



**ICGN**

International Corporate Governance Network  
*Inspiring good governance & stewardship*

Vanessa A. Countryman, Secretary  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1090

Submitted via SEC email: [rule-comments@sec.gov](mailto:rule-comments@sec.gov)

22nd November 2021

Re: Release No. 33-10998-Reopening of Comment Period for Listing Standards for Recovery of Erroneously Awarded Compensation, File Number S7-12-15

## **Securities and Exchange Commission Request for Comment**

### **ICGN submission**

The International Corporate Governance Network (“ICGN”) is pleased to respond to the Securities and Exchange Commission (“SEC”) upon its reopening of the comment period for listing standards for the recovery of erroneously awarded compensation.

Led by investors responsible for assets under management in excess of US\$59 trillion, ICGN is a leading authority on global standards of corporate governance and investor stewardship. Our membership is based in more than 40 countries and includes companies, advisors and other stakeholders. ICGN’s mission is to promote high standards of professionalism in governance for investors and companies alike in their mutual pursuit of long-term value creation contributing to sustainable economies world-wide. ICGN offers an important investor perspective on corporate governance to help inform public policy development and to encourage good practices by capital market participants.

The United States (US) is an important market for ICGN, as many of our members are based in the US, with an even larger group of ICGN members invested in US companies. ICGN engages regularly with global regulatory bodies, including the SEC, where we have commented frequently.<sup>1</sup>

The ICGN has issued guidance on matters that relate to this request for comments, including the:

- ICGN Global Governance Principles;<sup>2</sup>
- ICGN Global Stewardship Principles;<sup>3</sup>
- ICGN Guidance on Executive Director Remuneration,<sup>4</sup> and

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<sup>1</sup> [ICGN Universal Proxy Letter to US SEC.pdf](#)

<sup>2</sup> <https://www.icgn.org/policy/global-governance-principles>

<sup>3</sup> <https://www.icgn.org/policy/global-stewardship-principles>

<sup>4</sup> [ICGN Guidance on Executive Remuneration \(2016\)](#)

- ICGN Viewpoint on Integrating ESG into Executive Compensation Plans.<sup>5</sup>

Our main policy positions are guided by the ICGN Global Governance Principles (GGP) and the ICGN Global Stewardship Principles (GSP), both of which have been developed in consultation with, and ratified by, ICGN members and as part of a wider peer review. We believe our GGP have relevance for the governance of companies, including for boards of directors who have the responsibility to set remuneration that is “reasonable and equitable”.<sup>6</sup>

Equitable remuneration for CEOs and executive officers is a continual priority for ICGN and its members, necessitating that ICGN establish specific policies and guidance for issuers and investors. It is a topic that is frequently raised by investors during proxy season and engagement meetings, given the nature of high levels of executive remuneration compared to worker pay. The need for issuers to transparently communicate the terms and effectively administer remuneration policies that align with long-term strategy and value creation for investors, is paramount to good governance. If compensation practices are aligned as such, investors could potentially have fewer concerns with executives adopting strategies that heighten risk for investors or fail to fully disclose an issuer’s financial situation. Including an effective claw back of unwarranted or ill-gotten gains as part of the compensation process enhances alignment and improves transparency.

### Reopening of the comment period

We appreciate the decision by the SEC to reopen the comment period for its proposal to implement the provisions of Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”). As disclosed in the notice, the proposed rule would “direct the national securities exchanges and national securities associations to establish listing standards that would require each issuer to develop and implement a policy providing for the recovery, under certain circumstances, of incentive-based compensation based on financial information required to be reported under the securities laws that is received by current or former executive officers, and require disclosure of the policy (the “Proposed Rules”)”.<sup>7</sup>

ICGN recognises that since the enactment of Section 954 of the Dodd-Frank Act in 2010, and the publication of the SEC’s proposed rules in 2015, there have been important developments relating to the adoption and application of clawback policies. For investors, the recoupment of ill-gotten or unwarranted gains from executives due to fraud, restatements, or misstatements of material fact, is essential. Clawback policies can be an effective deterrent, however, the application of such, “*under certain circumstances,*” as the Section 954 provides, must be clear.

While there may have been more issuers disclosing information on clawback policies since 2015, the efforts to recoup previously issued performance-based awards, are mixed at best. It can be difficult for investors to gain access to that information, particularly if clawback provisions in employment contracts are subject to non-disclosure agreements. The legal requirements for

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<sup>5</sup> [ICGN Viewpoint on Integrating ESG in Executive Compensation \(2020\)](#)

<sup>6</sup> [ICGN Global Governance Principles 2021](#), p. 20.

<sup>7</sup> <https://www.sec.gov/rules/proposed/2021/33-10998>

that which constitutes an effective trigger of clawback provisions may be subject to interpretation and require the courts to intervene. In a March 2021, Harvard Business Review report, Professors Charles Elson and Sanjai Bhagat, explained why most executive compensation clawback provisions don't work:

There are two simple reasons for this. First, the legal requirement for recovering monies already paid to an executive typically involve the notion of “cause” — unless convicted of a crime, an executive will argue the company has no legal right to reclaim the cash. Second, and just as important, once the money is out the door, the burden is on the party without the cash to get it back. And, in many circumstances, the money may be spent and basically unrecoverable.<sup>8</sup>

The question to be addressed, therefore, in the proposed rule is how the words, “under certain circumstances,” will be defined. In the Global Governance Principles, Principle 5, Remuneration, ICGN provided at least two scenarios when clawback provisions should be utilised:

Principle 5.4 Malus and clawback. Companies should include provisions in their incentive plans that enable the company to withhold the payment of any sum (‘malus’), or recover sums paid (‘clawback’), in the event of serious misconduct or a material misstatement in the company’s financial statements.<sup>9</sup>

In addition to defining the circumstances when companies should seek the return of performance-based awards, ICGN suggests that the SEC include metrics in the form of material Environmental, Social and Governance (ESG) factors in the determination. In an ICGN Viewpoint, entitled, “Integrating ESG into Executive Compensation Plans”, from November 2020, we said:

ESG metrics, whose ‘non-financial’ label sometime creates confusion because their impacts may not appear in financial results in the short-term, have the potential to impact the bottom line of the business in the mid or longer term. This can be through reputational damage, other risk-laden decision-making, or the actual interruption of business continuity. The focus should be on materially relevant ESG issues, including an explanation of how these have been defined and whether the company has been tracking its performance on these factors for a few years before tying their compensation to it. It is important to incorporate sustainability-related performance factors that the executive team can be held accountable for and directly influence. This requires looking beyond the current crisis and proactively considering such factors as climate risk and inclusion policies.

In principle, competent executives generally do what they are paid to accomplish. The inclusion of ESG metrics in their long-term incentives is intended to influence their behavior to ensure that material ESG issues are addressed. This may include tying

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<sup>8</sup> Harvard Business Review, [Why Executive Compensation Clawbacks Don't Work \(hbr.org\)](https://hbr.org), March 22, 2021 by Sanjai Bhagat and Charles M. Elson.

<sup>9</sup> [ICGN Global Governance Principles 2021](#), p.21

annual bonuses to ESG-related metrics, such as customer satisfaction or occupational health and safety (OH&S) performance.

In the context of the growing focus on long-term value creation, it is not surprising that a growing number of shareholder proposals focus on linking executive compensation to sustainability metrics.<sup>10</sup>

In summary, ICGN recommends that the SEC consider the following as it reviews the comments received:

- The need to define the appropriate disclosure language in an issuer’s clawback policy to include *when* the company has exercised a clawback(s), *when* serious misconduct and/or a material misstatement is alleged or has occurred, *whether* the policy has been triggered and, if so, the circumstances under which the issuer recouped any erroneously awarded compensation.
- That restatements, as well as restatements to correct errors that are material to the previously issued financial statements, would be considered “an accounting restatement due to material non-compliance”, and therefore would result in a clawback recovery analysis.
- If the clawback was not exercised even with serious misconduct or misstatements, disclosure should be required what the intervening factors were and whether the issuer will amend its policy to capture clawbacks in the future.
- Disclosure whether employment agreements, in the US or other countries, that provide for the non-disclosure of clawbacks, have been entered into prior to the rule proposal for exchanges to require disclosure and if so, what information the issuer will disclose.
- It would be useful for the rules to provide additional discretion for compensation committees of the issuer’s board of directors to determine whether to pursue recovery of incentive-based compensation and how much to recover, to be consistent with Section 954.
- We recognise that it may be more appropriate to rely on existing guidance, literature, and definitions concerning accounting errors rather than have the SEC define “accounting restatement” and “material non-compliance.” ICGN believes the revised clawback trigger would be useful, which would specifically refer to “all required restatements to previously issued financial statements, including those restatements that were not material to those previously issued financial statements, but would result in a material misstatement if (a) the errors were left uncorrected in the current report or (b) the error correction was recognized in the current period.”
- It would be useful for the trigger for the three-year lookback period to include a definition that incorporates the proposed triggering events rather than leaving the determination solely to the discretion of the issuer, to better realise the objectives of Section 10D.
- It would be useful to retain the “reasonably should have concluded” standard, regardless of whether the SEC revises the proposed trigger to accommodate the additional

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<sup>10</sup> [Integrating ESG into Executive Compensation Plans | ICGN](#), November 2020.

accounting restatements. Investors should be given more latitude to pursue clawback remedies, especially if board action is not taken.

- It would be important to provide greater transparency around restatements, albeit by adding “check boxes to the cover page of the Form 10-K that indicate separately (a) whether the previously issued financial statements included in the filing include an error correction, and (b) whether any such corrections are restatements that triggered a clawback analysis during the fiscal year.” We also could see that such disclosure could occur in the Form 8-K filing, as another useful tool for investors.
- The proposed definition of the recoverable amount, as described, should be useful, which is “the amount of incentive-based compensation received by the executive officer or former executive officer that exceeds the amount of incentive-based compensation that otherwise would have been received had it been determined based on the accounting restatement.”
- We believe that investors would benefit from “disclosure of how issuers calculated the recoverable amount, including their analysis of the amount of the executive’s compensation that is recoverable under the rule, and/or the amount that is not subject to recovery.” With respect to incentive-based compensation that was based on stock price or total shareholder return, “disclosure regarding the determination and methodology that an issuer used to estimate the effect of stock price or total shareholder return” would provide investors with an understanding how the issuer determined what remuneration would be subject to return or not subject to recovery.
- Adopting a methodology, such as Inline XBRL detail, to provide investors with greater flexibility to review some or all of the compensation recovery disclosures would be valuable to investors. ICGN would have no comment on the type of methodology utilised by tagging entities.
- The need to tie ESG-related metrics to the awarding of executive compensation plans, to link executive compensation to sustainability metrics, using recognized standard(s). In this way, issuers may be able to curtail risk-taking actions by executives that could trigger serious misconduct, lead to misstatements of financial information and/or actions that cause reputational damage and harm shareholder value.

In conclusion, ICGN appreciates the reopening of the comment period, and we hope that our feedback and comments are helpful in your deliberations. Should you wish to discuss our comments further, please contact me or George Dallas, ICGN’s Policy Director, by email at [george.dallas@icgn.org](mailto:george.dallas@icgn.org).

Yours faithfully,



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## Appendix

To support ICGN's comments on the recovery of erroneously awarded compensation, it is relevant to discuss the most important components of ICGN's executive compensation policies.

ICGN has developed policy on this subject in its Global Governance Principles, Principle 5, which states:

Remuneration should be designed to equitably and effectively align the interests of the CEO, executive officers, and workforce with a company's strategy and purpose to help ensure long-term sustainable value preservation and creation. Aggregate remuneration should be appropriately balanced with the payment of dividends to shareholders and retention of capital for future investment and the level of quantum should be defensible relative to social considerations relating to income inequality.

From the investor stewardship side, ICGN has provided additional guidance to ensure that investors are able to evaluate issuer policies, including "Say on Pay," the approval of incentive compensation plans that adopt clawback policies, including disclosure whether it has and when it recouped compensation from any employees. In the ICGN Global Stewardship Principles, Principle 3, Monitoring and assessing investee companies, it says:

3.3 Comprehensive factors. Investors should be clear about what standards they are applying and how they monitor investee companies. Monitoring companies encompasses a wide range of factors including: a) the company's business model, strategy, and ongoing performance, as well as developments within and external to the company that might affect its value and the risks it faces; b) the company's approach to environmental and social matters that may influence a company's sustainable long-term success, for example, as described in the UN Sustainable Development Goals. c) the effectiveness of the company's governance and leadership; and d) the quality of the company's reporting.<sup>11</sup>

ICGN has provided guidance in its ICGN Guidance on Executive Director Remuneration, to address the use of employment contracts to limit the disclosure of contractual terms for executives that may include clawback provisions. In Part 3, Contractual Provisions, ICGN states:

3.1 Employment contracts, severance, change in control. Disclosure points.

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<sup>11</sup> [ICGN Global Stewardship Principles 2020](#), p. 17.

Disclosure of the existence of all employment agreements, severance arrangements, change in control agreements and any other contractual agreements with key executives. Disclosure should include a description of the agreements, which contain sufficient detail of all material factors such that shareholders have a complete understanding of their terms. Companies should provide estimated payments under specific scenarios such that shareholders can determine the potential pay-outs under each agreement.<sup>12</sup>

In addition, the Guidance on Executive Director Remuneration, Part 2, Remuneration Structure, states:

How the committee mitigates or eliminates the potential for unintended consequences. This should include a discussion of how incentive plans are structured and monitored to mitigate unintended drivers. The policy should also discuss the company's provisions for recapturing unearned incentive remuneration (claw back or disgorgement policies, for example). As a related topic, the policy should discuss how the company will minimize the potential for manipulation of performance related metrics, and monitor performance for potential fraud (internal risk controls, for example).<sup>13</sup>

Our final guidance is derived from the ICGN Viewpoint on Integrating ESG into Executive Compensation Plans. In the Viewpoint, ICGN specified:

The focus should be on materially relevant ESG issues, including an explanation of how these have been defined and whether the company has been tracking its performance on these factors for a few years before tying their compensation to it. It is important to incorporate sustainability-related performance factors that the executive team can be held accountable for and directly influence. This requires looking beyond the current crisis and proactively considering such factors as climate risk and inclusion policies.

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<sup>12</sup> [ICGN Guidance on Executive Remuneration \(2016\)](#), p. 20.

<sup>13</sup> [ICGN Guidance on Executive Remuneration \(2016\)](#), p. 13.