support the Commission's proposal to include stock price performance or total shareholder return ("TSR") as financial reporting measures for purposes of defining "incentive-based compensation" subject to recovery under the final version of Rule 10D-1. At the outset, we note that Section 10D of the Exchange Act expressly (and solely) applies to "incentive-based compensation that is based on financial information required to be reported under the securities laws."⁵⁸ It is axiomatic that an issuer's stock price and its TSR reflect many factors beyond its reported financial information. In our view, to equate stock price or TSR to reported financial information inappropriately expands the statutory mandate of Section 10D. Consequently, we recommend that the Commission delete these two items from the scope of the "financial reporting measures" used to define incentive-based compensation for purposes of Section 10D.⁵⁹

⁵⁸ See Section 10D(b)(2) of the Exchange Act.

⁵⁹ Even if the Commission ultimately disagrees with our approach for defining "incentive-based compensation" as described in our response to Question 26 above, we request that it delete these two items from the scope of what constitutes a "financial reporting measure."

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 proposed Rule 10D-1. At a minimum, determining the correct (or an appropriate) amount to recover when the incentive-based compensation has been granted, earned, or vested based, in whole or in part, on an issuer’s stock price or TSR will be significantly more difficult than making a similar determination where the compensation has been granted, earned, or vested based on a measure that is determined and presented in accordance with the accounting principles used to prepare the issuer’s financial statements,⁶⁰ as the relationship between these measures and their impact on an issuer’s common stock is, at best, indirect.

Where compensation is granted, earned, or vested based on stock price or TSR, the amount of erroneously-awarded compensation is not subject to mathematical recalculation directly from the information in an accounting restatement. As a result, it will be extremely challenging to estimate how much (if any) of a change in an issuer’s stock price or TSR is attributable to the restatement. That complexity is compounded when, in addition to the restatement, other events have occurred or been announced during the performance period that, as a practical matter, may have affected the issuer’s stock price or TSR. As many have argued, the reasons underlying movements in stock price and TSR are often speculative in nature and may have more to do with third-party events than with developments at the issuer, including a financial restatement.

Although we agree that permitting the use of “reasonable estimates” is one way to address these challenges, this potential “solution” is not without its own drawbacks. As the Commission notes, both in its explanation and economic analysis of the proposed rules and rule amendments, most issuers will need to engage third-party experts to assist (if not entirely provide) the needed calculations. This assistance will be necessary for several reasons, first to provide the degree of expertise required, then to satisfy the level of independence required, and finally to address the sensitivity of the matter. Further, to formulate their estimates, these experts will probably need to conduct one or more event studies or similar analyses. These analyses will likely involve a number of assumptions and qualitative decisions that typically produce a range of outcomes, each based on a combination of statistical probability and the good faith, albeit subjective, judgment of the individual conducting the study.

Thus, treating stock price and TSR as financial reporting measures for purposes of defining “incentive-based compensation” will force issuers to incur potentially significant costs to determine whether a financial restatement resulted in excess incentive-based compensation, without any assurance that such amounts represent compensation that has been “erroneously” awarded to an issuer’s executive officers. Further, given the high degree of subjectivity that will necessarily go into the analysis, it is highly likely that the resulting estimate will be subject to challenge, both by the

⁶⁰ Or any measure that is derived wholly or in part from such measures.

affected executive officer (which will certainly be the case if the amount at stake is sufficiently large) and by shareholders (who may believe that the amount to be recovered is not large enough). We believe that it is untenable to put issuers in a position where their efforts to enforce their compensation recovery policy will be unduly expensive and almost certain to be second-guessed.

Finally, we do not anticipate that the removal of TSR from the definition of a “financial reporting measure” will cause issuers to select this measure over other appropriate measures for their incentive-based compensation plans and arrangements.⁶¹ While the number of issuers that include TSR as a performance measure in the design of their short-term and long-term incentive compensation arrangements has steadily grown over the past several years, a recent study indicates that much of this increase is largely the result of the influence of the proxy advisory firms and, to a certain extent, peer pressure. Absent these factors, we believe that many issuers would select performance measures that better serve their business purpose and/or de-emphasize the use of TSR.

30. Should incentive-based compensation be defined to include compensation that is based on satisfying one or more subjective standards (such as demonstrated leadership) to the extent that such subjective standards are satisfied in whole or in part by meeting a financial reporting measure performance goal (such as stock price performance or revenue metrics)? If so, how could this approach be implemented? Is it sufficient that the current proposal encompasses “any compensation that is granted, earned or vested based wholly or in part upon the attainment of a financial reporting measure”? If not, why not?

We do not believe that the language or purpose of Section 10D of the Exchange Act requires inclusion of compensation that is based on satisfying one or more subjective standards (to the extent that such subjective standards are satisfied in whole or in part by meeting a financial reporting measure performance goal (such as stock price performance or revenue metrics)) as “incentive-based compensation.” In our view, implementing such an approach would be extremely complex; requiring an issuer (or, more likely, its Board of Directors (or Compensation Committee)) to determine the extent to which decisions based on qualitative factors were influenced or based on financial criteria. We note that issuers currently struggle to identify such relationships when analyzing compensation decisions for purposes of preparing their Compensation Discussion and Analysis.

In our experience, most, if not all, of these decisions, result from the exercise of the business judgment of the members of the Board of Directors (or Compensation Committee) after considering a number of quantitative and qualitative factors. They

⁶¹ In fact, we note that, in recent years, the value of using TSR as a performance measure has been called into question. See, for example, *The Limits of Using TSR as an Incentive Measure*, David N. Swinford, Pearl Meyer & Partners LLC (Oct. 13, 2015), available at <http://corp.gov.law.harvard.edu/2015/10/13/the-limits-of-using-tsr-as-an-incentive-measure/>.

are not formulaic, nor do they necessarily lend themselves to a formulaic recreation. Linking the recovery of incentive-based compensation to such an amorphous assessment would be extremely challenging – as well as unreliable – as it would force issuers to draw after-the-fact conclusions that simply would not accurately capture the decision-making process of the Board of Directors (or Compensation Committee).

As more fully explained in our responses to Questions 26 and 29 above, we believe that defining “incentive-based compensation” as those amounts reported in the Grants of Plan-Based Awards Table that were “granted, earned or vested based wholly or in part upon the attainment of a “financial reporting measure” most accurately captures the compensation intended to be subject to Section 10D.

31. Should the proposed rule or listing standards contain any anti-evasion language that would treat as incentive-based compensation amounts received purportedly based on one or more subjective standards but that are in fact based on financial information metrics, total shareholder return or stock price performance? If so, what should the language provide?

We have not identified any “anti-evasion” language that we believe would treat as “incentive-based compensation” amounts received purportedly based on one or more subjective standards but that are in fact based on financial information metrics, TSR or stock price performance other than as addressed in our responses to Questions 26 through 30 above.

32. Should the definition of “incentive-based compensation” included in Rule 10D-1 be principles-based, as proposed? Alternatively, should the definition specify performance measures that may be affected by an accounting restatement? If so, please explain which examples should be included and why.

As we note at the outset and throughout this Comment Letter, we agree that proposed Rule 10D-1 should be implemented using a principles-based approach and do not believe that examples of specific performance measures that may be affected by an accounting restatement are necessary.

33. Regarding the statutory provision that incentive-based compensation subject to recovery “includ[es] stock options awarded as compensation,” does the proposed definition provide a basis by which issuers can identify equity awards that would be covered? If not, please explain why not. If all options should be subject to recovery, how should the amount subject to recovery following an accounting restatement be computed for time-vested options that are not granted based on satisfaction of a financial reporting measure performance goal?

We recommend that the Commission expressly and unambiguously confirm that equity awards, including stock options and restricted stock awards, that are earned

("vest") solely on the completion of a specified employment period or passage of time are not "incentive-based compensation" for purposes of proposed Rule 10D-1(c)(4) (or the final version of Rule 10D-1), even though their ultimate value fluctuates with the value of the issuer's stock. While this conclusion may be obvious to some,⁶² we are concerned that the proposed definition of the term "incentive-based compensation" may be read as potentially encompassing these "time-based" awards.

As proposed, "incentive-based compensation" is defined as "any compensation that is granted, earned or vested based wholly or in part upon the attainment of any financial reporting measure." We believe that there are two potential interpretive concerns with this definition that are needlessly problematic and worthy of clarification.

First, by defining the term "financial reporting measure" to include stock price, we are concerned that such definition may be interpreted broadly to include an equity award for which the ultimate value is determined directly by reference to an issuer's stock price but which, in fact, is to be earned solely upon satisfaction of a specified employment period or passage of time.

Second, in our experience, an issuer's Board of Directors (or Compensation Committee) typically determines the size of an equity award granted to an individual executive officer after considering a variety of quantitative and qualitative factors, such as the issuer's prior operational performance, competitive market practices and conditions, and the individual executive officer's position, responsibilities, tenure, experience, prior performance, and expected future contributions. While the financial performance of the issuer, including its stock price, as well as the individual executive officer's contributions to that performance, may be evaluated by the Board of Directors (or Compensation Committee) in the course of its deliberations, this consideration will be of a general nature and not with reference to specific target levels of either required or aspirational performance. We believe that, where the shares of stock subject to an award are to vest solely based on continued employment for a pre-established period or the passage of time, the fact that the Board of Directors (or Compensation Committee) may have considered the issuer's financial performance, including changes in the price of its stock, in deciding to grant the award, does not cause the award to be compensation that is granted upon the attainment of a financial reporting measure and, thus, incentive-based compensation for purposes of proposed Rule 10D-1.

We believe that any ambiguity or uncertainty with respect to these issues can be effectively resolved with an express statement as set forth above in the first paragraph of this response.

⁶² See the Proposing Release, at Section II.C.2.a: "Examples of compensation that would not be "incentive-based compensation" for this purpose would include, but not be limited to . . . Equity awards for which the grant is not contingent upon achieving any financial reporting measure performance goal and vesting is contingent solely upon completion of a specified employment period"

34. Regarding bonuses granted from a “bonus pool,” the size of which is based wholly or in part upon satisfying a financial reporting measure performance goal, does the proposed definition properly subject this form of compensation to recovery? If not, how should we treat such compensation for purposes of Rule 10D-1?

We believe that as long as the bonus awarded from a “bonus pool” meets the definition of “incentive-based compensation” as we recommend in our response to Question 26 above, the proposed approach will properly subject such bonus amounts to the final version of Rule 10D-1.

35. Is further guidance needed as to how the proposed definition would apply to forms of compensation that may be paid out on a deferred basis, such as employee or employer contributions of incentive-based compensation to nonqualified deferred compensation plans and earnings thereon, and future retirement benefits payable under pension plans, such as supplemental retirement benefit plans, that are calculated based on incentive-based compensation? If so, what further guidance should we provide?

We believe that, to the extent that the Commission does not expressly exclude such arrangements from the proposed definition of “incentive-based compensation,” guidance should be provided as to how the definition would apply to forms of compensation that may be paid out on a deferred basis, such as employee or employer contributions of incentive-based compensation to nonqualified deferred compensation plans and earnings thereon, and future retirement benefits payable under pension plans, such as supplemental retirement benefit plans, that are calculated based on incentive-based compensation.

We also note that proposed Rule 10D-1 may be interpreted to apply to tax-qualified retirement plans that take into account incentive-based compensation in their benefit formula or that condition contributions on the attainment of financial reporting measures. We believe that the amounts contributed to or paid from such plans are not “incentive-based compensation,” and, accordingly, the final version of Rule 10D-1 should include a clear statement to the effect that such amounts, as well as amounts contributed to or paid from related non-qualified retirement plans, are not subject to the final rule.

In addition, we understand that subjecting tax-qualified retirement plan amounts to recovery under proposed Rule 10D-1 would likely violate the anti-forfeiture, anti-alienation, and anti-reversion rules of ERISA and the Code provisions applicable to such plans:

- Both ERISA and the Code provide that any vested amounts held in a tax-qualified retirement plan may not be forfeited, with very limited exceptions which would not apply in these circumstances.⁶³

⁶³ ERISA §203; Code §411(a).

- Subjecting a tax-qualified retirement plan benefit to a repayment obligation would violate the provisions of ERISA and the Code that prohibit the alienation of a retirement plan benefit. In *Guidry v. Sheet Metal Workers*, for example, the Supreme Court considered whether a constructive trust could be imposed under labor law on the retirement plan benefit of a union official guilty of embezzling funds⁶⁴ but ruled that would violate ERISA's anti-alienation rule concluding that "[w]here there is no clear intention otherwise, a specific statute will not be controlled or nullified by a general one...."⁶⁵ We believe courts will conclude that ERISA's anti-alienation rule would similarly override an SEC regulation under the Dodd-Frank Act alienating tax-qualified retirement plan benefits.
- ERISA and the Code also prohibit amounts held in a tax-qualified retirement plan from reverting to the employer, with limited exceptions not applicable here.⁶⁶ Repayment of benefits from a plan to the employer would likely be viewed as an impermissible reversion.

Further, applying proposed Rule 10D-1 to tax-qualified retirement plan benefits would have broader consequences, as it would likely cause a violation of ERISA and the Code and could subject the plan, plan sponsor, and participants to significant adverse consequences, which could include lawsuits by participants and the Department of Labor or loss of favorable tax-qualified status. We understand that, in such case, all plan participants, not just the subject executive officers, could suffer the adverse tax consequences with respect to their plan benefits.

As we have noted above in our responses to Questions 26 through 33 above, the Commission need not take such a broad view of the scope of Section 10D of the Exchange Act. The statute covers "incentive-based compensation" paid to the executive officers of an issuer. Tax-qualified retirement plans are non-discriminatory in application and, thus, are not incentive-based compensation. As such, they are not subject to disclosure in the various "incentive plan" columns of the Grants of Plan Based Awards Table, even if incentive compensation factors into the benefit formula of a retirement plan.

For similar reasons the Commission need not interpret through a general rule or instruction the term "incentive-based compensation" so broadly as to include non-qualified retirement plans. Non-qualified retirement plans provide tax-efficient compensation and retirement benefits, rather than serve the purpose of incentivizing performance. Even a defined contribution plan in which issuer performance may be a direct factor in determining the amount of the issuer's contribution does not alter the

⁶⁴ ERISA §206(d); Code §401(a)(13).

⁶⁵ 493 U.S. 365, 369-71 (1990).

⁶⁶ *Id.*, at 375-76, 376 *quoting *Morton v. Mancari*, 417 U.S. 535, 550-51 (1974).

retirement purpose for the plan. We believe that applying the compensation recovery requirement to non-qualified plans does not serve the purposes of Section 10D.

To avoid the potential for abuse, however, the exclusion of non-qualified retirement plans from being “incentive-based compensation” should not extend to specific amounts that would otherwise be “incentive-based compensation” under the principles we discuss in our response to Question 26 above, and which are credited to a nonqualified deferred compensation plan. Such deferral, whether mandated by the employer or elected by the executive officer, does not change the character of those amounts and they should remain “incentive-based compensation” subject to the final version of Rule 10D-1.

b. Time Period Covered by Recovery Policy

36. Is the proposed approach to determine the three-year look-back period for recovery an appropriate means to implement Section 10D? Does it properly reflect the way in which issuers make their compensation decisions (on a fiscal year by fiscal year basis)? Why or why not?

We support the Commission's proposal to define the three-year “look-back” period specified in Section 10D(b)(2) of the Exchange Act as the “three completed fiscal years immediately preceding the date that the issuer is required to prepare a restatement of its previously issued financial statements to correct a material error.”⁶⁷ In our experience, most issuers make their executive compensation decisions on a fiscal year-by-fiscal year basis, with such decisions typically taken during the first quarter of each fiscal year. We believe that using a look-back period that covers three completed fiscal years helps to simplify compliance in terms of both identifying the specific executive officers and the incentive-based compensation that would be subject to an issuer's mandated compensation recovery policy. In our view, to base the calculation of the three-year look-back period on a specific date (such as the proposed date on which an issuer would be considered to be required to prepare an accounting restatement⁶⁸) would potentially lead to incongruous results.⁶⁹ For example, depending on the specific date when an accounting restatement would be deemed to be required, between two and four compensation cycles may wind up being captured within the 36-month look-back period. We believe that, to promote efficient compliance and in the interests of fairness, the look-back period should be consistently applied to all issuers.

⁶⁷ See proposed Rule 10D-1(b)(1)(ii).

⁶⁸ See proposed Rule 10D-1(c)(2).

⁶⁹ We also agree with the Commission's observation that an issuer should not be able to delay or relieve itself from the obligation to recover erroneously-awarded compensation by delaying or failing to file restated financial statements.

37. Should a different approach be used to determine the three-year look-back period for recovery? If so, how should the look-back period be determined, and why? For example, should an issuer be permitted to apply its recovery policy to any three-year period in which incentive-based compensation received by executive officers was affected by the accounting error?

Please see our response to Question 36 above. As we discuss, we believe that the objective and uniform application of the three-year look-back period to all issuers outweighs any benefits to be gained by permitting issuers to select the specific three-year period in which incentive-based compensation received by executive officers that was affected by the accounting error is to be recovered. While certainly there will be some situations where granting this discretion to an issuer's Board of Directors may produce a result that may be more appropriate than the application of an objectively-mandated three-year look-back period, we are concerned that this discretion may be exercised in a manner that will invite "second-guessing" by shareholders or, more likely, third parties who will view this decision as a litigation opportunity. As we note throughout this Comment Letter, we believe that, ultimately, the final version of Rule 10D-1 should operate in a manner that minimizes the risk to issuers of costly and protracted litigation to defend their decisions against spurious claims by plaintiffs.

38. Is the proposed approach regarding transition periods related to a change in fiscal year appropriate? If not, what alternative approach should we consider? Consistent with Rule 3-06(a) of Regulation S-X, should a transition period of nine to 12 months be considered a full year in satisfying the three-year look-back period requirement?

We support the Commission's proposal to require issuers to recover any excess incentive-based compensation received during the transition period occurring during, or immediately following a three-year look-back period where the issuer has changed its fiscal year during the look-back period (that is, a total of four accounting periods).⁷⁰

Consistent with our response to Question 36 above, we believe that the overarching goal here should be the objective and uniform application of the standard to all listed issuers. We further believe that the Commission's proposal, including the treatment of a transition period of nine to 12 months as a full fiscal year,⁷¹ would achieve this goal.

c. When Incentive-Based Compensation Is "Received"

39. Should incentive-based compensation be deemed "received" for purposes of triggering the recovery policy under Section 10D in the fiscal year during

⁷⁰ See proposed Rule 10D-1(b)(1)(ii).

⁷¹ *Id.* With respect to the treatment of a transition period of nine to 12 months as a full fiscal year for purposes of satisfying the three-year "look-back" period requirement, see Rule 3-06(a) of Regulation S-X [17 CFR 210.3-06(a)].

which attainment of the financial reporting measure specified in the incentive-based compensation award, by its terms, causes the incentive-based compensation to be granted, to be earned or to vest, as proposed? If not, when should incentive-based compensation be deemed “received” for purposes of triggering the recovery policy?

We support the Commission's proposal to treat incentive-based compensation as “received” in the fiscal period during which the financial reporting measure specified in the incentive-based compensation award is attained, even if the payment or grant of the incentive-based compensation occurs after the end of that period.⁷² This approach is consistent with the reporting requirements of Item 402 of Regulation S-K, particularly as it involves the discussion of compensation earned during the last completed fiscal year for purposes of preparing the Compensation Discussion and Analysis.⁷³

Further, in our experience, this approach conforms to how most issuers view the receipt of incentive-based compensation by their executive officers. Typically, there is a time lag between the end of a performance period and the date when an issuer's Board of Directors (or Compensation Committee) certifies the financial results for that period and determines how much, if any, of the related incentive-based compensation awards has vested or been earned and the award is settled. Since the administrative aspects of the award certification and settlement can vary in length (and are wholly unrelated to the underlying performance which forms the substantive basis for the award), we believe that it is appropriate to treat the fiscal period to which the financial reporting measure relates as the date for deeming incentive-based compensation to be received. In our view, this will provide a degree of predictability and certainty to the process of enforcing the mandated compensation recovery policy.

40. Should an executive officer be required to obtain a non-forfeitable entitlement to the incentive-based compensation to “receive” the compensation? Would such a requirement effectuate the purpose of Section 10D? Should the rule specifically address the treatment of awards subject to multiple vesting conditions, only some of which may be linked to financial reporting measures? If so, what would be the appropriate treatment of such rewards?

Please see our response to Question 39 above.

41. If following receipt, as proposed to be defined, an executive officer contributes incentive-based compensation to a nonqualified deferred compensation plan, how should deferral affect recovery?

Please see our response to Question 35 above.

⁷² See proposed Rule 10D-1(c)(6).

⁷³ See Instruction 2 to Item 402(b) of Regulation S-K.

42. Should incentive-based compensation be subject to the issuer's recovery policy only to the extent that it is received while the issuer has a class of securities listed, as proposed? If not, please explain in what circumstances a different standard should apply and why. For example, if a company lists in 2017, and restates the three prior fiscal years in 2018, should its policy require recovery of incentive-based compensation received in 2015 or 2016?

We support the Commission's proposal to subject incentive-based compensation to an issuer's compensation recovery policy only to the extent that it was received while the issuer has a class of securities listed on a national securities exchange or association.⁷⁴ In our view, this approach would establish a "bright line" test for identifying the incentive-based compensation arrangements that would be potentially subject to an issuer's mandated compensation recovery policy. As issuers prepare to adopt such policies in anticipation of their eventual listing, this should simplify compliance and make it easier for them to advise their executive officers of the potential application of these policies to them.

We agree that, based on this proposal, an award of incentive-based compensation granted to an executive officer *prior to* the time an issuer lists a class of securities on a national securities exchange or association should be subject to its compensation recovery policy, so long as the compensation was received by him or her *while* the issuer had a class of listed securities. Conversely, we agree that incentive-based compensation received by an executive officer before an issuer's securities were listed should not be subject to its compensation recovery policy.⁷⁵

3. Recovery Process

a. Determination of Excess Compensation

43. Do the proposed rule and rule amendments articulate an appropriate standard for calculating the amount of excess incentive-based compensation that listed issuers must recover? Why or why not?

Under proposed Rule 10D-1, an issuer's Board of Directors would have almost no discretion in determining whether to pursue recovery of excess incentive-based compensation. As proposed, erroneously-awarded compensation would be recoverable in all cases with only one limited exception – where recovery is "impracticable" (as defined in proposed Rule 10D-1(b)(1)(iv)). Just as discretion is

⁷⁴ Proposed Rule 10D-1(b)(1)(i)(A).

⁷⁵ In addition, a national securities exchange or national securities association would not be permitted to list an issuer that it has delisted or that has been delisted from another exchange for failing to comply with its compensation recovery policy until such time as the issuer complies with that policy. See proposed Rule 10D-1(b)(1)(vi).

severely limited with respect to an issuer's decision not to seek recovery, it would also have virtually no discretion to determine how much to recover. As stated in proposed Rule 10D-1(b)(1)(iii):

The amount of incentive-based compensation subject to the issuer's recovery policy (the "erroneously awarded compensation") shall be the amount of incentive-based compensation received that exceeds the amount of incentive-based compensation that otherwise would have been received had it been determined based on the accounting restatement, and shall be computed without regard to any taxes paid.

Should the Commission not agree with our response to Question 51 below and ultimately decide to apply the final version of Rule 10D-1 to the recovery of excess incentive-based compensation without the exercise of discretion (in all instances except to the extent that recovery is "impracticable,"), we believe that, subject to the suggested revision described below, the proposed standard for calculating the amount of excess incentive-based compensation that listed issuers must recover is clear and understandable.

In this instance, we recommend that the Commission modify the proposed standard to require that the amount of excess incentive-based compensation be computed on a post-tax, rather than a pre-tax, basis. We believe that it would be punitive and inequitable to require an executive officer to forfeit incentive-based compensation on a pre-tax basis after taxes have been paid on that amount.⁷⁶ Given the likelihood that a financial restatement may not occur until months, if not years, following the receipt of incentive-based compensation – and the probability that an issuer's executive officers may have already paid tax on the compensation as if they had earned it, they could potentially end up in a position where they are left with less money than they had before receiving the incentive-based compensation.

An executive officer's ability to recover or "unwind" the taxes that he or she has paid on compensation that has been recovered by the issuer is unclear. In many instances, such "recovery" may be limited to claiming an itemized deduction in the year of repayment, which would be subject to a 2% "floor" and the alternative minimum tax. While an executive officer may be able to obtain additional relief under Section 1341 of the Code, under the current federal income tax rules this treatment is unclear. To avoid an inequitable result – and undoubtedly undue hardship for the executive officer, we recommend that the final version of Rule 10D-1 should require issuers to recover only from his or her after-tax proceeds.

44. For incentive-based compensation based on stock price or total shareholder return, would permitting the recoverable amount to be determined based on

⁷⁶ An executive officer may have already paid income and employment taxes on the amount being recovered, and absent relief, would need to independently seek recoupment from the applicable taxing authority.

a reasonable estimate of the effect of the accounting restatement, as proposed, facilitate administration of the rule by issuers and exchanges? Why or why not? Should we provide additional guidance regarding how such estimates should be calculated? If so, what particular factors should that guidance address?

Consistent with our response to Question 29 above, we do not believe including stock price or TSR as “financial reporting measures” for purposes of determining “incentive-based compensation” is required or appropriate. Please also see our response to Question 52 below.

45. As proposed, should the issuer be required to maintain documentation of the determination of that reasonable estimate and provide such documentation to the relevant exchange? Why or why not? Is the documentation required sufficient for compliance monitoring? If not, what else should be required? Should the rule specify a period of time that an issuer would need to maintain such documentation or what types of documentation should be maintained? If so, what period of time or documentation is appropriate? Should we require that such determination be disclosed, either to the exchange or in Commission filings? What would be the effects of such disclosure?

Please see our response to Question 29 above. Alternatively, should the Commission ultimately decide to retain stock price and TSR as financial reporting measures, we agree with the proposal to require issuers to maintain documentation of their determination of the reasonable estimate of the effect of the accounting restatement on the applicable measure. We believe that, as proposed, this documentation should be sufficient for compliance monitoring.

We recommend one change to the proposal. Rather than requiring that such documentation be automatically provided to the national securities exchange or association on which an issuer's equity securities are listed, we recommend that the issuer simply be required to provide such documentation upon the request of the exchange or association. This will both simplify compliance and limit the provision of such documentation to situations where the exchange or association is conducting an active review of an issuer's compliance with the listing standard.

Further, to counter the largely prescriptive orientation of enforcement of the required compensation recovery policy, we believe that it is unnecessary to specify a period of time that an issuer would need to maintain such documentation or the type or types of documentation that should be maintained. We believe that issuers can be trusted to determine for themselves what constitutes sufficient documentation of their reasonable estimate and supporting data. In this regard, we note that, since most issuers will be compelled to retain one or more outside experts to assist in making the required determinations, they will likely receive written reports containing such experts' conclusions and supporting materials. These reports will undoubtedly form the basis of the required documentation.

Finally, we see no compelling reason for requiring disclosure of an issuer's determination of the reasonable estimate of the effect of an accounting restatement on its stock price or TSR, either to the national securities exchange or association on which its equity securities are listed or in a Commission filing. We believe that the calculation of any such reasonable estimate, as well as the related documentation, is likely to contain sensitive information, the disclosure of which could cause competitive harm to the issuer. Thus, we would oppose a requirement to disclose such information generally and believe that it should only be required to be disclosed to the applicable exchange or association upon request and with adequate confidentiality assurances.

46. Should the rule and rule amendments alternatively, or in addition, include specific instructions for how to compute the excess amount of specific forms of incentive-based compensation? If so, which ones and why?

For the reasons discussed elsewhere, we believe that such guidance is not required for issuers to be able to apply the final version of Rule 10D-1 and the proposed rule amendments under a principle-based approach.

47. Is further guidance needed on the application of the proposed standard? If yes, what additional guidance is necessary? Is further guidance required regarding any particular form of compensation? For example:

- a. **Should we provide guidance on how to determine the recoverable amount of supplemental retirement plan benefits that are calculated based on erroneously awarded incentive-based compensation? If so, what should that guidance be?**
- b. **For equity awards granted based on satisfaction of a financial reporting measure, the guidance above directs listed issuers to recover the excess number of shares or, if no longer held, the proceeds from the sale of the excess shares so that executive officers cannot benefit from future appreciation in shares that were not earned. Instead of recovering the excess number of shares, should listed issuers have the choice to recover the cash value of the excess shares? If so, should the shares be valued at the vesting date, the date the recoverable amount is determined, or some other date?**
- c. **Where the number of excess shares is less than the entire award and some of the shares received were sold and some are still held, should recovery be made first against the remaining shares that are held? Alternatively, should recovery apply first to shares that were sold, so as not to erode company stock holding policies? Should this decision be left to the listed issuer's discretion?**
- d. **Where excess shares have been gifted, such as gifts to charities, should the recoverable amount be the shares' fair market value at the date of the gift? If**

not, at what other date should the excess shares be valued?

e. Is the guidance above appropriate for determining the recoverable amount where the listed issuer has exercised discretion to reduce or increase the original amount of incentive-based compensation received?

We believe that, depending on the substantive content of the final version of Rule 10D-1, the Commission should consider including in the final rule specific instructions on how to compute the excess amount of specific forms of incentive-based compensation. Subject to our response to Questions 51 and 52 below, such instructions should address, but not necessarily be limited to, the following:

- The amount recoverable from any supplemental retirement plan benefits that have been calculated based on erroneously awarded incentive-based compensation, but only to the extent that such benefits have been paid or are otherwise payable to a subject executive officer. To the extent that the compensation that will be used for purposes of the benefits formula has not been finally determined, we expect that a notional adjustment excluding the applicable amount of excess incentive-based compensation would suffice to ensure that the ultimate benefits would not be based, wholly or in part, on erroneously awarded incentive-based compensation.
- The methodology for determining the cash value of the number of shares that represent erroneously awarded incentive-based compensation where such shares were granted on the basis of satisfying a financial reporting measure and have subsequently been sold or otherwise disposed of for consideration.⁷⁷ In this situation, we recommend that the recoverable amount be based on the market fair value of the shares on the date the recoverable amount is determined. In our view, this approach will ensure that fluctuations in the value of the excess shares following the date when the shares have been granted, earned, or vested do not unduly benefit or penalize the executive officer.
- The methodology for determining the order of recovery where the number of shares representing erroneously awarded incentive-based compensation is less than an entire award and some of the shares received have been sold and some are still held by an executive officer. In this situation, we recommend that recovery be made first against the remaining shares that are held.⁷⁸

⁷⁷ We believe that, where an executive officer holds the shares representing excess incentive-based compensation at the time that an issuer's compensation recovery policy is triggered, the excess number of shares should be subject to recovery.

⁷⁸ While we appreciate the question raised about the possible ramifications of such a result where recovery of excess shares would potentially cause an executive officer to violate the issuer's stock ownership and/or holding policies, to us this dilemma simply underscores our belief that an issuer and its

- The methodology for determining the recoverable amount where shares representing erroneously awarded incentive-based compensation have been transferred as a gift. In this situation, we recommend that the recoverable amount be based on the shares' fair market value at the date of the gift. Once again, we believe this approach will ensure that fluctuations in the value of the excess shares following the date when the shares have been granted, earned, or vested do not unduly benefit or penalize the executive officer.

48. Where the issuer chose to increase the original amount of incentive-based compensation, should an amount proportionate to the effect of the restatement on the financial statement measure also be recovered from the discretionary enhancement?

We believe that where an issuer's Board of Directors (or Compensation Committee) exercised its discretion to increase the amount of incentive-based compensation received by its executive officers, such discretionary enhancement should not be subject to the mandated compensation recovery policy, with one possible exception. Where it can be conclusively established that the amount of the discretionary enhancement was based on the amount of incentive-based compensation earned, then we would agree that such amount should be recoverable since it was directly derived from the erroneously-awarded compensation. In all other situations, we believe that recovery would be inconsistent with the objectives of Section 10D of the Exchange Act.

Otherwise, please see our response to Question 51 below. We believe that where an issuer's Board of Directors has the discretion to determine the appropriate application of the mandated compensation recovery policy to the facts and circumstances of each situation, it should be up to the Board to determine whether or not the discretionary portion of an incentive-based compensation award was based on the financial reporting measure and, accordingly, whether such amount should be subject to recovery.

49. One commenter recommended that the Commission require recovery of a proportionate amount of incentive compensation awarded under qualitative standards. Should we require recovery of amounts awarded under qualitative standards that may involve judgement by the board? If so, how would the excess compensation be calculated in those instances?

We believe that including amounts based on qualitative standards would take proposed Rule 10D-1 beyond the scope of Section 10D of the Exchange Act, which by its terms is to apply to only compensation based on "financial information" required to

be reported.

50. Is further guidance needed regarding circumstances in which both proposed Rule 10D-1 and SOX Section 304 would apply?

We believe that further guidance is not needed at this time because proposed Rule 10D-1 precludes duplicate recovery.

b. Board Discretion Regarding Whether to Seek Recovery

51. Is the proposed issuer discretion not to pursue recovery of incentive-based compensation consistent with the purpose of Section 10D? Is the scope of this discretion appropriate? Why or why not?

We believe that the contemplated level of issuer discretion is problematic and, in our view, represents the single biggest impediment to the effective implementation of Section 10D of the Exchange Act. While we understand why the Commission may be inclined to take a largely prescriptive approach to the enforcement of the mandated compensation recovery policy required by Section 10D, we believe that a more pragmatic approach is warranted. Further, such an approach is necessary to provide the flexibility that will be required to address the myriad of complex and possibly intractable situations that will inevitably arise and to ensure that issuers do not get embroiled in lengthy disputes and irresolvable questions when attempting to enforce their compensation recovery policy.

At the outset, we note that proposed Rule 10D-1 is largely inflexible. An issuer's Board of Directors would have almost no discretion in determining whether to pursue recovery, as well as how much to recover. As proposed, an issuer would be required to recover erroneously-awarded compensation in all instances, with only one limited exception – where recovery is impracticable.⁷⁹ This exception would permit an issuer to determine that recovery would be “impracticable,” which would be narrowly defined to encompass only two specific situations: in the case of a domestic issuer, where the direct expense paid to a third party to assist in enforcing the policy would exceed the amount to be recovered⁸⁰ and, in the case of a foreign private issuer, where recovery would violate home country law.⁸¹

⁷⁹ Proposed Rule 10D-1(b)(1)(iv).

⁸⁰ Further, reliance on this exception would be predicated on an issuer first making a reasonable attempt to recover any excess incentive-based compensation, its independent directors making an affirmative “impracticability” determination, documenting this recovery attempt (or attempts), providing such documentation to the national securities exchange on which its securities are listed, and disclosing the reasons as to why it has decided not to pursue recovery. See proposed Rule 10D-1(b)(1)(iv).

⁸¹ *Id.*

We believe that 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 following a financial restatement.

First, issuers will be required to recalculate their incentive-based compensation payments and awards to identify the group of current and former executive officers from whom recovery is required. Given the length of the specified “look-back” period, issuers will undoubtedly face challenges in locating any former executive officers who are subject to the policy. Then, once located and, assuming contact has been made, a new set of challenges will likely arise. Recovery of the erroneously-awarded compensation will likely create repayment issues, such as how to obtain recovery when the amounts due are no longer available to an individual (whether a current or former executive officer), or how to pursue recovery when such action may be subject to limitations under the laws of the individual’s state or country of employment or residence.

In more pragmatic terms, the Board of Directors will also need to consider how to approach a very sensitive subject with individuals that it is depending on to successfully manage the business. Some executive officers may face serious hardship or practical problems⁸² if required to rapidly liquidate assets sufficient to return multiple years of incentive-based compensation, which could further exacerbate the potential inequity to such individuals. Further, if the current market price of the issuer’s shares of stock is depressed as a result of the announcement of the accounting restatement, requiring an executive officer without sufficient resources to rapidly fund a recovery by “promptly” disposing of such securities would lead to further inequities.

Further, the issuer’s Board of Directors will have to consider several overarching issues – such as whether pursuing recovery will make recruiting or retaining executive officers more difficult or expensive, or otherwise adversely affect the value of the issuer from an investment perspective. Each of these issues, and their many permutations, may give rise to numerous complex and sensitive financial, legal, and personal issues which will need to be untangled and addressed in determining the amount and manner of recovery. These are all matters that the issuer’s Board of Directors should be permitted to consider and address in the manner that it determines to be in the best interests of the issuer and its security holders.

These concerns underscore the need for flexibility in making these types of recovery calculations on a case-by-case basis and the need for an issuer’s Board of

⁸² There may be numerous legal hurdles that need to be addressed before an executive officer is in a position to liquidate the equity securities of his or her employer. For example, the issuer’s trading “window period” may be closed, the executive officer may be in possession of material nonpublic information, he or she may be subject to the “short swing profits” trading restriction of Section 16(b) of the Exchange Act, he or she may be subject to the issuer’s stock ownership policy, or the conditions of Securities Act Rule 144 may need to be satisfied.

Directors to have reasonable discretion in determining how to recover compensation that must be repaid. While an issuer's Board of Directors is, perhaps, uniquely situated to decide what action, if any, is in the best interests of the issuer, particularly when it comes to a matter which is largely within the purview of its responsibilities for designing and implementing the issuer's executive compensation program,⁸³ proposed Rule 10D-1 precludes it from doing so.

Because of the myriad of situations that may exist at the time that an issuer seeks to enforce its compensation recovery policy, we request that the Commission reconsider whether Boards of Directors of listed issuers should be given broad discretion to assess whether recovery is in the best interests of the issuer and its security holders, and, if so, how to effect that recovery consistent with the foregoing objectives.⁸⁴ 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.⁸⁵

We believe that a careful reading of Section 954 supports our request. In the Proposing Release, the Commission suggests that its decision to limit the discretion of an issuer when enforcing its compensation recovery policy is dictated by the express language of Section 10D,⁸⁶ which states that "the issuer will recover" any excess incentive-based compensation.⁸⁷ We note that the Commission goes on to observe, however, that the statute "does not address whether there are circumstances in which the Board of Directors may exercise discretion not to recover."⁸⁸ Thus, we believe that the Commission has the authority to permit the exercise of discretion to enforce the mandated compensation recovery policy as long as doing so is necessary or appropriate in the public interest, and is consistent with the protection of investors.⁸⁹

Accordingly, we recommend that the Commission consider whether the final version of Rule 10D-1 should reflect the general principle that an issuer's Board of

⁸³ See the letter of The Society of Corporate Secretaries & Governance Professionals dated September 18, 2015, at page 7.

⁸⁴ In our view, this discretion would encompass the ability to pursue recovery, to not pursue recovery, to settle for a lesser amount, or to otherwise pursue an alternative means of recovery.

⁸⁵ In our view, such disclosure would include a summary of an issuer's attempts to recover the excess incentive-based compensation, if any, and all additional facts that contributed to the decision to forgo recovery or settle for a lesser or different amount. Shareholders that are dissatisfied with a Board of Directors' decisions, or its rationale for settling for less than full recovery, could register their disagreement either by voting against individual directors when they are next up for re-election or against the issuer's shareholder advisory vote on named executive officer compensation.

⁸⁶ See Section 10D(b)(2) of the Exchange Act.

⁸⁷ See the Proposing Release, at Section II.C.3.b.

⁸⁸ *Id.*

⁸⁹ See Section 36(a)(1) of the Exchange Act.

Directors⁹⁰ be able to exercise discretion regarding the amount of excess incentive-based compensation to be recovered, as well as how that recovery is to be accomplished. In our view, this flexibility recognizes the role that the business judgment of the Board of Directors plays designing and awarding incentive-based compensation and allows the Board of Directors to make determinations to ensure that the recovery is in the best interests of the issuer and its security holders.

Alternatively, should the Commission ultimately decide to apply the final version of Rule 10D-1 to the recovery of excess incentive-based compensation without the exercise of discretion (except to the extent that recovery is "impracticable"), we request that the Commission also permit the Board of Directors to exercise its discretion to decide not to pursue recovery where:

- the amount to be recovered is *de minimis* (for example, \$10,000 or less); or
- it has determined that protracted litigation would be required to recover the compensation.

We believe that each of these situations is appropriate for relief because recovery would impose undue costs on an issuer and its security holders. In situations such as these, we believe the Commission should explicitly recognize the Board of Directors' authority to decide not to recover excess incentive-based compensation when it is not in the best interests of the issuer to do so. As with our general recommendation as to the use of discretion, we further recommend that the disclosure requirements of proposed Item 402(w) be used to monitor any decision by a Board of Directors to forgo recovery to provide the necessary oversight of these exceptions.

52. Should the standard for exercising discretion not to recover be limited to the extent to which that recovery is impracticable? Should direct costs of recovery be a basis for exercising discretion not to recover? If so, what specific costs of recovery should be considered? For example, should only direct expenditures to third-parties be considered, as proposed? Should we further define what constitutes "direct costs"? Should an issuer be permitted to consider indirect costs, such as opportunity costs or reputational costs? Should the issuer disclose the cost estimates in its Exchange Act annual reports? If the cost estimates are not disclosed in the issuer's annual reports, should those costs be independently verified?

Please see our response to Question 51 above. Should the Commission ultimately decide to apply the final version of Rule 10D-1 to the recovery of excess incentive-based compensation without the exercise of discretion (except to the extent that recovery is "impracticable"), we recommend that, with respect to the exception where

⁹⁰ For purposes of this Section II.3., when we refer to an issuer's "Board of Directors," we mean the issuer's committee of independent directors responsible for executive compensation decisions, or, in the absence of such a committee, a majority of the independent directors serving on the Board of Directors.

the costs of recovery would exceed the amount to be recovered, the cost-benefit analysis not be limited simply to the direct expenses paid to a third party to assist in enforcing the policy. Instead, we believe that the analysis should 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 costs⁹¹ that it can reasonably allocate to the recovery process.

In addition, we believe that the final version of Rule 10D-1 should make it clear that, for purposes of this exception, a “reasonable attempt to recover” erroneously-awarded compensation need be made only if and to the extent that an issuer’s Board of Directors determines that, in view of the economic costs and benefits to the issuer, it is in the best interests of the issuer’s security holders to seek recovery. In our view, the final version of the rule should not require an attempt to recover that would reasonably be expected to result in an issuer’s incurring costs that are greater than the benefits of recovery. We fail to see the benefit in requiring a Board of Directors to act in a manner that it has determined is not in the best interests of the issuer and its security holders simply to be permitted to rely on the exception.

We believe that these modifications are particularly important where, as contemplated by proposed Rule 10D-1(b)(1)(iii) and (c)(4), the financial reporting measure involved in determining the existence of excess incentive-based compensation involves stock price or TSR. As the Commission acknowledges in the Proposing Release:

In some cases, issuers may need to engage in complex analyses that require significant technical expertise and specialized knowledge, and may involve substantial exercise of judgment in order to determine the stock price impact of a material restatement. Due to the presence of confounding factors, it sometimes may be difficult to establish the relationship between an accounting error and the stock price.⁹²

Further, in connection with its discussion of the selection of a methodology to derive a reasonable estimate of the effect of an accounting restatement on stock price and/or TSR, the Commission goes on to note that:

If an issuer chooses to retain an expert, the monetary costs that would be incurred to estimate the “but for” price and subsequent calculation of the

⁹¹ We note that, in the Proposing Release, the Commission states that “[o]nly direct costs involving financial expenditures, such as reasonable legal expenses, would be considered for [the purpose of identifying enforcement costs]. Indirect costs relating to concerns such as reputation or the effect on hiring new executive officers would not be taken into account.” See the Proposing Release, at footnote 183. For purposes of our recommendation, we believe a Board of Directors should be able to consider the comprehensive cost of financial, compensation, legal, and accounting advisors whose services would be required to make the necessary assessments and estimates called for by proposed Rule 10D-1, as well as the costs of collection, the diversion of issuer resources to pursue enforcement, and other such costs that are not purely direct, out-of-pocket expenses.

⁹² See the Proposing Release, at Section II.C.2.a.

amount of excess incentive-based compensation required to be recovered could be substantial. In these circumstances, we expect that the determination of the “but for” price would require a significant number of hours of work by highly skilled experts. In addition, once a “but for” price is estimated, the determination of the amount of excess incentive-based compensation could involve complex calculations and assumptions that may require additional hours of work by the expert.⁹³

Consequently, we expect that, in situations where an issuer’s incentive-based compensation arrangements involve stock price and/or TSR as the financial reporting measure, the issuer may incur significant expense in determining whether any excess incentive-based compensation has resulted from the accounting restatement. Accordingly, we believe that the issuer should be permitted to take the expenses required to make this determination into consideration, along with the recovery costs that it may incur, in deciding whether recovery is “impracticable.” To do otherwise may put an issuer’s security holders in a worse economic position than if recovery had never been initiated in the first place.⁹⁴

To implement this approach, we recommend that the Commission change the definition of “impracticability”⁹⁵ and/or provide guidance on what would constitute an appropriate “cost” for purposes of determining the availability of this exception, and that it permit the inclusion of the direct costs associated with implementing a methodology to reasonably determine whether there is any amount to recover. We further recommend that the disclosure requirements of proposed Item 402(w) be used to monitor a decision by a Board of Directors to forgo recovery on the basis of this form of “impracticability.” Finally, we do not believe that it is necessary to impose a requirement that these costs be independently verified. We are satisfied that an issuer’s Board of Directors can be trusted to make a good faith determination of how its recovery costs compare to the amount to be recovered and decide whether enforcing its compensation recovery policy under these circumstances is in the best interests of the issuer and its security holders.

53. Should the issuer first be required to make a reasonable attempt to recover that compensation, as proposed? If so, should we specify what steps to recover excess incentive-based compensation should be required or what constitutes a “reasonable attempt” to recover such compensation? Should this requirement depend on what financial reporting metric triggers recovery?

⁹³ See the Proposing Release, at Section III.B.2.

⁹⁴ For example, in the case of excess incentive-based compensation predicated on stock price and/or TSR, the mere process of calculating the excess amount may well exceed the amount recoverable. These funds would be spent before the issuer even attempts to recover the amount from its executive officers.

⁹⁵ For example, we support the approach proposed by The Society of Corporate Secretaries & Governance Professionals in its letter dated September 18, 2015, at page 8: “Specifically, recovery would be considered ‘impracticable’ if the ‘costs an issuer would reasonably incur in enforcing the policy would exceed the amount to be recovered.’”

Should the issuer be required to document its attempts to recover, and provide that documentation to the exchange?

Please see our response to Questions 51 and 52 above. Should the Commission ultimately decide to apply final version of Rule 10D-1 to the recovery of excess incentive-based compensation without the exercise of discretion (except to the extent that recovery is "impracticable"), we recommend that it abandon its proposed requirement that "[b]efore concluding that it would be impracticable to recover any amount of erroneously awarded compensation based on expense of enforcement, the issuer must first make a reasonable attempt to recover that erroneously awarded compensation." First, we believe that this proposed requirement, by its very terms, is subjective in nature. What will constitute a "reasonable attempt" to recover any excess incentive-based compensation will vary based on the facts and circumstances of each specific situation. As proposed, an issuer may be required to devote significant time, effort, and expense before its Board of Directors could be assured it was eligible to rely on the exception. Further, any attempt by the Commission to specify the steps that must be taken to recover excess incentive-based compensation or what constitutes a "reasonable attempt" to recover such compensation will make an already overly-prescriptive rule even more so with no assurance that such specificity will alleviate the likely compliance burden.

54. Should a listed issuer be permitted to forego recovering incentive-based compensation if doing so would violate home country law? In this circumstance, should the issuer first be required to obtain a legal opinion from home country counsel, as proposed? If not, why not? Are there any other conditions that should be met beyond a legal opinion from home country counsel before an issuer should be permitted to forego recovering incentive-based compensation in these circumstances? Should the proposed accommodation apply only to the extent that recovery would conflict with home country laws in effect before the date of publication of proposed Rule 10D-1 in the Federal Register, as proposed? If not, please explain why not. In addition, as proposed, the listed issuer would need to provide such opinion to the exchange upon request. Should a copy of this opinion be filed with the Commission as an exhibit? Why or why not?

Please see our responses to Questions 1 (wherein we recommend that foreign private issuers be exempted from the final version of Rule 10D-1) and 51 above. Should the Commission ultimately decide to apply the final version of Rule 10D-1 to the recovery of excess incentive-based compensation without the exercise of discretion (except to the extent that recovery is "impracticable") with respect to the exception where recovery would violate home county law, we support the requirement that issuers obtain a legal opinion from home country counsel, as long as such condition expressly acknowledges and accommodates the quite real likelihood that obtaining such an opinion may take a lengthy period of time.

We are concerned that, by requiring the legal opinion be obtained before an issuer is permitted to conclude that the recovery is "impracticable," the Commission is

effectively putting an issuer in the untenable position of not pursuing the recovery of excess incentive-based compensation “promptly” (as would be required by the proposed rule) and, therefore, vulnerable to spurious claims by plaintiffs that it is not properly enforcing its compensation recovery policy. We request that the Commission expressly provide that a decision to not recover compensation because it violates home country law will be considered “impracticable” as long as the issuer obtains an opinion of home country counsel to that effect either before or within a reasonable time after reaching that conclusion.

Further, we believe it is sufficient that, as proposed, a listed issuer provide such opinion to its national securities exchange or association.⁹⁶ We see no reason why a copy of this opinion need be filed with the Commission as an exhibit. To the extent that there is a compelling reason for ensuring that security holders have access to this opinion, we believe that this interest can be met by requiring the issuer to provide, as part of its required disclosure, a statement indicating that the opinion is available, upon request, from the applicable exchange or association.

We also recommend that this exception be available to domestic, as well as foreign private, issuers. We believe that domestic issuers with executive officers living and working in a foreign country may face the same obstacles as foreign private issuers in recovering excess incentive-based compensation where the home country law of the executive officer prohibits or hinders recovery. We see no reason why such issuers should not be able to avail themselves of this exception should the circumstances warrant.⁹⁷ In our view, as currently proposed, the exception produces an inequitable result by ultimately treating the security holders of domestic and foreign listed issuers differently, solely based on the laws of the country where the issuer is organized.

Finally, as discussed in our response to Question 3 above, we do not support the proposal that would limit the use of the home country laws exception to situations where the subject law was in effect as of July 14, 2015. We are not persuaded by the Commission's concern that, absent such a limitation, foreign countries will be motivated by the exception to change their laws, presumably to entice issuers to relocate in that jurisdiction based solely on the opportunity to avoid having to adopt the mandated compensation recovery policy. Given that many jurisdictions follow the lead of the United States in the development and adoption of appropriate corporate governance standards, we believe that it is unfair to penalize an issuer because it happens to be organized in a jurisdiction that has not had the foresight to adopt a law or regulation governing the recovery of erroneously-awarded compensation ahead of the Commission's own timetable from implementing such a requirement.

⁹⁶ We note that, as contained in proposed Rule 10D-1(b)(1)(iv), this opinion “shall” be provided the applicable national securities exchange or association.

⁹⁷ We recognize that the Commission may contemplate that, in this situation, an issuer would avail itself of the “impracticability” exception based on the expenses of recovery exceeding the amount to be recovered. We believe, however, that domestic issuers should be permitted to use whichever of the two “impracticability” exceptions best fit their specific facts and circumstances.

55. Should the determination that recovery would be impracticable need to be made by the issuer's committee of independent directors responsible for executive compensation decisions, or in the absence of such a committee, by a majority of the independent directors serving on the board? If not, why not, and who should be authorized to make the determination?

Please see our response to Question 51 above. Should the Commission ultimately decide to apply the final version of Rule 10D-1 to the recovery of excess incentive-based compensation without the exercise of discretion (except to the extent that recovery is "impracticable"), we support its proposal that this "impracticability" determination be made by an issuer's committee of independent directors responsible for executive compensation decisions, or, in the absence of such a committee, by a majority of the independent directors serving on the issuer's Board of Directors.

56. Are there other circumstances in which a listed issuer should be permitted to not pursue recovery from its former executive officers? If so, please explain the circumstances and what, if any, conditions should apply.

Please see our response to Question 51 above.

57. Could application of the Section 10D recovery policy to current or former employees cause an issuer to violate any existing statutory or contractual provisions? If so, please specify the applicable provisions, how they might make affect recovery, and how an issuer could address them to implement recovery

With respect to the possibility that application of the compensation recovery policy required by Section 10D of the Exchange Act to current or former executive officers could cause an issuer to violate existing statutory provisions, we note that the Commission appears to recognize the possibility (if not the likelihood) of such a violation in the case of a foreign private issuer⁹⁸ but not a domestic issuer. We believe that the Commission must address the issues associated with state law that may prevent enforcement of a compensation recovery policy in certain jurisdictions. Consequently, we recommend that the Commission provide an exception to the largely mandatory compensation recovery requirement of proposed Rule 10D-1 where recovery could or is reasonably likely to cause an issuer to violate state law or, at a minimum, provide clear guidance as to how issuers should structure their compensation recovery policies in light of applicable state laws. Given the unqualified "no fault" approach of proposed Rule 10D-1, we believe that such relief and/or guidance is necessary to ensure the efficient enforcement of the statutory requirement.

⁹⁸ See proposed Rule 10D-1(b)(1)(iv). While proposed Rule 10D-1 contains a carve-out for impracticality created by a violation of home country law for foreign private issuers, it sidesteps this issue for domestic issuers.

We understand that, in certain states, wage and hour laws may affect – or even preclude – an issuer’s ability to enforce a compensation recovery policy. For example, Section 221 of the California Labor Code provides that “[i]t shall be unlawful for any employer to collect or receive from an employee any part of wages theretofore paid by said employer to said employee.” Similarly, Section 193 of the New York Labor Code contains a provision that states that “[n]o employer shall make any charge against wages, or require an employee to make any payment by separate transaction unless such charge or payment is permitted as a deduction from wages under the provisions of subdivision one of this section.” Further, it appears that in some situations incentive or “bonus” compensation promised or previously paid to an employee may be considered “wages” or “earned compensation” that may not be forfeited pursuant to applicable state wage and hour laws.⁹⁹ While we understand that it is not clear whether these laws would apply to the Commission’s proposed definition of “incentive-based compensation,” nor are we aware of any case law that addresses the matter, we anticipate that, in the absence of a clearly-delineated exception or appropriate Commission guidance, this question would likely be the subject of litigation by a recalcitrant executive officer seeking to test the reach of an issuer’s compensation recovery policy. This very uncertainty may create significant impediments to the enforcement of the mandated compensation recovery policy.

Since neither Section 10D nor proposed Rule 10D-1 impose a direct mandate on issuers, instead imposing a listing requirement on national securities exchanges and associations such that they may delist the securities of non-complying issuers, there may, in fact, be no basis for preempting state law such as Section 221 and Section 193, which are intended to protect employee wages.¹⁰⁰ Thus, in the absence of Commission action, issuers may be put in the untenable position of having to decide whether to face delisting or potentially violate state law. Perhaps just as troubling, absent Commission action, it is likely that this issue will wind up being among the initial claims litigated if an executive officer objects to or resists recovery.

In summary, we believe that an issuer should not be required to seek recovery of incentive-based compensation from a current or former executive officer under any circumstance where its Board of Directors (or appropriate board committee) determines that such recovery would violate, or is reasonably likely to violate, applicable local law.

⁹⁹ For example, see *Schachter v. Citigroup, Inc.*, 47 Cal. 4th 610, 618 (2009) (California Supreme Court holds that incentive compensation, such as bonuses and profit-sharing plans, constitutes “wages” under Section 221). Further, while discretionary bonuses that are based on the employer’s financial performance and not directly related to the “personal productivity” of an employee are not considered “wages” under the New York State Labor Law (see *Truelove v. Northeast Capital & Advisory, Inc.*, 715 N.Y.S.2d 366 (N.Y. 2000)), once paid, even a discretionary bonus may be deemed to be a “wage,” thereby making recovery problematic.

¹⁰⁰ We note that, with respect to the application of proposed Rule 10D-1 to existing statutory provisions, it appears to be unclear whether Subtitle E of Title IX of the Dodd-Frank Act, Accountability and Executive Compensation, preempts state law. Section 954 does not address this matter, nor is it covered in the Proposing Release.

With respect to the application of the compensation recovery policy required by Section 10D to current or former executive officers possibly causing an issuer to violate existing compensation contracts, please see our response to Question 98 below.

* * *

c. Board Discretion Regarding Manner of Recovery

i. Amount to Be Recovered

59. How and under what circumstances, if any, should the board of directors be able to exercise discretion regarding the amount to be recovered? What steps should the board of directors be required to take, if any, before exercising any permitted discretion about the amount to be recovered from individual executive officers?

We believe that the Commission's proposal to require issuers to recover excess incentive-based compensation *pro rata* based on the size of the original award in situations involving the Board of Directors' discretion as to the retention or payment of individual awards in allocating a "bonus pool"¹⁰¹ is overly prescriptive and inflexible. Consistent with our responses to Questions 51 through 57 above, we recommend that the Commission allow an issuer's Board of Directors to exercise discretion regarding the amount of excess incentive-based compensation to be recovered when discretion was used in determining the original award amount. Accordingly, where an issuer maintains an incentive plan in which the achievement of a financial reporting measure or measures determines the aggregate amount of the "bonus pool," we believe that the Board of Directors should have the discretion to work with the affected individuals to decide on how much will be recovered from each executive officer.¹⁰² Ultimately, the facts and circumstances of each specific situation will dictate how the Board of Directors balances the competing interests that come into play when enforcing its compensation recovery policy.

We further believe that an issuer's Board of Directors should be permitted to settle for less than the full recovery amount based on the exercise of its discretion to determine an outcome that is in the best interests of the issuer and consistent with the purpose of Section 10D of the Exchange Act. As discussed above, we believe that a compulsory requirement to recover the full amount of excess incentive-based compensation under all circumstances unnecessarily precludes a Board of Directors from exercising its fiduciary duties on behalf of shareholders based on its assessment of the facts and circumstances that exist at the time of recovery and may lead to inequitable results that are detrimental to the issuer.

¹⁰¹ See the Proposing Release, at Section II.B.3.c.1.

¹⁰² This approach would work in situations where, after giving effect to the financial restatement, the "bonus pool" was both sufficient and insufficient to support the amount to be recovered.

60. Are there any material tax considerations relevant to whether an issuer should be able to exercise discretion as to the amount of recovery? If so, please explain.

Please see our response to Question 35 above. In addition, we note that, while proposed Rule 10D-1 contemplates that issuers would have discretion over the manner of recovery of excess incentive-based compensation, it does not contemplate any such discretion with respect whether or not to seek recovery in the first place (with the two very limited exceptions previously noted).

61. Would the exercise of discretion by an issuer's board of directors on the amount to be recovered where discretion was used in determining the original award amount (e.g., in a pool plan) be consistent with the purpose of Section 10D? If so, how?

Please see our response to Question 59 above.

ii. Means of Recovery

62. Should an issuer's board of directors be able to exercise discretion regarding the means of recovery, as proposed? If so, how and under what circumstances should the board be able to exercise discretion regarding the means of recovery? Are there any steps the board should be required to take before it exercises any permitted discretion regarding the means of recovery?

We support the Commission's 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, including cancellation of outstanding and unvested compensatory awards (whether payable in cash or equity), cancellation of pending or future incentive-based awards (whether payable in cash or equity), an offset of the amount to be recovered against amounts otherwise payable by the issuer to the executive officer, or the adoption of a deferred payment arrangement.¹⁰³ We believe that this flexibility will help to mitigate some of the procedural complexities involved in enforcing the compensation recovery policy. Consistent with our belief that enforcement of a compensation recovery policy should not be overly prescriptive, we recommend that the Commission refrain from requiring specific steps be taken by a Board of Directors before its exercises discretion regarding

¹⁰³ Notwithstanding this recommendation, we support the suggestion of other commenters that in no event should an issuer be required to recover excess incentive-based compensation through the offset, reduction, or withholding of amounts from the other compensation of an executive officer if such action would violate Sections 401(a) or 409A of the Code or Section 206(d)(1) of the Employee Retirement Income Security Act of 1974 ("ERISA"), each as amended. See the letter of The Society of Corporate Secretaries & Governance Professionals dated September 18, 2015, at page 12.

any specific means of recovery.

63. Should any of the principles discussed in this section be codified?

Consistent with our response to Question 62 above, we do not support the codification of any of the principles discussed in the section covering the manner of recovery of excess incentive-based compensation.

64. Should deferred payment arrangements be permitted when an executive officer otherwise is unable to repay excess incentive-based compensation? If so, should the time period over which repayment may be deferred be limited?

Consistent with our response to Question 62 above, we believe that a deferred payment arrangement should be permitted as a means for recovering excess incentive-based compensation. Accordingly, we believe that, given the myriad of situations that may exist at the time that an issuer seeks to enforce its compensation recovery policy, such arrangements should be permitted:

- when an executive officer otherwise is unable to repay the excess incentive-based compensation that he or she has previously received;
- when an executive officer is able to demonstrate to the satisfaction of an issuer's Board of Directors that prompt recovery of excess incentive-based compensation would result in adverse tax or economic consequences (other than the mere inability to repay the compensation promptly); or
- when an issuer's Board of Directors determines that the prompt repayment of the excess incentive-based compensation would not be in the best interests of the issuer.

To ensure full transparency, we further recommend that an issuer be required to disclose and explain each exercise of discretion to permit a deferred payment arrangement so that security holders can evaluate how a Board of Directors has chosen to handle each situation where excess incentive-based compensation has been identified.

Finally, consistent with our belief that enforcement of a compensation recovery policy should not be overly prescriptive, we recommend that the Commission refrain from limiting the time period over which repayment of excess incentive-based compensation may be deferred.

65. If recovery does not occur reasonably promptly, this would constitute non-compliance with an issuer's policy. Should there be an explicit window of time within which an issuer must have recovered excess incentive-based compensation from an executive beyond which the

failure to recover would not be considered “reasonably prompt”? Why or why not? If so, what should that time period be?

As discussed in our response to Question 51 above, we believe that there are a variety of factors that must be taken into consideration in crafting an appropriate arrangement for the recovery of excess incentive-based compensation. Moreover, each situation will have to be evaluated on the basis of its own specific facts and circumstances. Consequently, we believe that the final version of Rule 10D-1 should not specify an explicit period of time within which recovery must be made. We believe that the specific disclosure items that are contained in proposed Item 402(w) provide ample motivation for an issuer to take recovery seriously and to act promptly to recover outstanding amounts.

66. Should an issuer be permitted to recover excess incentive-based compensation by netting incentive-based compensation overpayments with incentive-based compensation underpayments that result from restating financial statements for multiple periods during the three-year recovery period? For example, suppose an issuer’s restatement for a material error in revenue recognition results in a shift in revenue from the most recent year to an earlier year in the three-year period, such that an incentive payment in the earlier year would have been greater under the restatement. Should the issuer be permitted to recover the excess incentive-based compensation in the later year by crediting the earlier “underpayment”? Why or why not? Should the conclusion be different from the situation where the executive officer received incentive-based compensation due to the achievement of a cumulative performance goal for the three-year period based on the financial reporting measure? Why or why not?

We believe that, for purposes of enforcing their compensation recovery policy, issuers should be permitted to calculate excess incentive-based compensation by “netting” incentive-based compensation overpayments with incentive-based compensation underpayments that result from restating financial statements for multiple periods during the same three-year look-back period. As illustrated above, the ultimate objective of Section 10D of the Exchange Act is to put an issuer’s executive officers in the same position they would have been in had the subject financial statements been accurate from the outset. Absent the flexibility to “net” underpayments against overpayments, executive officers would not only have to bear the risk that incentive-based compensation purportedly earned is subject to subsequent forfeiture but also the prospect of not being able to receive amounts actually earned as substantiated by the restatement.

We also recommend that the Commission consider expanding this “netting” technique to what it really represents – the concept of “setoff.”¹⁰⁴ In our view, an issuer’s

¹⁰⁴ We also believe that the concept of “offset” is consistent with the Commission’s objective that repayments be made promptly.

Board of Directors should have the discretion to “setoff” an amount of excess of incentive-based compensation against any other amounts that are currently owing or could be owing in the future to the subject executive officer, such as earned but unpaid incentive compensation, non-qualified deferred compensation obligations, future compensation obligations, and/or other amounts, such as dividends on issuer stock that may be owed to the executive officer. We believe that the only limitation that should be placed on this flexibility is that the netting or offset be legally permitted.

We further believe that, in the case of a situation where an executive officer received incentive-based compensation due to the achievement of a cumulative performance goal for the three-year period based on the financial reporting measure, netting should also be permitted. Ultimately, the objective of Section 10D is to ensure that the incentive-based compensation paid to an issuer’s executive officers accurately reflects the financial performance that generated that payment. If a financial restatement results in an overpayment, as well as an underpayment (without regard to whether these results are linked to the same performance period), the final version of Rule 10D-1 should be crafted to ensure that an issuer can take this into consideration in determining whether the restatement resulted in any excess incentive-based compensation that must be repaid to the issuer.

67. One commenter suggested that we specifically authorize or approve of the use of a nonqualified deferred compensation plan (e.g., a “holdback plan” or “bonus bank”) to aid in the recovery of erroneously awarded incentive-based compensation. Would these or other mechanisms aid in the recovery of such compensation? Why or why not?

As discussed in our responses to Questions 51 and 52 above, we recommend the Commission provide an issuer’s Board of Directors with broad discretion to fashion an appropriate means of recovery of excess incentive-based compensation. We note, however, that the use of a “nonqualified deferred compensation plan” (at least as the term is normally understood) for such purposes may raise significant tax issues under Section 409A of the Code.¹⁰⁵

It is our understanding that Section 409A contains specific rules regarding the documentation and operation of nonqualified deferred compensation plans.¹⁰⁶ In addition, Section 409A imposes severe tax penalties on employees for violations of these rules. Among other things, Section 409A generally prohibits the settlement of a current employee debt in an amount over \$5,000 by reducing the amount of deferred compensation the employee is scheduled to receive at a future time.¹⁰⁷ This general prohibition on what is considered an impermissible “acceleration” of a deferred amount means an issuer could not recover excess incentive-based compensation paid

¹⁰⁵ 26 U.S.C. 409A (2012).

¹⁰⁶ See Treas. Reg. 1.409A-1, -2, and -3.

¹⁰⁷ Under Section 409A, such a reduction would be considered an impermissible acceleration of a deferred compensation payment. See Treas. Reg. 1.409A-3(j) (4) (xiii).

to an executive officer by deducting the amount to be recovered from his or her nonqualified deferred compensation account (or, effectively, any other amount that is subject to Section 409A) without exposing him or her to a tax penalty.¹⁰⁸

Alternatively, we note that in conjunction with the reference to a “nonqualified deferred compensation plan,” the Commission references as examples of such a plan a “holdback plan” and a “bonus bank.” To the extent that such arrangements constitute “nonqualified deferred compensation plans” for purposes of Section 409A, the forfeiture of any excess incentive-based compensation deferred into such arrangements, as a recovery mechanism, is permissible and would not result in an accelerated payment under Section 409A. To the extent that these arrangements involve alternative plan forms, we recommend that the Commission refrain from authorizing or approving an exclusive list of permitted recovery mechanisms. As discussed previously, we believe that the Board of Directors is in the best position to evaluate the myriad of situations that arise in enforcing the compensation recovery policy. In our view, the Board of Directors is best-suited, through the exercise its business judgment, to select a means of recovery that is in the best interests of the issuer and consistent with the purpose of Section 10D of the Exchange Act.

4. Compliance with Recovery Policy

68. Should Rule 10D-1 specify the time by which the issuer must complete the recovery of excess incentive-based compensation required by the listing standards?

We believe that the final version of Rule 10D-1 should not specify a time by which an issuer must complete recovery of excess incentive-based compensation. We are concerned that, given the contemplated scope of the mandated compensation recovery policy, as well as the multitude of permutations that may arise, issuers would be at significant risk of missing any specified deadline for recovery. For example, significant challenges and delays may arise in recovering excess incentive-based compensation from executive officers who have terminated their employment with the issuer. Similarly, if an executive officer elects to litigate either the application of the compensation recovery policy, or the amount to be recovered, lengthy delays may result, making it impractical, if not impossible, for the issuer to meet any required deadline. Further, a specified time limit would be especially problematic where recovery could create a personal hardship for a particular executive officer, or where the funds to be recovered are no longer available to him or her.

We believe that any specified time period to complete recovery would have to provide for exceptions to address these possibilities (as well as any other situations where recovery could be delayed), thereby adding needless complexity to an already

¹⁰⁸ We understand that there may also be an issue if the documentation for an arrangement that is subject to Section 409A provides for recovering amounts owed by the executive officer, even if recovery is to take place at the originally scheduled payment date. See the Preamble Section VIII.A. to Application of Section 409A to Nonqualified Deferred Compensation Plans, 72 Fed. Reg. 19234, 19266 (Apr. 17, 2007).

severely prescriptive rule. In our view, the proposed identification of any individual from whom, as of the end of the last completed fiscal year, excess incentive-based compensation had been outstanding for 180 days or longer since the date the issuer determined the amount the individual owed is sufficient motivation for both the issuer and the subject executive officer to complete the recovery expeditiously.

Please also see our response to Question 76 below.

69. Should Rule 10D-1 provide an objective standard to determine whether an issuer is complying with its recovery policy? For example, if the issuer has not recovered a certain percentage of excess incentive-based compensation within a certain time period after a restatement that triggers application of the policy, should it be deemed non-compliant? If so, what percentages or time periods should be used, and why?

We believe that the Commission should not modify proposed Rule 10D-1 to provide an objective standard to determine whether an issuer is complying with its recovery policy. As we discuss in our response to Question 51 above, we prefer that Boards of Directors be given broad discretion to fashion both the means and timing of recovery, based on all of the relevant facts and circumstances of each specific situation. We are concerned that, by its very nature, any objective standard mandating full or partial recovery within a specified time period would be insufficiently flexible to address the myriad of issues that may arise in the course of enforcing a compensation recovery policy. Similarly, a standard combining both objective and subjective criteria would be subject to the same limitations, as well as an additional one – the risk of spurious claims by plaintiffs who seek to second-guess the decisions of an issuer's Board of Directors. By permitting it to exercise its discretion with respect to the manner of recovery,¹⁰⁹ the Commission is implicitly relying on the collective judgment of the members of the Board of Directors in balancing the various items that will go into any recovery – the type of compensation arrangement involved, the ability of the affected individual to return erroneously-awarded amounts, and the interests of the issuer – and its security holders – to implement and enforce the effects of the restated financial results.

We firmly believe that Boards of Directors will be sufficiently motivated both by their fiduciary obligations, as well as the implicit pressure that is likely to result from the required disclosure, to take appropriate action to recover excess incentive-based compensation in an expeditious and pragmatic manner. Additional detailed requirements that will either govern or impact the manner of recovery would simply make an already overly-prescriptive rule even more formalistic and difficult to enforce.

70. Alternatively, should Rule 10D-1 provide a standard that includes different subjective criteria, or both subjective and objective criteria, to determine

¹⁰⁹ See the Proposing Release, at Section II.C.3.c.

whether an issuer is complying with its recovery policy? If so, what standard should be used and why?

Please see our response to Question 69 above.

* * *

72. Could proposed Rule 10D-1 be revised to better ensure compliance with the obligation to recover? If so, how?

Please see our response to Questions 51 and 52 above.

D. Disclosure of Issuer Policy on Incentive-Based Compensation

1. **Listed U.S. Issuers**
2. **Listed Foreign Issuers**

73. Is the proposed approach of having the listing standard require an issuer to disclose its compensation recovery policy an appropriate means to implement Sections 10D(a) and 10D(b)(1)?

We support the Commission's proposal to have the listing standard require an issuer to file all disclosures with respect to its compensation recovery policy in accordance with the requirements of the federal securities laws.¹¹⁰ We agree that such an approach will facilitate the ability of the national securities exchanges and associations to commence delisting proceedings for issuers that fail to make the required disclosure, as well as those issuers that fail to adopt or enforce their compensation recovery policy. And, as noted, it will also enable the Commission to monitor the disclosure to the same extent that it has oversight of the disclosure required in other filings under the federal securities laws.

74. Would it be preferable to implement the disclosure requirement only through issuer disclosure requirements? Alternatively, would it be preferable to make the disclosure requirement solely a listing standard requirement? If so, please explain why.

We support the Commission's proposal to implement the disclosure requirement of Section 10D(b)(1) of the Exchange Act through the use of a listing standard requirement that looks to the federal securities laws for the specific details of the necessary disclosure. We see no compelling reason to require this information only through issuer disclosure requirements or, alternatively, solely through a listing standard requirement. As noted in our response to Question 73 above, we agree with the Commission that the national securities exchanges and associations should be able to

¹¹⁰ See proposed Rule 10D-1(b)(1).

determine an issuer's status for continued listing, in part, on its satisfaction of its disclosure obligations with respect to its compensation recovery policy. Further, we agree that this dual approach to the disclosure requirement would ensure that the content and operation of an issuer's compensation recovery policy was subject to Commission oversight to the same extent as other disclosure required in Commissions filings.

75. Should a listed issuer be required, as proposed, to file as an exhibit to its Exchange Act annual report its policy regarding the recovery of incentive-based compensation that is based on or derived from financial information required to be reported under the securities laws? Are there better ways to disclose the policy? Should the policy be included in the text of the Exchange Act annual report?

Rather than require listed issuers to file as an exhibit to their Exchange Act annual report their mandated compensation recovery policy, 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. In the event that a current copy of the policy was not available to security holders on the issuer's Web site, the issuer would be required to include a copy of the policy in an appendix to its proxy or information statement that is provided to security holders at least once every three fiscal years, or if the policy has been materially amended since the beginning of the issuer's last fiscal year. Finally, if a current copy of the policy was not available to security holders on the issuer's Web site, and is not included as an appendix to the issuer's most recent proxy or information statement, the issuer would be required to identify in which of the prior fiscal years the policy was so included in satisfaction of this requirement.

In our experience, many issuers already disclose their formal compensation recovery policies on their corporate Web site and investors have become familiar with accessing such information, as well as an issuer's other corporate governance information, on such Web sites. Consequently, we believe that codifying this practice would not impose a significant burden on issuers. We also consider this approach to be a reasonable means for implementing Sections 10D(a) and 10D(b)(1) of the Exchange Act.

76. Would proposed Item 402(w) and the proposed amendment to Item 404 elicit the appropriate level of detail about how issuers have applied their recovery policies? Should listed issuers be required to disclose the names of executive officers from whom recovery has been forgone, the amounts forgone and the reason the listed issuer decided not to pursue recovery? Should listed issuers be required to disclose the names of executive officers from whom, as of the end of the last completed fiscal year, excess incentive-based compensation had been outstanding for 180 days or longer since the date the issuer

determined the amount the person owed? If not, are there different disclosures that should be required?

We believe that, with the modifications described below, proposed Item 402(w) and the proposed amendment to Item 404 of Regulation S-K would elicit a sufficient amount of detailed information about how a listed issuer has enforced its compensation recovery policy. Since the disclosure requirement should assume that a listed issuer's Board of Directors will act diligently to enforce its compensation recovery policy in the event that the policy is triggered, we do not believe that it is necessary to require a lengthy detailed explanation of the issuer's enforcement efforts to ensure that it discharges its obligations.

We believe that security holders (and the applicable national securities exchange or association) will want to know the four specific items enumerated in proposed Item 402(w)(b)(1):

- The date on which the listed registrant was required to prepare an accounting restatement;
- The aggregate dollar amount of excess incentive-based compensation attributable to such accounting restatement;
- Any estimate or estimates used in determining the excess incentive-based compensation attributable to the accounting restatement (if the financial reporting measure related to a stock price or TSR metric); and
- The aggregate dollar amount of excess incentive-based compensation that remains outstanding at the end of the last completed fiscal year.

In addition, we recommend that an issuer be required to generally identify the incentive-based compensation arrangements that were subject to recovery (for example, "the issuer's 20XX Executive Bonus Plan" or "restricted stock unit awards granted in 20XX"). We believe that a general understanding of the compensation plans or arrangements that were the source of the erroneously-awarded compensation will help to place into context the amount of excess incentive-based compensation resulting from the restatement.

Similarly, we believe that security holders will want to know whether the issuer has decided to forgo recovery of any portion of the excess incentive-based compensation attributable to such accounting restatement and, if applicable, the aggregate dollar amount for which recovery has been forgone, the number of individuals from whom the issuer decided not to seek recovery, and the reason or reasons for not seeking recovery. While an issuer may decide to voluntarily disclose additional information about the circumstances triggering the enforcement of its compensation recovery policy, we believe that this should be left to the discretion of the issuer's Board of

Directors to determine based on the specific facts and circumstances of each separate restatement.

Finally, we believe that investors would want to know the aggregate dollar amount, if any, of excess incentive-based compensation that, as of the end of the last completed fiscal year, had been outstanding for 180 days or longer since the date the issuer determined the amount the individual owed, the number of individuals from whom such amounts were outstanding, and the dollar amount of outstanding excess incentive-based compensation due from each such individual.

We do not support the Commission's proposal, as reflected in proposed Item 402(w), to require the identification of each individual executive officer subject to recovery of excess incentive-based compensation attributable to an accounting restatement from whom the listed issuer decided during the last completed fiscal year not to pursue recovery,¹¹¹ or the identification of each individual from whom, as of the end of the last completed fiscal year, excess incentive-based compensation has been outstanding for 180 days or longer since the date the issuer determined the amount the individual owed.¹¹² In the former case, we believe that it is sufficient for an issuer 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 that it is sufficient for an issuer 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 of excess incentive-based compensation remaining due from each such individual.

Owing to the "no fault" nature of the compensation recovery policy trigger and given the reputational stigma that may attach (however unintentional) to being identified as an individual who received erroneously-awarded compensation, we believe that such identification is wholly unwarranted, particularly where the individual in question had absolutely no involvement in the preparation of the issuer's financial statements.¹¹³ At most, we recommend limiting identification to named executive officers, whose names and compensation information are already subject to significant disclosure requirements.

77. Should an issuer also be required to disclose the basis of the determination of the amount of excess incentive-based compensation and any critical estimates used in determining the amounts? Should a listed issuer also be

¹¹¹ See proposed Item 402(w)(2).

¹¹² See proposed Item 402(w)(3).

¹¹³ While, arguably, the identification requirements may serve as almost as much of a deterrent to the registrant and its executive officers as the compensation recovery policy itself, we believe that disclosing this information goes too far as it may invite second-guessing of an issuer's rationale for not pursuing one or more executive officers who owe money and subject executive officers to embarrassing disclosure as to why they are unable to repay previously-received amounts.

required to disclose the process or procedures by which it will seek to recover excess incentive-based compensation for amounts in which it is seeking recovery? Why or why not? If not, what should be disclosed and why?

We believe that it is not appropriate to require issuers to disclose, either pursuant to proposed Item 402(w) or otherwise, the basis of the determination of the amount of excess incentive-based compensation to be recovered and/or any critical estimates used in determining such amount. Nor do we believe that it is necessary for security holders to know the process or procedures by which an issuer will seek to recover excess incentive-based compensation for amounts in which it is seeking recovery.

In our view, each of these items involves an internal decision that will be based on the subjective business judgment of the Board of Directors and may, at least in the case of the determination of excess incentive-based compensation, involve sensitive business information, the disclosure of which could result in competitive harm to the issuer. While we believe that it would be reasonable to require issuers to maintain appropriate documentation for production to their national securities exchange or association if necessary to further their oversight function,¹¹⁴ we also believe that the public disclosure of such information is not necessary for security holders to ascertain whether an issuer has a compliant policy and is enforcing such policy in a reasonable and timely manner.

78. As proposed, Item 402(w) disclosure would be required if at any time during the last completed fiscal year either a restatement was completed that required recovery pursuant to the listed issuer's compensation recovery policy, or there was an outstanding balance of excess incentive-based compensation based on application of that policy to a prior restatement. Should the disclosure proposed in Item 402(w) be required in both these circumstances? If not, please explain why. Will it be clear if a restatement was completed during a fiscal year, such that disclosure would be required? If not, what guidance should we provide? Alternatively, should listed issuers be required to disclose every restatement in Item 402(w) – even if recovery of excess incentive-based compensation is not required?

Subject to our response to Question 76 above, we support the Commission's proposal to require disclosure pursuant to proposed Item 402(w) if at any time during the last completed fiscal year either a restatement was completed that required recovery pursuant to the listed issuer's compensation recovery policy, or there was an outstanding balance of excess incentive-based compensation based on application of that policy to a prior restatement. The disclosure would address a shortcoming in current disclosure practice, where issuers disclose the existence and general design of their compensation recovery policy, but rarely disclose whether (or when) enforcement of the policy has been triggered. Such disclosure would serve as an incentive for issuers to take appropriate steps to enforce their policy promptly, or risk additional scrutiny

¹¹⁴ In our view, this would already be required to a large extent by proposed Rule 10D-1(b)(1)(iii)(B).

from their security holders and the applicable national securities exchange or association.

Consistent with our reading of proposed Item 402(w), we recommend that the Commission clarify that disclosure also would be required in each of the following situations, even though each situation may not result in the actual recovery of any excess incentive-based compensation:

- Following an accounting statement as described in proposed Rule 10D-1(b)(1), erroneously-awarded compensation is calculated, but no such compensation is actually recovered because the issuer's committee of independent directors responsible for executive compensation decisions (or, in the absence of such a committee, a majority of the independent directors serving on the Board of Directors) has made a determination that recovery of all such compensation would be "impracticable"; and
- Following an accounting statement as described in proposed Rule 10D-1(b)(1), an issuer's calculation results in no erroneously-awarded compensation.

While we find the language of proposed Item 402(w) to be sufficiently clear that, if an accounting restatement was completed during a fiscal year, disclosure would be required, in view of the precision provided in the proposed rule as to the date when an issuer is required to prepare an accounting restatement, we believe that it may be prudent to provide similar precision as to when the restatement is considered "completed" for purposes of identifying the correct fiscal year with respect to which such disclosure is required.

79. Should Item 402(w) disclosure be required even after an issuer has been delisted if it has not recovered all compensation under the policy?

Unless recovery has become "impracticable" (as provided in the proposed rule), we believe that disclosure under Item 402(w) should be required even after an issuer has been delisted if it has not recovered all of the erroneously-awarded compensation from the application of the issuer's compensation recovery policy. Based on our reading of proposed Item 402(w)(1) and (3), we understand that this disclosure would consist of:

- the aggregate dollar amount of excess incentive-based compensation that remains outstanding at the end of the last completed fiscal year (but, except as provided hereafter, not the names of the individuals from whom such amounts are owed);
- the name of each individual from whom, as of the end of the last completed fiscal year, excess incentive-based compensation has been outstanding for 180 days or longer since the date the issuer determined

the amount the individual owed; and

- the dollar amount of outstanding excess incentive-based compensation due from each such individual.

80. Would the proposed Item 402(w) disclosure properly track any amount of incentive-based compensation subject to recovery through the duration of the recovery obligation until that amount either is recovered or the listed issuer concludes that recovery would be impracticable? If not, how should we revise the disclosure requirement to better track such amounts?

We believe that the disclosure contemplated by proposed Item 402(w) should track any amount of incentive-based compensation subject to recovery through the duration of the recovery obligation until that amount either is recovered or the listed issuer concludes that recovery would be impracticable.

As provided in proposed Item 402(w)(1)(iv) and (2), for the fiscal year in which an accounting restatement requiring recovery of excess incentive-based compensation pursuant to a listed issuer's compensation recovery policy was completed, the issuer would be required to disclose the aggregate dollar amount of such compensation that remained outstanding at the end of that fiscal year,¹¹⁵ as well as the name of and amount forgone from each individual from whom the issuer has decided not to pursue recovery. In addition, as provided in proposed Item 402(w)(3), the listed issuer would be required to disclose the name of each individual from whom, as of the end of the last completed fiscal year, excess incentive-based compensation had been outstanding for 180 days or longer since the date the issuer determined the amount the individual owed (as well as the dollar amount of outstanding excess incentive-based compensation due from each such individual).

In our estimation, the combination of these two disclosure requirements would effectively give an issuer and its executive officers approximately six months from the date the issuer determined the amount of excess incentive-based compensation each individual owed to recover such compensation without requiring disclosure of the outstanding amount (either on an aggregate and/or individual basis depending on the specific facts and circumstances). In the initial and each subsequent fiscal year, the issuer would be required to disclose the status of any unrecovered amount until such amount either is recovered or it concludes that recovery would be "impracticable."

While, after the initial disclosure required by proposed Item 402(w)(1) and (3), an executive officer who failed to disgorge any excess incentive-based compensation within 180 days of the date the issuer determined the amount the individual owed (and

¹¹⁵ The only information that is not required to be disclosed at that time is the name of each individual from whom such excess incentive-based compensation remains outstanding (as well as the specific amount outstanding with respect to each such individual). As we discuss in our response to Question 76 above, we believe that, at this stage of the recovery process, identification of each such individual is not warranted.

assuming that the restatement requiring such recovery was completed in the same fiscal year) would not be subject to further disclosure until the filing of the proxy or information statement for the subsequent fiscal year, we believe that the unfavorable reaction to the initial disclosure coupled with the likelihood of additional future disclosure would be sufficient incentive for the issuer to vigorously pursue recovery.

81. Is there any additional information that would be important to investors that should be disclosed?

Please see our response to Question 76 above.

82. Should the disclosure proposed by Item 402(w) of Regulation S-K be required only in annual reports and proxy and consent solicitations, as proposed? If not, please explain why. Should the disclosure of a listed issuer's application of its recovery policy be implemented by amending the executive compensation disclosure requirements of Item 402, as proposed? Alternatively, should it be implemented by amending the Item 407 corporate governance disclosure requirements, or by adopting a new Item of Regulation S-K? If so, please explain why.

We support the Commission's proposal to require the disclosure proposed by Item 402(w) in annual reports on Form 10-K and proxy and consent solicitations. As proposed, the disclosure would be included along with the listed issuer's other Item 402 disclosure in annual reports on Form 10-K and any proxy and consent solicitation materials that require executive compensation disclosure pursuant to Item 402.¹¹⁶

Over the past decade, these filings have become the accepted means for providing the annual executive compensation disclosure required by Item 402 to investors. Further, pending adoption of final rules to implement Section 10D of the Exchange Act, the Compensation Discussion and Analysis has become the *de facto* location for issuers to disclose and describe their existing compensation recovery policy.¹¹⁷ Thus, we believe that investors have come to expect that the description of an issuer's compensation recovery policy and any related information will be included in its annual report on Form 10-K and/or definitive proxy statement and that, as a practical matter, it makes sense to encourage issuers to continue this practice.¹¹⁸

¹¹⁶ See Instruction 5 to proposed Item 402(w).

¹¹⁷ See Item 402(b)(2)(viii) of Regulation S-K [17 CFR 229.402(b)(2)(viii)], which includes, as an example of the kind of information that should be addressed, if material, in a registrant's Compensation Discussion and Analysis, registrant policies and decisions regarding the adjustment or recovery of awards or payments to named executive officers if the relevant registrant performance measures upon which they are based are restated or otherwise adjusted in a manner that would reduce the size of an award or payment.

¹¹⁸ The Commission has stated in the Proposing Release that, since proposed Rule 10D-1 would subject any current or former executive officer to recovery, rather than only the "named executive officers" whose compensation is subject to discussion in Compensation Discussion and Analysis, it is proposing the disclosure requirement as a separate item rather than as an amendment to Item 402(b) of Regulation S-K. See the Proposing Release, at Section II.D.1. Notwithstanding this position, we anticipate that many

For these reasons, we recommend that the Commission adopt its proposal to implement the disclosure of a listed issuer's application of its compensation recovery policy by amending the executive compensation disclosure requirements of Item 402. While, arguably, the disclosure could be implemented by amending the corporate governance disclosure requirements of Item 407 of Regulation S-K¹¹⁹ (or even by adopting a new Item under Regulation S-K), we believe that the widely-held perception of a compensation recovery policy as a compensation-related, rather than a governance-oriented, policy warrants its inclusion in the regulation's executive compensation disclosure requirement.

83. Should a listed issuer only be required to provide the disclosure proposed by Item 402(w) in a report to its listing exchange or association, rather than in its annual reports and proxy and consent solicitations? If detailed notification is provided to its exchange or association, what type of disclosure, if any, should be made in a listed issuer's Commission filings? Alternatively, should a listed issuer be required to provide the proposed Item 402(w) disclosure and, in addition, be required to make a separate notification to its exchange or association?

Please see our response to Question 82 above. We believe that, given the origins of and current practice involving the disclosure of compensation recovery policies, listed issuers should be expected to provide the disclosure contemplated by proposed Item 402(w) in their annual reports on Form 10-K and proxy and consent solicitations, as proposed. Since, to date, information about such policies has appeared as in these filings, we see no compelling reason to deviate from this practice.

Further, requiring listed issuers to provide the disclosure contemplated by proposed Item 402(w) only in a report to its listing exchange or association would appear to be inconsistent with Congress' objectives with respect to Section 954. In this regard, we agree with the Commission's reading of the specific language of Sections 10D(a) and (b) of the Exchange Act to require listed issuers to adopt, comply with, and provide disclosure about their compensation recovery policies. We believe that, to fulfill these objectives, this disclosure should be readily available to investors; something that would not occur if it were merely provided to the applicable national securities exchange or association.

We have no objection to a requirement that a listed issuer be required to make a separate notification to the national securities exchange or association on which its equity securities are listed, in addition to providing the disclosure required by proposed Item 402(w). In fact, this may be the most efficient way to inform security holders and

issuers will continue to address its compensation recovery policy and the related disclosure in their Compensation Discussion and Analyses. As the Commission notes, "[s]uch a practice could benefit investors by disclosing all compensation recovery information in a single location in the filing." *Id.*

¹¹⁹ 17 CFR 229.407.

the listing exchange or association as to both the substance of a listed issuer's compensation recovery policy and how it enforces this policy in practice. We believe, however, that any such notification requirement should originate with the applicable national securities exchange or association, consistent with its own decisions as to how it monitors compliance with its listing standards.

* * *

85. Should we require that the disclosure required by proposed Item 402(w) be tagged in XBRL format, as proposed? Should we require a different format, such as, for example, eXtensible Markup Language (XML)? Would tagging these disclosures enhance the ability of shareholders and exchanges to assess issuers' compliance with their recovery policies? Alternatively, instead of requiring that either of these disclosures be tagged, should tagging this disclosure be optional?

We recommend that the Commission reconsider its proposal to require the disclosure required by proposed Item 402(w) to be tagged in eXtensible Business Reporting Language ("XBRL") format. We note that, until this year, the Commission had not previously proposed that information required in proxy statements pursuant to Schedule 14A¹²⁰ be tagged in XBRL. This changed in April, when the Commission proposed that the disclosure to be required by proposed Item 402(v) be electronically formatted using XBRL in accordance with the EDGAR filing manual.¹²¹ Accordingly, the current proposal with respect to proposed Item 402(w) represents the second initiative to have information that would otherwise be included in a definitive proxy or information statement presented in XBRL.¹²²

We are not in favor of this formatting requirement because of the significant burden that it imposes on registrants (particularly small-cap and mid-cap companies) to develop appropriate processes and systems to convert their definitive proxy statement into an XBRL-compatible format and to allocate time for the necessary training and review for the team preparing the definitive proxy statement to implement the required XBRL tags.¹²³ Further, we are not aware of any evidence to support the conclusion that, since the imposition of the XBRL requirement in periodic reports filed under the Exchange Act, investors have been receptive to or benefited from the availability of information in this format.

¹²⁰ See Pay Versus Performance, Release No. 34-74835 (Apr. 29, 2015) [80 FR 33589] (the "Pay Versus Performance Release").

¹²¹ See proposed Item 402(v)(6); see also the Pay Versus Performance Release, at Section II.B.2.

¹²² We acknowledge that, pursuant to proposed Item 402(v)(6), this information would also be required as an exhibit to an annual report on Form 10-K (17 CFR 249.310).

¹²³ We note that the Advisory Committee on Small and Emerging Companies has recommended that the Commission exempt smaller reporting companies from XBRL tagging. See the Letter from the Securities and Exchange Commission Advisory Committee on Small and Emerging Companies to the Honorable Mary Jo White, Chair, U.S. Securities and Exchange Commission dated September 23, 2015.

Further, we do not believe that the information that would be disclosed pursuant to proposed Item 402(w) necessarily lends itself to meaningful comparability among registrants. We fail to see how investors benefit from being able to compare the aggregate dollar amount of excess incentive-based compensation attributable to an accounting restatement, the aggregate dollar amount of excess incentive-based compensation that is outstanding at the end of the last completed fiscal year, or the dollar amount of excess incentive-based compensation that has been outstanding for 180 days or more. Since financial restatements are episodic in nature, the underlying reason or reasons for the restatement, the relevant facts and circumstances, and the frequency of their occurrence will be specific to each individual registrant. In addition, any resulting excess incentive-based compensation attributable to the restatement, as well as the registrant's ability to recover this compensation, will depend on the specific design of the incentive-based compensation plan or arrangement, the financial wherewithal of each affected executive officer, and the methods of recovery approved by the registrant's Board of Directors.

While we support the goal of making executive compensation information easier for investors to process and analyze, we do not recommend that the Commission begin this initiative with this particular rule. We view the information that would be tagged to be wholly contextual to each registrant's specific situation and, therefore, of little general value to investors beyond providing an understanding of how an individual registrant has responded to the identification of erroneously-awarded compensation. Combined with the potential for such information to be misleading to investors, we believe that the perceived benefit of tagging this information in an XBRL format does not outweigh the compliance burden to registrants.

86. Is the burden to implement the proposed tagging requirements comparatively greater for smaller reporting companies and emerging growth companies than for other issuers, such that we should exempt them or provide them a phase-in period for this requirement? If so, please explain the differential burden and how long a phase-in period it would justify.

Should the Commission decide to ultimately require the disclosure contemplated by proposed Item 402(w) to be tagged in the XBRL format, for the reasons set forth in our response to Question 85 above we recommend that smaller reporting companies and emerging growth companies be exempted from such requirement given the disproportionate compliance costs that such registrants will experience compared to the limited benefits to be derived from investors from such tagging. Alternatively, we recommend that such registrants be given a phase-in period of at least 12 months to develop appropriate processes and systems to convert their definitive proxy statement into an XBRL-compatible format and to allocate time for the necessary training and review to prepare the definitive proxy statement for the required XBRL tags.

* * *

88. Is the proposed instruction to Item 404(a), which would exclude a transaction involving recovery of excess incentive-based compensation that is disclosed pursuant to Item 402(w) from disclosure as a related party transaction, appropriate? Why or why not?

We support the Commission's proposal to add an instruction to Item 404(a) of Regulation S-K which would exclude a transaction involving the recovery of excess incentive-based compensation that is disclosed pursuant to Item 402(w) from disclosure as a related party transaction.¹²⁴ As proposed, an issuer would be required to provide the information specified in proposed Item 402(w) as to how it has applied its compensation recovery policy in its annual report on Form 10-K¹²⁵ and its definitive proxy¹²⁶ or information¹²⁷ statement as part of its executive compensation disclosure. In our view, since most investors consider compensation recovery policies to be either corporate governance-related or a feature serving to mitigate compensation-related risk, disclosure as part of an issuer's executive compensation disclosure is the most logical – and expected – location for this information. Requiring the disclosure as part of an issuer's related party disclosure would be, at best, duplicative and, at worst, potentially misleading.

89. In the Summary Compensation Table, should any amount recovered pursuant to a listed issuer's recovery policy reduce the amount reported in the applicable column for the fiscal year in which the amount recovered initially was reported, as proposed? For example, with respect to equity awards, should the then-probable grant date fair value reported be reduced by the portion of that grant date fair value attributable to the number of shares or options recovered? Should this disclosure be required in any filing containing Summary Compensation Table disclosure? Should we require similar reductions in amounts reported in compensation tables required for registered management investment companies? Why or why not? Are there any special considerations relating to registered management investment companies that make disclosing this information more or less useful than similar disclosure by operating companies? If so, please describe.

We support the Commission's proposal to add an instruction to Item 402(c) of Regulation S-K that would permit listed issuers to reduce the amount reported in the applicable column of the Summary Compensation Table by any amount recovered pursuant to the issuer's compensation recovery policy for the fiscal year in which the amount recovered initially was reported.¹²⁸ To the extent that a named executive

¹²⁴ See proposed Instruction 5.a.iii to Item 404(a) of Regulation S-K.

¹²⁵ See Item 11 of Form 10-K (17 CFR 249.310).

¹²⁶ See Item 8 of Schedule 14A (17 CFR 240.14a-101).

¹²⁷ See Item 1 of Schedule 14C (17 CFR 240.14c-101).

¹²⁸ See proposed Instruction 5 to Item 402(c). See also proposed Instruction 5 to Item 402(n) of Regulation S-K which would apply the same reporting principle to smaller reporting companies. As we understand this proposal, it would affect the "Stock Awards" column (column (e)), the "Option Awards" column

officer has been required to return any erroneously-awarded compensation to the issuer, we believe that the amount being reported in the Summary Compensation Table with respect to such compensation should be adjusted to reflect this subsequent development if the covered fiscal year is still being included in the table.¹²⁹ If the amount recovered involves incentive-based compensation that was originally paid in cash, then this adjustment would be made on a dollar-for-dollar basis. If the amount recovered involves incentive-based compensation that was originally delivered in the form of shares of or options for the issuer's stock, we agree that the appropriate adjustment would be to reduce the grant date fair value previously reported by the portion of the award's grant date fair value attributable to the number of shares or options recovered.

As proposed, to minimize investor confusion, we agree that the listed issuer should be required to add a footnote to the applicable column identifying the reduction in the previously reported amount, as well as the reason for the reduction.

Finally, we note that the Commission has proposed the adoption of a new "Pay Versus Performance" table¹³⁰ in connection with its rulemaking to implement Section 953(a) of the Dodd-Frank Act.¹³¹ Among other things, this new table requires issuers to disclose, for each of their last five completed fiscal years:

- The Principal Executive Officer's total compensation for the covered fiscal year as reported in the Summary Compensation Table pursuant to Item 402(c)(2)(x) of Regulation S-K, or Item 402(n)(2)(x) for smaller reporting companies (column (b)), and the average total compensation reported for the remaining named executive officers reported pursuant to those paragraphs (column (d));¹³² and
- The executive compensation actually paid to the Principal Executive Officer (column (c)) and the average executive compensation actually paid to the remaining named executive officers (column (e))¹³³.

(column (f)), and the "Non-Equity Incentive Plan Compensation" column (column (g)) of the Summary Compensation Table.

¹²⁹ If excess incentive-based compensation has been recovered for a fiscal year that is no longer required to be included in the Summary Compensation, we recommend that the final rule make clear that such amount need not be disclosed in the table, a footnote to the table, or the narrative accompanying the table as required by Item 402(e) of Regulation S-K. For example, assume that in June 2018 a listed issuer with a calendar year fiscal year concludes that, because of a material error, it is required to prepare a restatement of its previously-issued financial statement for 2016. As set forth by its compensation recovery policy, any incentive-based compensation received by any individuals who served as executive officers 2015, 2016, and 2017 – the three completed fiscal years immediately preceding the date the issuer was required to prepare the restatement – would be subject to recovery.

¹³⁰ See proposed Item 402(v)(1).

¹³¹ See the Pay Versus Performance Release, at Section II.B.2.

¹³² See proposed Item 402(v)(2)(ii).

¹³³ See proposed Item 402(v)(2)(iii).

Similar to the adjustment to the Summary Compensation Table contemplated by the proposed instruction to Item 402(c), we request that the Commission provide guidance as to how the compensation information that would be required pursuant to proposed Item 402(v)(2)(ii) and (iii) is to be adjusted (that is, reduced) in the event that a current or former named executive officer has been required to return any erroneously-awarded compensation to the issuer to reflect this subsequent development.

90. Our rules permit emerging growth companies and smaller reporting companies to provide scaled disclosure of certain requirements. Should the proposed disclosure rules for incentive-based compensation recovery policies be scaled for these companies? If so, please explain why and in what manner.

In our response to Question 1 above, we strongly recommend that the Commission exercise its general exemptive authority under the Exchange Act to exclude smaller reporting companies and emerging growth companies from the final version of Rule 10D-1 as being necessary or appropriate in the public interest and consistent with the protection of investors. Alternatively, should the Commission ultimately decide to apply the final version of Rule 10D-1 to all listed issuers, we request that the Commission consider relaxing the proposed disclosure requirements for incentive-based compensation recovery policies for such issuers. Specifically, we recommend that proposed Item 402(w) be modified to provide that, in the case of smaller reporting companies and emerging growth companies that take advantage of the scaled disclosure requirements of Item 402(n) of Regulation S-K,¹³⁴ such companies provide the following information:

- For each restatement:
- The date on which the listed registrant was required to prepare an accounting restatement (as defined in proposed Rule 10D-1(c)(2)); and
- The aggregate dollar amount of excess incentive-based compensation attributable to such accounting restatement;
- If during the last completed fiscal year the listed registrant decided not to pursue recovery from any individual subject to recovery of excess incentive-based compensation attributable to an accounting restatement, for each such individual, the name and amount forgone; and

¹³⁴ 17 CFR 229.402(n).

- The name of each individual from whom, as of the end of the last completed fiscal year, excess incentive-based compensation had been outstanding for 180 days or longer since the date the issuer determined the amount the individual owed, and the dollar amount of outstanding excess incentive-based compensation due from each such individual.

In the case of any estimate or estimates used to determine the excess incentive-based compensation attributable to such accounting restatement, if the financial reporting measure related to a stock price or total shareholder return metric,¹³⁵ we believe that such information should simply be made available upon request to the applicable national securities exchange or association. In our view, smaller reporting companies and emerging growth companies that use scaled disclosure should not be required to disclose what could be potentially lengthy descriptions and explanations of such estimates.

Similarly, we believe that smaller reporting companies and emerging growth companies that use scaled disclosure should not be required to disclose the aggregate dollar amount of excess incentive-based compensation that remains outstanding at the end of the last completed fiscal year.¹³⁶ Listed issuers will be expected to diligently enforce their compensation recovery policies. We believe that the implicit stigma that would result from requiring such issuers to disclose that they have not yet recovered the excess incentive-based compensation by fiscal year-end may compel them to incur additional legal and/or other costs to avoid this disclosure. We further believe that the disclosure required by proposed Item 402(w)(3), which would be triggered if excess incentive-based compensation had been outstanding for 180 days or longer since the date the amount owed had been determined the amount the individual owed, would provide sufficient incentive to ensure that such companies pursue the recoverable compensation.

Finally, in the case of the requirement to provide a brief description of the reason a listed registrant decided not to pursue recovery from any individual subject to recovery of excess incentive-based compensation attributable to an accounting restatement,¹³⁷ we believe that such information should simply be made available upon request to the applicable national securities exchange or association. In our view, smaller reporting companies and emerging growth companies that use scaled disclosure should not be required to disclose what could be a potentially lengthy explanation of the reason for not pursuing recovery. In our view, allowing such companies to omit such information from their disclosure will not deprive investors of critical information given the limited reason permitted under proposed Rule 10D-1(b)(1)(iv) for an issuer to forego recovery.

* * *

¹³⁵ See proposed Item 402(w)(1)(iii).

¹³⁶ See proposed Item 402(w)(1)(iv).

¹³⁷ See proposed Item 402(w)(2).

92. Should listed foreign private issuers, including MJDS filers, be exempt from the requirement to provide disclosure about compensation recovery policies? If so, please explain why.

Please see our response to Question 1 above. Consistent with our views as expressed therein as to the application of the final version of Rule 10D-1 to foreign private issuers, we recommend that the Commission require listed foreign private issuers to disclose their compensation recovery policy (or disclose that they do not maintain such a policy).¹³⁸

E. Indemnification and Insurance

93. Should we require the exchanges to adopt listing standards that would prohibit issuers from indemnifying executive officers and/or funding the purchase of insurance to protect against the risk that an executive officer will be subject to the issuer's recovery policy, as proposed?

We agree with the Commission's proposal to require the national securities exchanges and associations to adopt listing standards that would prohibit issuers from indemnifying their executive officers against the forfeiture of excess incentive-based compensation and/or funding or reimbursing the purchase of third-party insurance to protect against the risk that an executive officer will be subject to the issuer's compensation recovery policy. We believe that security holders should not bear the costs of providing such indemnification.

As the Commission notes, we expect that an active market for insurance will develop as a result of the adoption of proposed Rule 10D-1. Further, we expect that, as private insurance policies become available, some executive officers will purchase such policies to hedge the risk of loss of incentive-based compensation in situations where the material accounting error is not attributable to the executive officer.

However, while we believe that issuers should be prohibited from directly paying for or reimbursing their executive officers for the premiums for such policies, we also anticipate that the availability of such insurance may raise questions as to whether one or more components of an executive officer's total direct compensation¹³⁹ has been increased to offset the cost of such insurance.¹⁴⁰ In our view, it would be problematic for

¹³⁸ We note that this approach would be consistent with the Commission's requirement that foreign private issuers provide annual disclosure to their shareholders of the reasons why they do not have an independent compensation committee. See Exchange Act Rule 10C-1(b)(1)(iii) [17 CFR 240.10C-1(b)(1)(iii)].

¹³⁹ For this purpose, we are defining "total direct compensation" to mean the sum of base salary, annual bonus, and long-term incentive compensation.

¹⁴⁰ In fact, the Commission expressly states in its Economic Analysis that "[i]f an active insurance market develops such that the executive could hedge against the uncertainty caused by the recovery policy,

the national securities exchanges and associations to attempt to determine the reasons underlying increases in executive officers' compensation and we strongly urge the Commission to resist the temptation to try to incorporate such a requirement into the proposed listing standard. We believe that any such requirement would introduce an unreasonable level of complexity and uncertainty into the indemnification prohibition. Further, we believe that any such requirement could subject issuers to potential second-guessing of their executive compensation decisions and, potentially, to costly and protracted litigation to defend their decisions against spurious claims by plaintiffs. The rationale for determining the amount of compensation paid by an issuer to its executive officers should be relevant only to the extent that the issuer is currently required to explain its decisions based on performance or retention. We believe that the existing executive compensation disclosure requirements, including the Compensation Discussion and Analysis and the compensation tables required by Item 402 of Regulation S-K, are sufficient to enable investors to determine whether they approve of an issuer's compensation policies and decisions.

94. Should such listing standards also prohibit issuers from indemnifying executive officers' litigation expenses in recovery actions?

We believe that the mandated listing standard should not prohibit issuers from indemnifying their executive officers' litigation expenses in compensation recovery actions. In our experience, issuers typically maintain indemnification agreements consistent with state law for their executive officers. Generally, these arrangements contain provisions which allow for the advancement of legal fees and expenses incurred in defending a claim brought by the issuer, if the executive officer acted "in good faith" and in a manner reasonably believed to be, or not opposed to, the best interests of the issuer.¹⁴¹ We believe that a claim pursuant to a compensation recovery policy required by Section 10D of the Exchange Act is consistent with the state law provisions on advancement.

95. As noted above, the anti-indemnification provisions of Rule 10D-1 would prohibit agreements, arrangements or understandings that directly or indirectly mitigate some or all of the consequences of recovery. Will the exchanges and issuers be able to distinguish between payments that are made to mitigate the effect of a recovery and those that are paid as compensation in the ordinary course of business?

As amply illustrated by the typical Compensation Discussion and Analysis, executive compensation decisions are based on a multitude of objective and subjective factors. Further, the significance of any individual factor is frequently not

then market-determined compensation packages would likely increase to cover the costs of such policy." See the Proposing Release, at Section III.B.5.

¹⁴¹ See 8 D.G.C.L. Section 145(b). Because of the conditions that must be satisfied for advancement provisions to be available, we believe that such provisions would not serve as an incentive for an executive officer to resist recovery, without regard to the merits of his or her defense.

capable of being quantified. Since, in our experience, executive compensation decisions are ultimately based on the expertise, experience, and business judgment of the members of the Compensation Committee of the Board of Directors, we believe that the national securities exchange or association (or, for that matter, the issuer itself) will be unable to distinguish between amounts that are being paid as compensation in the ordinary course of an issuer's business and amounts that are intended to mitigate the effect of a recovery where they are not specifically enumerated. Consistent with our response to Question 93 above, we believe it is not appropriate or necessary to require further analysis or disclosure to the specific rationale for the payment of compensation to executive officers. The ambiguity of this distinction is exacerbated by the overarching objectives of executive compensation elements – to motivate and incent an issuer's executive officers to achieve exemplary performance.

We are not aware of any analytical tools that presently exist that would enable the national securities exchanges and associations to effectively determine the primary reasons for a specific increase in the amount of an individual executive compensation element. Consequently, unless the Commission is prepared to provide specific guidance as the factors that the exchanges should consider in making this distinction, we believe that this is a subject which does not lend itself to effective regulation.

96. Should we define “indemnification” for purposes of the recovery under Section 10D? If so, how should it be defined? Should it require that there be an agreement on the part of the indemnitor in advance of the event for which the indemnitee is being indemnified?

We believe that the Commission should not define the term “indemnification” for purposes of the recovery of erroneously-paid compensation under Section 10D of the Exchange Act. In our view, leaving the term for interpretation by the national securities exchanges and associations, as well as issuers, may be the most effective way to discourage the rise of techniques intended to mitigate the effect of a recovery. For example, issuers may be less likely to take action to compensate their executive officers for the loss resulting from a recovery if they are concerned that such action may be considered as “indemnifying” the individual in contravention of proposed Rule 10D-1(b)(1)(v).

F. Transition and Timing

97. Is the proposed schedule for exchanges to file their proposed listing rules and have them effective following the effective date of proposed Rule 10D-1 workable and appropriate? Similarly, is the proposal to require each listed issuer to adopt the required recovery policy within 60 days following the effective date of the exchanges' listing rules workable and appropriate? If not, what other schedule should apply?

We believe that the Commission's proposed schedule for the national securities exchanges and associations to file their proposed listing standards and endeavor to

have them declared effective following the effective date of proposed Rule 10D-1 is both workable and appropriate. Given the detail provided in proposed Rule 10D-1 (b) and (c) as to the content of the required standard, we do not anticipate that the exchanges should have any difficulty in submitting their proposed listing standards within the 90-day period contemplated by proposed Rule 10D-1 (a) (2) (i). Nor do we anticipate that, once reviewed and approved by the Commission, the exchanges should encounter any difficulty in having these standards declared effective within one year of the publication of the final rule in the Federal Register. We note that, to promote consistency in the application of the compensation recovery policies among issuers, the Commission is unlikely to approve standards that deviate significantly among the national securities exchanges and associations. Consequently, we expect that the proposed standard filed with the Commission by each national securities exchange and association will be similar in both form and substance, thereby minimizing the need for lengthy and protracted negotiations between the Commission and the exchanges to arrive at mutually-agreed final standards.

With respect to the proposal to require each listed issuer to adopt the required compensation recovery policy within 60 days following the effective date of the applicable national securities exchange's or association's listing standard, please see our response to Question 1 above, in which we request that, should the Commission ultimately decide to apply proposed Rule 10D-1 to all listed issuers, it provide additional time for smaller reporting companies and emerging growth companies to adopt a compliant compensation recovery policy. Specifically, instead of the contemplated 60-day period, we recommend that listed smaller reporting companies and emerging growth companies be given at least two years to adopt the policy required by proposed Rule 10D-1.

98. Should the Commission provide that the recovery policy will apply to require recovery of all erroneously awarded incentive-based compensation received by a current or former executive officer on or after the effective date of Rule 10D-1 that results from attaining a financial reporting measure based on or derived from financial information for periods that end on or after the effective date of Rule 10D-1, as proposed? Alternatively, should the recovery policy apply to incentive-based compensation received by an executive officer on or after the effective date of the exchange's listing standard that results from attaining a financial reporting measure based on or derived from financial information for periods that end on or after the effective date of Rule 10D-1? If neither of these alternatives, what date(s) would be more appropriate and why? Should the Commission consider the date of compensation agreements and the ability of issuers to modify those agreements as part of the transition? If so, how?

We recommend that the Commission provide that the compensation recovery policy required by Section 10D of the Exchange Act will 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.¹⁴² We believe that requiring issuers, as proposed, to apply their mandated compensation recovery policy (which may not be formally adopted until as late as mid-November 2017) to erroneously-awarded 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 create needless complexity and uncertainty.

We also believe that such a result would be grossly unfair, and subject to challenge in a court of law, as it potentially applies the prescriptive terms of the mandated compensation recovery policy to compensation that was granted or awarded up to three years before the specific terms and scope of the mandated policy were known, but that is subject to a performance period that ends after the effective date of the final version of Rule 10D-1.

We believe that such retroactive application would present significant challenges for issuers with an existing compensation recovery policy. Further, executive officers would be faced with the prospect of forfeiture of potentially significant amounts of compensation pursuant to a policy that may be materially different from the compensation recovery policy that they understood (and possibly even affirmatively agreed) would apply to their compensation arrangements.¹⁴³

Finally, the proposed transition provision presents an issue with respect to pre-existing employment agreements and incentive-based compensation awards that may not permit the kind of recovery contemplated by proposed Rule 10D-1. In the Proposing Release, the Commission states that any inconsistency between the proposed rule and existing employment agreements should not, in itself, create a conflict "because issuers can amend those contracts to accommodate recovery."¹⁴⁴ In our experience, this is typically not the case. As a matter of contract law, issuers cannot unilaterally amend an employment agreement; particularly if the amendment would be viewed as adverse to the other party. Instead, an issuer would need to seek the consent of the affected individual and, possibly, offer new consideration for the amendment. There is no assurance that the affected individual would agree to such an amendment, especially where the effect would be to his or her disadvantage by permitting the forfeiture of a potentially significant portion of his or her compensation.

¹⁴² Until such time, we believe that an issuer's pre-existing compensation recovery policy (as in effect as of the effective date of the Proposing Release or subsequently adopted or amended) should govern the disposition of its executive or other compensation in the event of a financial restatement.

¹⁴³ In the Proposing Release, the Commission acknowledged this possibility in at least one situation – where both proposed Rule 10D-1 and Section 304 of the -Oxley Act could provide for recovery of the same incentive-based compensation. See the Proposing Release, at Section II.C.3.a. While the Commission is unable to eliminate this possibility, we see no reason why, in providing transition guidance, it needs to exacerbate this situation by requiring for retroactive application of proposed Rule 10D-1.

¹⁴⁴ See the Proposing Release, at footnote 182 and the accompanying text.

Such an amendment could be further complicated for executive officers located in a foreign jurisdiction, where employment laws and standards for employment agreements may differ significantly from those in the United States. This issue is further exacerbated in the case of individuals who are both former executive officers and former employees, who would have no incentive to cooperate with a former employer unless offered meaningful consideration. Consequently, to avoid these problems, we believe that the final version of Rule 10D-1 should be applied on a prospective basis only so that employment agreements entered into in the future can be drafted to contain appropriate provisions to address this issue.

Since we believe that Congress did not intend for Section 10D to have retroactive effect, we urge the Commission to reconsider its approach to transition timing and only apply the final version of Rule 10D-1 to incentive-based compensation that is granted or awarded after an issuer adopts a compliant compensation recovery policy following the effective date of the listing standard of the applicable national securities exchange or association as approved by the Commission. Alternatively, should the Commission ultimately decide to not to apply the final version of Rule 10D-1 on a wholly prospective basis, we request that it provide that the compensation recovery policy required by Section 10D will apply only to erroneously-awarded compensation that is granted or awarded after the effective date of the final version of Rule 10D-1.

99. Is there anything the Commission should do to address the potential effect proposed Rule 10D-1 will have on existing compensation plans and employment agreements that do not contemplate recovery under a policy required by the rule and rule amendments implementing Section 10D? To what extent will issuers need to amend their existing compensation plans and employment agreements to provide for the application of the recovery policy? Should the recovery policy only apply to new compensation plans and employment agreements entered into after the effective date of the exchange's listing standard? Why or why not?

We agree with the Commission's concern that the currently contemplated implementation of proposed Rule 10D-1 would have (in our view) a significant effect on existing compensation plans and employment agreements that do not contemplate recovery under a policy that reflects the features and conditions of the proposed rule. With respect to an existing compensation plan, a listed issuer should be able to amend any such plans to ensure that future awards granted pursuant to such plan will be subject to its compensation recovery policy.

However, as we have discussed in our response to Question 98 above, we believe that, given the likelihood that extending the issuer's compensation recovery policy to such arrangements will be considered an adverse event, existing employment agreements and outstanding incentive-based compensation awards cannot be amended or otherwise modified without the consent of the other party. As we explained above, these individuals may not be willing to consent to the application of

the compensation recovery policy to these arrangements without receiving additional benefits in exchange.

Consequently, as noted above, we request that the Commission only apply the final version of Rule 10D-1 to incentive-based compensation that is granted or awarded after an issuer adopts a compliant compensation recovery policy following the effective date of the listing standard of the applicable national securities exchange or associations as approved by the Commission. Alternatively, should the Commission ultimately decide to not to apply the final version of Rule 10D-1 on a wholly prospective basis, we request that it provide that the compensation recovery policy required by Section 10D of the Exchange Act will apply only to erroneously-awarded compensation that is granted or awarded after the effective date of the final version of Rule 10D-1.

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We appreciate the opportunity to comment on the Proposing Release and respectfully request that the Commission consider our recommendations and suggestions. We are available to meet and discuss these matters with the Commission and its staff, and to respond to any questions.

Very truly yours,

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