

## Alert | Corporate



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# NYSE, Nasdaq Propose Listing Standards Implementing SEC Clawback Rules

## Background

On Oct. 26, 2022, the Securities and Exchange Commission (SEC) adopted [Rule 10D-1](#) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), pursuant to Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Rule 10D-1 directs the national securities exchanges to establish listing standards that require issuers to adopt and comply with a policy for the recovery of erroneously awarded incentive-based compensation from current and former executive officers (the “Recovery Policy”) and provide relevant disclosure requirements for annual reports and other SEC filings. Listed issuer disclosure requirements the SEC directs include a description of the policy, filing the policy as an exhibit to annual reports, and additional disclosures in the event a recovery analysis is triggered under the policy.

On Feb. 22, 2023, the New York Stock Exchange (NYSE) submitted [Proposed Section 303A.14](#), and the Nasdaq Stock Market (Nasdaq) submitted [Proposed Listing Rule 5608](#) (together, the “Proposed Listing Standards”) to the SEC to implement the policies and provisions under Rule 10D-1. Once published in the Federal Register, a 21-day comment period for the Proposed Listing Standards begins. The Proposed Listing Standards will become effective upon the SEC’s approval and no later than Nov. 28, 2023. Issuers subject to the Proposed Listing Standards must adopt a Recovery Policy within 60 days of the effective date of the Proposed Listing Standards (the “Effective Date”).

## **NYSE and Nasdaq Proposed Rules – Compliance**

As was widely expected, the Proposed Listing Standards mirror the standards outlined in Rule 10D-1. Under the Proposed Listing Standards, the issuer must “adopt and comply with a written Recovery Policy providing that the issuer will recover reasonably promptly 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.” Once implemented, the Proposed Listing Standards are required to include a provision requiring any accounting restatement to “correct an error in previously issued financial statements that is material to the previously 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.”

Additionally, the Proposed Listing standards must apply to all incentive-based compensation received by a person:

- after beginning service as an executive officer;
- who served as an executive officer at any time during the performance period for that incentive-based compensation;
- while the issuer has a class of securities listed on a national securities exchange or a national securities association; and
- during the three completed fiscal years immediately preceding the date when the issuer is required to prepare an accounting restatement.

The Proposed Listing Standards define incentive-based compensation as “any compensation that is granted, earned, or vested based wholly or in part upon the attainment of a financial reporting measure.” Under the Proposed Listing Standards, incentive-based compensation would be 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.”

## **NYSE Proposed Rule - Delisting**

NYSE’s Proposed Section 802.01F outlines delisting procedures for noncompliant issuers. Under Proposed Section 802.01F, “in any case where the Exchange determines that a listed issuer has not recovered erroneously-awarded compensation as required by its Recovery Policy reasonably promptly after such obligation is incurred, trading in all listed securities of such listed issuer would be immediately suspended and the Exchange would immediately commence delisting procedures with respect to all such listed securities.”

Proposed Section 802.01F(b) would deem a listed issuer to be below standards in the event of any failure by such listed issuer to adopt its required Recovery Policy by the Effective Date (a “Late Recovery Policy Adoption Delinquency”). The listed issuer would be required to notify the NYSE in writing within five days of the Effective Date if it failed to adopt its Recovery Policy by that date. Upon the occurrence of a Late Recovery Policy Adoption Delinquency, the NYSE would promptly send written notification (the “Late Recovery Policy Adoption Delinquency Notification”) to a listed issuer of the procedures set forth below. Within five days of the date of the Late Recovery Policy Adoption Delinquency Notification, the listed issuer would be required to:

- contact the NYSE to discuss the status of the delayed Recovery Policy; and
- issue a press release disclosing the occurrence of the Late Recovery Policy Adoption Delinquency, the reason for the Late Recovery Policy Adoption Delinquency and, if known, the anticipated date such Late Recovery Policy Adoption Delinquency will be cured.

### **Nasdaq Proposed Rule – Delisting**

Nasdaq’s proposed amendment to Listing Rule 5810(c)(2)(A)(iii) would clarify that a company that failed to comply with proposed Listing Rule 5608 would be required to submit to Nasdaq Staff a plan to regain compliance. The administrative process for such deficiencies would then follow the previously established pattern used for similar corporate governance deficiencies. This would allow the Nasdaq Staff to provide the issuer up to 180 days to cure the deficiency.

In determining whether the issuer was taking appropriate steps to fulfill its obligation to recover erroneously awarded incentive-based compensation reasonably promptly, Nasdaq would assess each scenario holistically and would weigh a variety of factors when considering such accounting restatement prepared by the issuer. The factors Nasdaq would consider include:

- whether the issuer was pursuing an appropriate balance of cost and speed in determining the appropriate means to seek recovery; and
- whether the issuer was securing recovery through means that were appropriate based on the particular facts and circumstances of each executive officer that owed a recoverable amount.

### **General Exemptions**

The requirements of both NYSE Proposed Rule 303A.14 and Nasdaq Proposed Listing Rule 5608 would not apply to the following:

- any security issued by a unit investment trust; and
- any security issued by a management company 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.

The requirements of the NYSE proposed rules would not apply to the following:

- a security futures product cleared by a registered clearing agency or that is exempt from the registration requirements of the Exchange Act; and
- a standardized option issued by a clearing agency that is registered pursuant to the Exchange Act.

### **Recent C&DIs From SEC Staff**

On Jan. 27, 2023, the SEC Staff (the “Staff”) released its first set of Compliance and Disclosure Interpretations (C&DI) regarding Rule 10D-1 reflecting the views of the staff of the Division of Corporation Finance of the SEC:

- C&DI 121H.01 clarifies that although Forms 10-K, 20-F, and 40-F now have been amended to include check boxes on the cover page to correct previously issued financial statements and a corresponding

recovery policy discussion, the Staff does not intend for such disclosure to be provided until an issuer is required to have a recovery policy under the applicable listing standard.

- C&DI 121H.02 explains which individuals will be considered named executive officers for the purpose of individualized disclosure as required in Form 20-F filed by foreign private issuers specifying members of the issuer's administrative, supervisory, or management bodies for whom the issuer otherwise provides individualized compensation disclosure in the filing.
- C&DI 121H.03 discusses which individuals will be considered named executive officers for the purpose of individualized disclosure as required in Form 40-F filed by foreign private issuers specifying executive officers for whom the issuer otherwise provides individualized compensation disclosure in the filing.
- C&DI 121H.04 emphasizes that Rule 10D-1 is meant to apply broadly, and that for plans which take into account incentive-based compensation, an issuer would be expected to claw back the amount contributed to the notional account based on erroneously awarded incentive-based compensation and any earnings accrued to date on that notional amount.

### **Key Takeaways for Issuers**

In light of the SEC's adoption of its Recovery Policy and direction to the exchanges under Rule 10D-1 and NYSE and Nasdaq's filing of Proposed Listing Standards, issuers should consider with experienced securities counsel the following action items:

- Monitor for the SEC's approval of the Proposed Listing Standards in order to determine and track the last date by which the issuer must adopt its Recovery Policy.
- Evaluate current board and committee charters and policies and meet with the board of directors, compensation committee and audit committee to discuss Proposed Listing Standards and strategize how to implement the necessary standards into existing corporate governance structure.
- Review existing recovery policies, both individualized and standalone, and determine whether to meet the new requirements by updating existing policies or to establish a singular standalone policy for ease of use and filing with the SEC.
- Take note of already existing incentive-based compensation plans and discuss how the Proposed Listing Standards might apply to these plans.
- Establish internal procedures and corporate governance processes such that when a financial restatement is required, actions and disclosures required pursuant to the Recovery Policy can be promptly coordinated and executed.

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