

## New York Stock Exchange Proposes New Compensation Clawback Rules

March 3, 2023

On February 22, 2023, the New York Stock Exchange (“NYSE”) proposed the adoption of new listing standards contained in the Corporate Governance section of the NYSE Listed Company Manual (the “Manual”). New [Section 303A.14](#) would “require issuers to develop and implement a policy providing for the recovery of erroneously awarded incentive-based compensation received by current or former executive officers.”

### Background

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In October 2022, the SEC adopted [Rule 10D-1](#) which implemented Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”). Section 954 directed “national securities exchanges and associations that list securities to establish listing standards that require each issuer to develop and implement a policy providing for the recovery, in the event of a required accounting restatement, of incentive-based compensation received by current or former executive officers where that compensation is based on the erroneously reported financial information.” The listing standards must require each listed issuer to:

- file written recovery policies as exhibits to annual reports;
- indicate by check boxes on annual reports whether the financial statements included in the filings reflect correction of an error to previously issued financial statements and whether any of those error corrections are restatements that required a recovery analysis; and
- disclose any actions they have taken pursuant to such recovery policies.

Rule 10D-1 became effective on January 27, 2023, and the exchanges’ listing standards must be effective by November 28, 2023.

The SEC also adopted amendments to Item 402 of Regulation S-K, Form 10-K, Form 40-F, Form 20-F, and Form N-CSR (for those listed funds subject to the compensation clawback rules), requiring a listed issuer to file its incentive compensation clawback policy as an exhibit to its annual report.

In addition, if a listed issuer has applied its policy, it must disclose:

- the date it was required to prepare an accounting restatement and the aggregate dollar amount of erroneously awarded compensation attributable to such accounting restatement (including the estimates used in calculating the recoverable amount in the case of awards based on the stock price or total shareholder return);
- the aggregate amount that remains outstanding and any outstanding amounts due from any current or former named executive officer for 180 days or more; and
- details regarding any reliance on the impracticability exceptions.

### Proposed NYSE Rule

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In response to Rule 10D-1, NYSE has proposed its incentive compensation clawback rule in new Section 303A.14 of the Manual. Section 303A.14 will require listed issuers “to develop and implement a policy providing for the recovery of erroneously awarded incentive-based compensation<sup>1</sup> received by current or former executive officers” and has been “designed to conform closely to the applicable language of Rule 10D-1.” In complying with Section 303A.14, issuers must agree to recover, in a reasonable and prompt manner, the amount of erroneously awarded incentive-

based compensation “in the event that the issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer with any financial reporting requirement under the securities laws, including any required accounting restatement to correct an error in previously issued financial statements that is material to the previous issued financial statements, or that would result in a material misstatement if the error were corrected in the current period or left uncorrected in the current period.”

Proposed Section 303A.14 establishes a timeframe for compliance with the new listing standards as follows:

- Each listed issuer must adopt the recovery policy required by proposed Section 303A.14 (“Recovery Policy”) **no later than 60 days** from the adoption of the proposed listing standard (“Effective Date”).
- Each listed issuer must comply with its Recovery Policy for all incentive-based compensation Received (as defined in proposed Section 303A.14(e) and as further discussed below) by current and former executive officers on or after the Effective Date that results from the attainment of a financial reporting measure based on or derived from financial information for any fiscal period ending on or after the Effective Date.
- Each listed issuer must provide the required disclosures in its applicable SEC filings required on or after the Effective Date.

If incentive-based compensation is tied to stock price or total shareholder return and the amount of erroneously awarded compensation is not subject to the calculations included in the accounting restatement, the amount of erroneously awarded compensation must reflect a reasonable estimate of the accounting restatement’s impact on stock price and total shareholder return tied to incentive-based compensation and the issuer must keep and disclose (to the NYSE) records of how the reasonable estimate was calculated.

The Recovery Policy of each issuer must require that the issuer recover erroneously awarded compensation unless one of the following is applicable:

- The direct expense paid to a third party to assist in enforcing the policy would exceed the amount to be recovered. Before concluding that it would be impracticable to recover any amount of erroneously awarded compensation based on expense of enforcement, the issuer must make a reasonable attempt to recover such erroneously awarded compensation, document such reasonable attempt(s) to recover, and provide that documentation to the NYSE.
- Recovery would violate home country law where that law was adopted prior to November 28, 2022. Before concluding that it would be impracticable to recover any amount of erroneously awarded compensation based on violation of home country law, the issuer must obtain an opinion of home country counsel, acceptable to the NYSE, that recovery would result in such a violation, and must provide such opinion to the NYSE.
- Recovery would likely cause an otherwise tax-qualified retirement plan, under which benefits are broadly available to employees of the registrant, to fail to meet the requirements of 26 U.S.C. 401(a)13<sup>2</sup> or 26 U.S.C. 411(a)<sup>3</sup> and regulations thereunder.

If any of the three conditions above are met, the issuer must then obtain permission from the issuer’s committee of independent directors with authority to decide on executive compensation, or if such a committee does not exist, from a majority of independent directors serving on the board, on the grounds that recovery would be impracticable.<sup>4</sup>

Proposed Section 303A.14 incorporates the three requirements outlined above as set forth in Rule 10D-1. It also outlines the requirements concerning the Recovery Policy and incentive-based compensation. The relevant recovery period is established in paragraph (c)(1) of Section 303A.14.

Rule 10D-1 and consequently Section 303A.14 apply to all U.S. issuers filing annual reports on Form 10-K and to foreign private issuers filing annual reports on Form 40-F or Form 20-F. It is important to note that the proposed Section 303A.14 will not apply to:

- Any security issued by a unit investment trust, as defined in 15 U.S.C. 80a-4(2) or

- Any security issued by a management company, as defined in 15 U.S.C. 80a-4(3), that is registered under Section 8 of the Investment Company Act of 1940, if such management company has not awarded incentive-based compensation to any executive officer of the company in any of the last three fiscal years, or in the case of a company that has been listed for less than three fiscal years, since the listing of the company.

In addition to the requirements outlined and discussed above, proposed Section 303A.14 defines key terms as they apply to the new rules, such as executive officer<sup>5</sup>, financial reporting measures<sup>6</sup>, incentive-based compensation<sup>7</sup>, and received<sup>8</sup>.

Should an issuer fail to comply with the requirements of proposed Section 303A.14, any initial or continued listing of any security of that issuer will be prohibited. In addition to Section 303A.14, the NYSE seeks to adopt a new Section 802.01F, which outlines penalties for issuers that, after the obligation is incurred, have not recovered erroneously-awarded compensation in compliance with the issuer's clawback policy in a reasonable and prompt manner. These penalties include immediate suspension of the trading of any securities of that listed issuer and the commencement of delisting procedures for all listed securities.

## What's Next

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Comments on the rule proposal may be submitted using the SEC's internet comment form available [here](#) or by sending an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov) with subject line File Number SR-NYSE-2023-12. The Commission has asked that comments be received on or before the date that is 60 days after the proposal's publication in the Federal Register<sup>9</sup>. As these proposed listing requirements are mandated by Section 954 of the Dodd-Frank Act and Rule 10D-1, it is likely that proposed Section 303A.14 of the Manual will be adopted substantially as proposed.

**Issuers subject to NYSE listing standards will be required to adopt a recovery policy no later than 60 days following the date on which the applicable listing standards become effective and must begin to comply with the disclosure requirements in proxy and information statements and the issuer's annual report filed on or after the issuer adopts its recovery policy.**

## For More Information

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If you would like further information concerning the matters discussed in this article, please contact a member of the Corporate and Securities Group or the Investment Management Group or visit us online at [chapman.com](http://chapman.com).

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- 1 Erroneously awarded compensation is defined as 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 restated amounts, and must be computed without regard to any taxes paid.
  - 2 26 U.S.C. 401(a)13 provides a general outline of qualified trusts, special rules for domestic relations orders, a special rule for certain judgments and settlements, and a determination of survivor annuity, as applied to qualified pension, profit-sharing, and stock bonus plans.
  - 3 26 U.S.C. 411(a) covers general rules for qualified trusts in relation to employee benefit plans.
  - 4 Section 303A.00 of the Manual provides an exemption from compliance with the NYSE's compensation committee requirements to listed companies that are foreign private issuers or controlled companies.
  - 5 *Executive Officer.* An executive officer is the issuer's president, principal financial officer, principal accounting officer (or if there is no such accounting officer, the controller), any vice-president of the issuer in charge of a principal business unit, division, or function (such as sales, administration, or finance), any other officer who performs a policy-making function, or any other person who performs similar policymaking functions for the issuer. Executive officers of the issuer's parent(s) or subsidiaries are deemed executive officers of the issuer if they perform such policy making functions for the issuer. In addition, when the issuer is a limited partnership, officers or employees of the general partner(s) who perform policy-making functions for the limited partnership are deemed officers of the limited partnership. When the issuer is a trust, officers, or employees of the trustee(s) who perform policy-making functions for the trust are deemed officers of the trust. Policy-making function is not intended to include policymaking functions that are not significant. Identification of an executive officer for purposes of Section 303A.14 would include at a minimum executive officers identified pursuant to Item 401(b) of Regulation S-K.
  - 6 *Financial reporting measures.* Financial reporting measures are 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. Stock price and total shareholder return are also financial reporting measures. A financial reporting measure need not be presented within the financial statements or included in a filing with the Commission.

- 7 *Incentive-based compensation.* Incentive-based compensation is any compensation that is granted, earned, or vested based wholly or in part upon the attainment of a financial reporting measure.
- 8 *Received.* Incentive-based compensation is deemed received in the issuer's 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.
- 9 It has not yet been published in the Federal Register.

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