March 4, 2022

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549
RIN 3235-AK99
File Number S7-07-15

**Re: Reopening of Comment Period for Pay Versus Performance**

Dear Madam:

McGuireWoods LLP ("MW") and Brownstein Hyatt Farber Schreck, LLP ("Brownstein") hereby submit this letter in response to the request for public comments by the Securities and Exchange Commission (the "SEC") to the Reopening of Comment Period for the Notice of Proposed Rulemaking that amends the current executive compensation disclosure rule to require a description of how executive compensation actually paid by a registrant related to the financial performance of that company (the "Proposed Rules") pursuant to Section 953(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), which was published in the Federal Register on May 7, 2015.[1]

Section 953(a) of the Dodd Frank Act added Section 14(i) to the Securities Exchange Act of 1934 (the "Exchange Act"), which requires the SEC to adopt rules requiring issuers to disclose in any proxy or consent solicitation materials for an annual meeting of the shareholders a clear description of any compensation required to be disclosed under Item 402 of Regulation S-K.[2] This includes providing information that shows the relationship between executive compensation actually paid and the financial performance of the issuer, taking into account any change in the value of the shares of stock, dividends of the issuer, and any distributions.[3]

## I. The final rules ("Final Rules") should provide registrants with maximum flexibility so that the pay versus performance disclosures actually provide helpful information to shareholders in assessing a registrant's performance and executive compensation.

Shareholders are keenly interested when an executive's compensation is increasing sharply despite a company's financial performance falling.[4] Thus, maximizing transparency of how executive

[1] Pay Versus Performance, 80 Fed. Reg. 26329 (May 7, 2015).
[2] Section 953(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, P.L. 111-203, 124 Stat 1376 (2010).
[3] *Id*.
[4] Report of the Senate Committee on Banking, Housing and Urban Affairs to accompany S. 3217, S. Rep. No. 111-176, at 135 (2010).

compensation is set enables shareholders to better evaluate a company's performance. To maximize transparency, it is critical to provides registrants with flexibility to determine the most appropriate and helpful information that will best inform shareholders as well as potential investors. The Senate Committee on Banking, Housing and Urban Affairs Committee Report indicates that the rules mandated by Section 953(a) of the Dodd-Frank Act were not intended to be overly-prescriptive and that Congress recognized that there could be many ways to disclose the relationship between executive compensation and financial performance of the registrant." This statement was acknowledged by the SEC in the introduction to the Proposed Rules. [5] The SEC also notes that the pay-versus-performance disclosure mandated by Section 953(a) of the Dodd-Frank Act is intended to provide shareholders with information that will help them assess a registrant's executive compensation.[6] Thus, it is clear that the intent of section 953(a) is to provide shareholders with flexibility to provide the most helpful, transparent information to shareholders and potential investors so that they can make an informed decision.

As such, we recommend and request that the Final Rules provide registrants with flexibility by implementing the following (each discussed in more detail below):

- The Final Rules should eliminate the requirement to disclose cumulative total shareholder return ("TSR") and allow registrants to determine and disclose their most appropriate measures of performance;
- The Final Rules should eliminate duplicative disclosures and allow registrants to determine the format and location of the pay-versus-performance disclosures; and
- The Final Rules should eliminate any requirement for XBRL tagging.

**A. *The Final Rules should eliminate the requirement to disclose TSR and allow registrants to determine and disclose the most appropriate measure(s) of performance used by such registrant to link compensation actually paid during the fiscal year to its performance.***

Section 953(a) of the Dodd-Frank Act requires the SEC promulgate regulations requiring disclosure in each issuer's proxy statement of the financial performance of the issuer, taking into account any change in the value of the shares of stock and dividends of the issuer and any distributions.[7] Nothing in the statute requires the use of TSR.[8] We believe that such reliance and emphasis on TSR is misguided and could be misleading to shareholders. While use of TSR may be appropriate in certain instances, we believe that each registrant should make the determination as to whether the use of TSR is the most appropriate measure to test the link between compensation actually paid during the fiscal year and company performance. Thus, we respectfully request that disclosure of TSR not be mandated in the pay-versus-performance disclosures.

1. The focus on TSR is misguided.

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[5] 80 Fed. Reg. at 26330, citing Report of the Senate Committee on Banking, Housing and Urban Affairs to accompany S. 3217, S. Rep. No. 111-176, at 135 (2010).
[6] 80 Fed. Reg. at 26331.
[7] Dodd-Frank Act Section 953(a).
[8] *See generally Id*.

There are several issues with requiring disclosure of TSR and using it as a mandated measure of financial performance, starting with the fact that, as the SEC notes, financial performance is a broad term that can mean different things to different registrants[9] – so why should all registrants be required to report financial performance uniformly? With thousands of companies of various sizes, industries, business models, and growth stages, identifying one performance measure that can be consistently and usefully applied to all registrants is impossible.

Another potential problem with using TSR as the measure of financial performance, is that it can overemphasize stock prices that don't correlate to company performance, such as what happened this past year with GameStop, AMC, and other "meme stocks." GameStop was the first target and one of the more prominent examples of the recent cultural trend of younger investors putting their money in "meme stocks." Meme stocks[10] are typically created when the shares of an underperforming company amass a large following on social media sites like Reddit and Twitter. These followers, such as subscribers to the subreddit r/WallStreetBets, observe hedge funds and other conventional traders making outsized bets against a particular company or sector (e.g., retail video games, in GameStop's case) and collectively invest their money in that company, causing massive fluctuations in stock price.

**Example**[11]

On December 31, 2020, GameStop's stock closed at $18.84.[12] Through 2021 and as of the third quarter of 2021,[13] GameStop's underlying financial performance declined, and the company's net loss increased (such that the overall loss from a year earlier of $0.29 per share increased to a loss of $1.39 per share).[14] However, despite poor actual performance as reflected in the underlying financial metrics in GameStop's balance sheet and income statement, GameStop's stock closed at $148.39 on December 31, 2021.[15]

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[9] *Id.*

[10] *7 New Meme Stocks That Retail Investors Can't Get Enough Of*, Business Insider (Nov. 12, 2021), https://markets.businessinsider.com/news/stocks/7-newest-meme-stocks-retail-investors-cant-get-enough-of-1030970937 (last visited Feb. 23, 2022).

[11] *'Dumb Money' Is on GameStop and It's Beating Wall Street at Its Own Game*, The New York Times (Jan. 27, 2021) https://www.nytimes.com/2021/01/27/business/gamestop-wall-street-bets.html (last visited Feb. 23, 2022); *see also* The Reddit revolt: GameStop and the impact of social media on institutional investors, The TRADE (Apr. 13, 2021) https://www.thetradenews.com/the-reddit-revolt-gamestop-and-the-impact-of-social-media-on-institutional-investors/ (last visited Feb. 23, 2022).

[12] *GameStop Corp. (GME) Historical Data*, Yahoo Finance (Feb. 23, 2022) https://finance.yahoo.com/quote/GME/history?period1=1603756800&period2=1611705600&interval=1d&filter=history&frequency=1d&includeAdjustedClose=true (last visited Feb. 23, 2022).

[13] We note that as of the date of this comment letter GameStop's 2021 fourth quarter financial information was not publicly available.

[14] *GameStop shares fall as video game retailer reports widening losses in third quarter*, CNBC (Dec. 8, 2021), https://www.cnbc.com/2021/12/08/gamestop-gme-3q-2021-earnings.html (last visited Feb. 23, 2022).

[15] *GameStop Corp. (GME) Historical Data*, Yahoo Finance (Feb. 23, 2022) https://finance.yahoo.com/quote/GME/history/ (last visited Feb. 23, 2022).

The problem here, of course, is that the run-up in GameStop's share price had nothing to do with its revenue, profits, or other performance factors on which public-company executives are typically and appropriately evaluated. GameStop is not currently profitable, nor does it project to be in the next three years.[16] In the past three years, it has seen its revenue decline by 17% per year.[17] Yet, over the same three-year period, the company experienced strong share price growth of 108% per year, compounded, and a TSR of over 832%.[18] We believe that this clear lack of correlation between financial fundamentals and share price underscores why TSR should not be mandated and endorsed by the SEC as *the* primary measure of financial performance for shareholders to rely on.

While the GameStop example highlights the flaw that TSR can overemphasize stock prices that don't correlate to company performance, it is far from the only problem with requiring the disclosure of TSR. TSR can also create perverse incentives when used as a primary metric of executive performance. For well-established companies, high expectations for future performance are often already priced into their valuation. As a result, management of these companies may perform quite well by simply meeting these high expectations. However, simply meeting high expectations will not increase TSR. In order to do so, executives of these companies must exceed already high expectations – a goal that in some instances may only be achieved by taking on more risk. In addition, an excessive focus on TSR may encourage companies and executives to take actions that pay off in the short-term to the detriment of creating long-term value. TSR is susceptible to manipulation, so there exists the very real possibility that companies will manipulate TSR by adopting strategies for boosting stock prices in the short-term (e.g., increasing debt, cutting research and development, engaging in stock buy-backs) that may be detrimental to positive long-term financial performance. This creates an inherent risk to investors.

Moreover, the focus on TSR could cause companies to substitute TSR for existing metrics in their compensation plans to ensure a "good" disclosure, resulting in the uniformization of executive pay programs that may not be in the best interests of shareholders. The SEC implicitly acknowledged this issue in its request for comment in the Proposed Rules.[19] Executive pay programs should not be universally uniform and instead should be designed around a company's particular business and support its business strategy, using whichever measures the organization's board of directors and compensation committee determine to be most appropriate. In view of the foregoing, we request that the Final Rules gives registrant's the ability to use the financial metric(s) most relevant to its business strategy and compensation plans.

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[16] *GameStop Stock Report*, Simply Wall St (Feb. 22, 2022) https://simplywall.st/stocks/us/retail/nyse-gme/gamestop?blueprint=1885535&utm_medium=finance_user&utm_campaign=integrated-pitch&utm_source=yahoo#executive-summary (last visited Feb. 23, 2022).

[17] *The 4.5% return this week takes GameStop's shareholders three-year gains to 832%*, Yahoo Finance (Feb. 7, 2022) https://www.yahoo.com/video/4-5-return-week-takes-112846042.html?guce_referrer=aHR0cHM6Ly93d3cuZ29vZ2xlLmNvbS8&guce_referrer_sig=AQAAAF6vidKaojessWYHgTUPmSSc6Aay53VfRnZutGG_5y-mSZ9GTBqEEO88aZJkEjV1XkxWeEV0S27htL5CS3ZmNUUptz3PdCgGn0xNNT3qL7DutOl3Eikx_008NnPYLRO2SikzBBdjcYjWowUddRDtKbAVpcigk9_yUGrTBWYNx8fW&guccounter=2#:~:text=It's%20nice%20to%20see%20that,has%20improved%20in%20recent%20times (last visited Feb. 23, 2022).

[18] *Id*.

[19] 80 Fed. Reg. at 26341 (request for comment 36).

Since TSR will not fairly present the link between performance and compensation for all registrants, we recommend that the SEC allow companies to choose the most appropriate measures of performance to disclose. Whether it be revenue growth, adjusted EBITDA margin, net income, or some other metric, each registrant is in the best position to determine how to define its own performance. Forcing companies to layer TSR into their disclosures would inappropriately influence executive compensation decisions leading to bad operational outcomes, can be misleading, and is not in investors' long-term interest.

2. Requiring additional prescriptive measures unnecessarily adds disclosures that may not be important to companies and shareholders.

In the Reopening of Comment Period for the Notice of Proposed Rulemaking, the SEC provided that it is considering requiring registrants to disclose, in addition to the disclosures in the Proposed Rules, pre-tax net income, net income, and a company-selected measure.[20] These additional tabular disclosures suffer from similar flaw as a mandated TSR disclosure and would increase redundancy with little to no benefit to investors. Thus, we request that they not be required.

3. Requiring additional prescriptive measures unnecessarily adds disclosures that may not be important to companies and shareholders.

We are concerned that the SEC is also considering whether to separately require registrants to provide a list of the five most important performance measures used by each registrant to link compensation actually paid during the fiscal year to company performance, over the time horizon of the disclosure, in order of importance.[21] We request that the SEC not require any such additional prescriptive measures and allow companies to disclose the information most pertinent to their facts and circumstances, as the SEC's proposed additions require disclosures that may not be relevant to registrants or shareholders, and would create tremendous burdens for the registrant.

For instance, much of the information the SEC is considering adding is already required and addressed by the Compensation Discussion and Analysis ("CD&A"). For example, the CD&A requires a discussion of the application of the performance metrics applied to short-term incentive plans ("STI") and long-term incentive plans ("LTI") along with other factors compensation committees evaluate in determining executive compensation. How should a company determine its most important measure when it views the various performance metrics wholistically? What if the list changes year to year or executive to executive? Not only is it duplicative, but a top five disclosure requirement also presents challenges to issuers who may base compensation decisions on fewer than or more than five performance metrics. Moreover, it does not account for the fact that many companies give multiple performance metrics equal weight, as would have already been described in the CD&A. Therefore, this proposal would only further mislead and confuse investors as it would require the disclosure of a prescriptive ranking that, in reality, may not align precisely with the CD&A, where how compensation is set and evaluated is already described in detail.

If the SEC decides to require an additional discussion of ranked performance metrics, we recommend allowing registrants to fulfill disclosure obligations via a simple cross reference to the

[20] Reopening of Comment Period for Pay Versus Performance, 87 Fed. Reg. 5751, 5753 (Feb. 2, 2022).
[21] *Id*. at 5754.

CD&A disclosures (avoiding prescriptive requirements to list a specific number of important performance metrics), to enable compensation committees to tailor compensation programs to core drivers of a registrant's business and adequately describe this process for investors. We believe that such a simple cross reference will enhance transparency for shareholders.

4. The Final Rules should eliminate peer group TSR disclosures.

Similar to the use of TSR disclosure, Section 953(a) of the Dodd-Frank Act does not require the use of peer groups or relative TSR peer group comparisons nor indicate such disclosure shows the relationship between company pay-versus-performance. While we acknowledge the SEC's desire to enhance comparability across registrants, it is inappropriate to overstep the SEC's statutory directive, and as such, we request that the Final Rules remove peer group TSR as a required disclosure.

Notwithstanding the issues noted above with using TSR as a metric of performance, we are also concerned with the use of peer group TSR comparisons because the disclosures will not inform an investor's understanding of the company's compensation programs and compensation paid to its executive officers. Peer group TSR is not necessary or helpful to include because performance of a peer group may not be relevant in registrants' compensation decisions. Furthermore, any helpful information related to peer group performance is already disclosed in the performance graph required by Item 201(e) of Regulation S-K.

**B. *The Final Rules should eliminate duplicative disclosures and allow registrants to determine the format and location of the pay-versus-performance disclosures.***

Proxy statements are already lengthy and provide a lot of compensation related information to investors in a variety of formats (e.g., narrative and tabular). Rather than add redundant information for investors to wade through, we recommend the Final Rules eliminate duplicative disclosures.

1. Eliminate the tabular disclosure requirement, permit a graphic representation, and provide safe-harbor examples.

Companies should be permitted the flexibility to choose the manner of presentation of the pay-versus-performance disclosure that best fits their facts and circumstances, including allowing companies to replace the tabular disclosure with a graphic representation showing registrant performance compared to compensation actually paid. The information contemplated by the tabular disclosure is easily described and more easily understandable via a graphical representation showing the correlation (or lack thereof) between a company's pay and its performance.

We request that the Final Rules include a safe-harbor template of a model graphic disclosure that addresses the items the SEC expects to see yet still provides maximum flexibility for registrants to determine appropriate performance measures and presentation.

2. The Final Rules should eliminate the SCT total compensation from the tabular disclosures.

In the event the Final Rules retain the tabular disclosures, we recommend removing the column showing total compensation from the Summary Compensation Table ("SCT"). We see no need for this repetitive disclosure of information that is already prominently presented elsewhere in the proxy statement. We also believe repeating total SCT compensation in the pay-versus-performance table would be contrary to the statutory focus on compensation "actually paid," since total compensation includes amounts such as grant date value of equity and performance awards and change in pension value that may not actually be paid to an executive, if at all, until sometime in the future.

While the tabular disclosure is presumably intended to facilitate an investor's understanding of the link between executive pay and a registrant's performance, the format and scope of the proposed disclosure undermines this objective. The table would more likely serve to confuse investors rather than help them understand the relationship between executive pay and company performance. Further undermining the clarity of the proposed table is the requirement for a registrant to include unnecessary data and information (e.g., SCT total compensation). The SEC appears to acknowledge these shortcomings by allowing a registrant to go through the table and add explanatory disclosures thought necessary by a registrant. However, these disclosures would needlessly add to the complexity and length of a registrant's pay versus performance disclosure.

3. The Final Rules should not require inclusion of the stock performance graph.

The Final Rules should not require inclusion of the stock performance graph because it is duplicative of other disclosures, is not an accurate measurement of company performance, and was never intended to compare pay and performance.

In connection with the adoption of the CD&A requirements in 2006, the SEC proposed eliminating the then-required performance graph, which had been intended to show "the relationship, if any, between compensation and corporate performance, as reflected by stock price."[22] The SEC expressed its belief that "the requirement for the performance graph is outdated, particularly since the disclosure in the Compensation Discussion and Analysis regarding the elements of corporate performance that a given company's policies might reach is intended to allow broader discussion than just that of the relationship of compensation to the performance of the company as reflected by stock price."[23] In response to those objecting to the elimination of the performance graph, the SEC retained the performance graph requirement, but only for inclusion in annual reports (and not in filed proxy materials).[24] The SEC adhered to its "view that the performance graph should not be presented as part of executive compensation disclosure," reiterating that the graph could "weaken [the] objective" of encouraging broader discussion in the CD&A of the elements of corporate performance considered by the company.[25] The SEC should hold to that view and not require the performance graph to be presented as part of the pay versus performance disclosure.

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[22] Executive Compensation and Related Party Disclosure, Release Nos. 33-8655; 34-53185; File No. S7-03-06 (Jan. 27, 2006) at 21.
[23] *Id*. at 21-22.
[24] Letter from Simpson Thacher & Bartlett LLP dated July 6, 2015 at 2.
[25] Executive Compensation and Related Party Disclosure, Release Nos. 33-8732A; 34-54302A; File No. S7-03-06 (Aug. 29, 2006) at 44.

### C. *The Final Rules should eliminate any requirement for XBRL tagging.*

The Proposed Rules include a requirement to data-tag the new pay-versus-performance table in the XBRL format. The SEC believes this will be useful to investors. Although the frequency of use by investors is debated, we agree that high-quality and reliable data tagging is generally beneficial to investors, but only to the extent that such data is comparable.

Commentators have noted that "since the SEC has begun requiring the use of XBRL in 2009, XBRL-tagged information has been fraught with errors and comparability challenges."[26] The SEC itself has admitted that "a high rate of custom tagging inhibits comparability of data," thus, mounting to these comparability challenges. Yet, data shows that the average custom tag rate increased for all types of registrants from 2019 to 2020.[27]

We are concerned that inconsistent use of XBRL will be misleading to investors. For instance, since some information will be tagged and other information not tagged, there is increased risk that investors using the XBRL tags will skip over the untagged areas, thereby missing the connection between the tagged numerical information and the untagged narratives and explanatory notes that give context for this information.

However, if the SEC decides to retain the XBRL tagging requirement, we request that Inline XBRL be permitted for disclosures. As the SEC noted in 2018, Inline XBRL only requires preparation of one Inline XBRL document that is both human-readable and machine-readable.[28] Inline XBRL removes the unnecessary step of generating an HTML document, then tagging a copy of the data to create a separate XBRL exhibit.

## II. The Final Rules should only require disclosure of executive officers that will be helpful to investors in understanding the link between compensation actually paid during the year and company performance.

### A. *The Final Rules should limit application of the disclosure to the Principal Executive Officer ("PEO").*

Section 953(a) of Dodd-Frank does not prescribe which executive population is required to be included in the pay-versus-performance disclosure. However, we recommend the SEC expressly limit the disclosure to a registrant's PEO. We believe this compensation information is most relevant to investors, and doing so would create the most streamlined disclosure and lower the potential for confusion stemming from the inclusion of other named executive officers ("NEOs") (as explained below).

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[26] See letter in response to the Inline XBRL Filing of Tagged Data (Release No. 33-10323, 34-80133; File No. S7-03-17) from Ernst & Young LLP (May 16, 2017).
[27] *U.S. GAAP – XBRL Custom Tags Trend*, U.S. Securities and Exchange Commission (June 29, 2021), https://www.sec.gov/structureddata/gaap_trends_2020 (last visited Feb. 25, 2022).
[28] Inline XBRL Filing of Tagged Data, 83 Fed. Reg. 40846, 40851 (Aug. 16, 2018).

The Proposed Rules require non-PEO NEO compensation to be disclosed as an average, under the premise that averaging compensation would prevent large fluctuations resulting from turnover and changes among the registrant's executives. However, by doing so, the Proposed Rules create a number that is meaningless for purposes of evaluating the link between a registrant's pay and its performance. A registrant's compensation committee determines the compensation structure and level individually for each NEO. By averaging NEO compensation, the Proposed Rules ignore this decision-making process and create a compensation number which may not reflect the intended or actual pay, actual role or expected individual contribution of any NEO.

Additionally, limiting the pay-versus-performance disclosure to just the PEO does not mean that NEO compensation information would completely disappear. The compensation of NEOs would still be included in the SCT and likely other locations in the CD&A.

### B. *If there is more than one PEO during the year, disclosure should be excluded for that year.*

The Proposed Rules provide that if more than one person serves as PEO in a given year, then the disclosure for such persons shall be aggregated. However, for investors to best understand the link between pay-versus-performance and to prevent distortion, we recommend this rule be modified to eliminate disclosure in a year where there is more than one PEO. Alternatively, we recommend the disclosure focus solely on the PEO serving at the end of the year. If the SEC continues to require PEO aggregation in the Final Rules, we request that one-time, non-recurring payments such as severance payments and sign-on bonuses be excluded from the aggregated compensation total.

In a year where a PEO transition occurs, there is a significant risk that aggregating PEO compensation could be misleading to shareholders because of the unique factors at play during a PEO transition. For example, there may be separation payments to the outgoing PEO and sign-on or other bonuses for the incoming PEO, both of which represent one-time, non-recurring compensation outside of a registrant's customary compensation program. Aggregating PEO compensation in and of itself leads to distortions, but the inclusion of non-recurring payments would lead to even greater distortions and would not be helpful to investors in understanding the link between PEO pay and company performance.

## III. The Final Rules should provide registrants with maximum flexibility to determine compensation actually paid.

What is considered "actual compensation paid" to an executive officer could vary highly depending on how a registrant designs their overall compensation packages. Requiring disclosure based on a prescriptive definition originally designed for other purposes would create grossly misleading disclosure.

### A. *Form W-2 wages could be grossly misleading due to the ability to defer compensation and should be rejected as a potential metric.*

Form W-2 was designed to determine the timing of taxability of various forms of compensation. The analysis as to when compensation should be subject to taxation is not precisely analogous to determining when compensation should be disclosed to analyze a registrant's link between pay and performance. Certain elements of compensation may be awarded / earned as a result of performance during one fiscal year but, because it is subject to additional time-based vesting restrictions (i.e., a continuous employment requirement), may be subject to deferred taxation and not be reported on Form W-2 as taxable wages until a later fiscal year. The Final Rules should provide registrants with the flexibility to report pay awarded for performance during the prior fiscal year, even if such pay is subject to additional vesting conditions as this avoids potential disconnect between awarded pay for performance versus realized pay.

**B. *The Final Rules should only require disclosure of core components of compensation with flexibility to determine what additional disclosure is most useful in the pay versus performance context.***

The Final Rules should require disclosure of core elements of executive compensation, such as base salary, STI and LTI, but also provide registrants with maximum flexibility to determine what additional disclosure is most meaningful to investors. Limiting compensation reported in this manner will avoid potential distortions caused by other compensation elements such as broad-based retirement plans or nonqualified deferred compensation programs.

**C. *When amounts are disclosed with respect to STI and LTI awards should reflect when they are actually tied to performance.***

In order to provide meaningful data to investors, the timing of disclosure with respect to STI and LTI should reflect whether the amounts are tied to future company performance. Therefore, there should be three separate categories of awards: (i) cash awards, (ii) time-based equity awards (other than stock options and stock appreciation rights), and (iii) performance-based equity awards.

1. Cash award and time-based equity awards (other than stock options and stock appreciation rights) should be included in the year they are awarded.

Because there is no additional *company* performance required for an executive to earn cash awards or time-based equity awards (other than stock options and stock appreciation rights), the assumption is often that these types of awards are being made based on company performance prior to the grant date. Therefore, these forms of STI and LTI should be included in compensation in the year they are awarded based on the grant date fair market value.

2. Performance-based equity awards (including all stock options and stock appreciation rights) should be included in the year they are earned.

Performance-based equity awards, on the other hand, are those that require additional, future company performance before they can be earned by the executive recipient. Therefore, they are most closely tied to performance in the year they are actually earned, not the year they are granted. Performance-based equity awards should be included in compensation in the year they are actually

earned (i.e., the year they vest) based on the fair market value of the cash or equity actually received.

Because their value is tied to a registrant's stock price, it is inherently tied to company performance regardless of whether it is subject to additional performance metrics. Therefore, all stock options and stock appreciation rights should be considered performance-based equity awards – meaning they should be included in compensation in the year in which they vest and become exercisable, and the value should be the amount realizable by the executive as if the award were exercised on the first date possible.

## IV. The Final Rules should modify the disclosure periods to provide meaningful disclosure to investors.

The Proposed Rules generally require (for registrants that are not exempt or are not smaller reporting companies) registrants to provide the pay-versus-performance disclosure for such registrant's five most recently completed fiscal years.[29] The SEC has requested comment on various aspects of the applicable time periods, including whether they should be longer or shorter, and the use of transition periods.[30]

As explained below, we request that the Final Rules allow registrants the flexibility to use a three-year disclosure period and provide for transition periods.

### A. *The Final Rules should permit a three-year disclosure period.*

The pay-versus-performance disclosure should complement and reinforce the registrant's discussion of compensation in other sections of the proxy statement. As such, a three-year period will provide more meaningful disclosure for some registrants, and will be consistent with information investors are accustomed to reviewing.

1. <u>A three-year disclosure period will provide meaningful disclosure and better align with common compensation program performance periods.</u>

Rather than providing investors with more meaningful information, expanding the time period from three years to five years would be counterproductive to this objective for companies basing their compensation programs on three-year measurement periods. For example, a 2021 report detailing the long-term incentive practices and trends of the 250 largest companies in the S&P 500, found that 89% of companies measure performance-based LTI over a three-year period (consistent with 2019 and up 3% since 2015).[31] The SEC explicitly recognized this disconnect in its request for comments when it provided that "the disclosure may not necessarily align a particular executive's compensation with the period during which the registrant's performance may be attributed to the executive."[32] We believe that a better option would be to allow registrant's the

[29] 80 Fed. Reg. at 26332.
[30] *Id*. at 26342 (see request for comment 42).
[31] *2021 Top 250 Report*, FW Cook (Dec. 2021) at 8, https://www.fwcook.com/content/documents/Publications/12-29-21_FWC_2021_Top_250_Final.pdf (last visited Feb. 23, 2022).
[32] 80 Fed. Reg. at 26340 (see request for comment 23).

ability to choose the time period that accurately aligns executive compensation with the period during which the registrant's performance may be attributed to the executive. In order to address concerns that registrants would "cherry pick" periods that put such registrant in the best light, once a registrant has chosen a time period, such registrant would be required to report consistently or provide an additional disclosure explaining the reasoning for why disclosure over a different period is appropriate.

We also note that registrants are already required to disclose compensation for each of their last three completed fiscal years in the SCT. Instead of using time periods that are consistent with such longstanding disclosure requirements and the vesting period of most performance-based equity awards, the SEC proposes a five-year disclosure period. Absent an especially strong reason for departing from the time frame over which most companies measure executive performance and which is reported for the SCT, a three-year disclosure period should trump the speculative benefits of a longer period.

2. <u>A five-year disclosure period increases the likelihood of data distortion.</u>

The inclusion of two added years of data (with a five-year period) increases the likelihood of turnover in the PEO and NEO group. Correspondingly, the odds increase that the data will reflect information on more than one PEO and is unlikely to reflect a consistent group of NEOs. For interested investors, this inconsistency in the data reduces year to year comparability and fails to add meaningful information to investors.

### B. *The Final Rules should provide for transition periods.*

We express our general support for transition periods for smaller reporting companies (and all other registrants). Providing transition periods will allow more time to refine compensation strategies and presentation of the pay-versus-performance disclosure to shareholders.

## V. Clear Description

### A. *The Final Rules should require the application of the Plain English Principles.*

Exchange Act Section 14(i) requires a "clear description" of the compensation disclosure required by Item 402 of Regulation S-K, and the SEC has requested comment about whether it is appropriate to apply the Plain English principles to the pay-versus-performance disclosures.

We express our view that it is appropriate to apply the Plain English principles to the pay-versus-performance disclosures and agree with other commenters[33] that applying the Plain English principles would be of direct benefit to shareholders and potential investors in reviewing the complex, lengthy, and cumbersome pay-versus-performance disclosures.

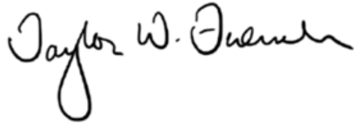
## VI. Closing

We would like to thank you for the opportunity to provide you with our comments.

[33] See, e.g., letter from Pay Governance LLC, dated June 30, 2015.

We welcome the opportunity to further discuss the concerns and recommendations set forth in this letter and hope that we can be a resource to the SEC as you review and consider all of the comments. If you have any questions, please do not hesitate to contact Taylor Wedge French at [redacted] or Rosemary Becchi at [redacted].

Sincerely,



Taylor Wedge French
Partner, **McGuireWoods**

Rosemary Becchi
Strategic Advisor and Counsel,
**Brownstein Hyatt Farber Schreck**