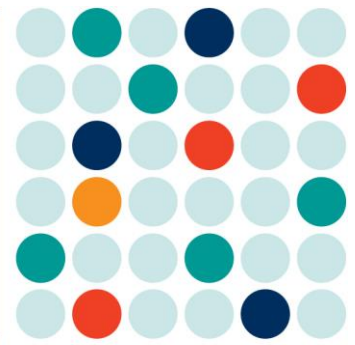


# LEGAL UPDATE

July 2015

By: Michael T. Campoli



## SEC DIGS ITS CLAWS INTO EXECUTIVE COMPENSATION

On July 1, 2015, the U.S. Securities and Exchange Commission (the “SEC”) proposed rules that would require the national securities exchanges to establish standards requiring the companies listed on such exchanges to adopt policies to “claw-back” from their executive officers incentive-based compensation that was erroneously awarded to such officers. The proposed rules are required by Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

### ADOPTION OF “CLAW-BACK” POLICY

The proposed rules, which would be codified in a new Rule 10D-1 under the Securities Exchange Act of 1934 (the “Exchange Act”), would require listed companies to develop and enforce recovery policies that, in the event of an accounting restatement, “claw-back” from current and former executive officers<sup>1</sup> incentive-based compensation that they would not have received based on the restatement. Any incentive-based compensation that was received during the three fiscal years preceding the date on which the company is required to prepare an accounting restatement to correct a material error would be subject to the claw-back.

Companies would be required to recover the amount of incentive-based compensation received by an executive officer that exceeds the amount that the executive officer would have received had the incentive-based compensation been determined based on the restated financial statements. For incentive-based compensation that is based on stock

price or total shareholder return, companies would be permitted to use a reasonable estimate of the effect of the restatement on the applicable measure to determine the recovery amount.

Recovery would be required on a “no-fault” basis – i.e., without regard to whether any misconduct occurred or whether the particular officer was responsible for the erroneous financial statements.

“Incentive-based compensation” is defined as compensation granted, earned or vested, based wholly or in part on the attainment of any financial reporting measure. Incentive-based compensation is deemed “received” at the time the financial measure is achieved, even if the payment or grant occurs on a later date, or there are additional payment requirements such as time-based vesting or certification by the compensation committee that have not yet been satisfied. “Financial reporting measures” are those based on the accounting principles used in preparing the company’s financial statements, any measures derived wholly or in part from such financial information, and stock price and total shareholder return.

### DISCLOSURE REQUIREMENTS

Listed companies would be required to publicly disclose the recovery policies that they have adopted, as well as the actions that they have taken under those policies. Specifically, each company would be required to file its recovery policy as an exhibit to its Exchange Act annual report. Each such company also would be required to disclose certain details regarding its recovery actions in its annual reports and any proxy statement that requires executive compensation disclosure if, during its last fiscal year, a restatement requiring recovery of excess incentive-based compensation was completed, or there was an outstanding balance of excess incentive-based compensation from a

<sup>1</sup> The definition of “executive officer” is modeled on the definition of “officer” under Section 16 of the Exchange Act, and includes the company’s president, principal financial officer, principal accounting officer, any vice-president in charge of a principal business unit, division or function, and any other person who performs policy-making functions for the company.

prior restatement. This information would include:

- The date on which such company was required to prepare each accounting restatement, the aggregate dollar amount of excess incentive-based compensation attributable to the restatement and the aggregate dollar amount that remained outstanding at the end of the last completed fiscal year;
- The name of each person subject to recovery from whom the company decided not to pursue recovery, the amounts due from each such person, and a brief description of the reason the company decided not to pursue recovery; and
- If amounts of excess incentive-based compensation are outstanding for more than 180 days, the name of, and amount due from, each person at the end of the last completed fiscal year.

## COMPANIES COVERED

As proposed, the rules would apply to all companies listed on national securities exchanges, including emerging growth companies, smaller reporting companies, foreign private issuers and controlled companies, with certain limited exceptions regarding registered investment companies and issuers of securities futures products or standardized options.

## CURRENT STATUS

The proposed rules are currently subject to a 60-day comment period. Following the publication of the final “claw-back” rules, the national securities exchanges would have 90 days to propose listing standards that are consistent with the final rules, which listing standards must be effective no later than one year following their publication. Given the number of steps required to fully implement the proposed rules, and the significant number of comments anticipated to the proposal, it is unlikely that new listing rules will be in place and effective prior to next year’s proxy season.

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*If you would like to learn more about this topic or how Pryor Cashman LLP can serve your legal needs, please contact Michael T. Campoli at [mcampoli@pryorcashman.com](mailto:mcampoli@pryorcashman.com), or any Pryor Cashman attorney with whom you are working.*

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Whether advising on financial investments to fuel emerging enterprises or counseling mature companies on vital business opportunities, Mike finds creative solutions that fit real-world objectives. He closely monitors trends in capital formation - especially investments related to the JOBS Act and crowdfunding - in order to provide sound, strategic guidance.