



CLIENT ALERT

Capital Markets/M&A Practice Group Update

September 1, 2015

SEC Proposes Executive Compensation Clawback

On July 1, 2015, the Securities and Exchange Commission issued a proposed rule for the clawback of executives' incentive-based compensation earned in connection with a material accounting restatement as well as the disclosure of the company's clawback policy and clawbacks caused by the policy. The proposed rule would put into practice the provisions of Section 954 of the Dodd-Frank Wall Street Reform and Protection Act of 2010 and Section 10D of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). This Client Alert gives only a brief summary of the proposal.

Proposed Rule

Briefly, the proposed rule would require national securities exchanges to adopt listing standards requiring listed companies to have a clawback policy to recover any incentive-based compensation paid to current and former executive officers during the three completed fiscal years preceding the date that a company is required to prepare an accounting restatement due to material non-compliance with financial reporting required under the federal securities laws. The recovery would be without regard to whether the executive officer engaged in misconduct or was responsible for the accounting error for causing the restatement. Further, recovery would apply to any compensation received after the restated period as long as it was based on the accounting non-compliance causing the restatement.

Recoverable Incentive-Based Compensation

The clawback would apply to any compensation attained wholly or in part based on any of following parameters that were or will have been impacted by the restatement:

- Measures, based in whole or in part, on accounting principles used in preparing the company's financial statements
- Company's stock price
- Company's aggregate shareholder return

Where the amount erroneously awarded is not subject to mathematical recalculation directly from the information in the restatement, the issuer must use a reasonable estimate of the effect of the accounting restatement on the stock price or total shareholder return upon which the compensation was based.

Amount Recoverable

The clawback would capture the amount of incentive compensation received by the executive officer that exceeds the amount to which he or she would have received had it been based on the restated financials. A company will be prohibited from indemnifying any executive officer against the loss of erroneously awarded compensation.

Executive Officers Covered

The definition of executive officer is similar to the definition of “officer” under Section 16 of the Exchange Act and includes:

- President
- Principal financial officer
- Principal accounting officer
- Any vice-president in charge of a principal business unit, division or function
- Any other person (including executive officers of a parent or subsidiaries) who performs policy-making functions

Exemptions to Recovery

There are exemptions to pursuing the recovery of the clawback provisions where the cost to enforce recovery exceeds the amount to be recovered and where recovery would violate the home country laws of any foreign issuer. However, the company must make a good faith effort to recover prior to concluding that recovery will be impractical.

Disclosure Requirements

A company listed on a national securities exchange would need to:

- Prepare and adopt a clawback policy and file the policy as an exhibit to its Form 10-K.
- If an accounting restatement results in a recovery or there is an outstanding balance from a recovery then details of the recovery or balance would need to be disclosed in the Form 10-K and proxy statement.

Timeline for Compliance

Securities exchanges would have to propose rules no later than 90 days after SEC adoption of the final rule and the rules must be effective no later than one year after the SEC adoption. Companies would be required to adopt clawback policies within 60 days after national securities exchanges’ listing rules become effective.

Disclosure requirements would begin upon the effective date of the national securities exchanges’ listing rules.

Comment Period

The proposal is subject to public comment through September 14, 2015. We will issue a Client Alert upon the adoption of the final rule.

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We are available to address your questions on the proposed executive compensation clawback provision. Please contact any of the attorneys below to discuss this Client Alert.

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