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November 19, 2021

Officers
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: File Number S7-12-15, Implementation of Dodd-Frank Section 954

Dear Officers,

On behalf of more than 500,000 members and supporters of Public Citizen, we welcome the invitation from the Securities and Exchange Commission (SEC, Commission) to comment on the proposal to finalize implementation of Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

The Dodd-Frank Act grew from the financial crash of 2008 that was rooted in dangerous compensation structures. These structures promoted the issuance and securitization of mortgages regardless of the ability of borrowers to repay. A number of sections in Title IV of Dodd-Frank address bank-related pay structures. Most important is Section 956, a ban specifically on bank compensation that leads to "inappropriate" risk-taking. The statute mandates completion of this rule by May 2011, a date now ten years in the past. We are gratified that the SEC lists completion of that much needed rule in its official work plan.

By contrast, Section 954 applies to all companies that seek to remain listed on a stock exchange. This statute requires little justification. Incentive compensation based on results that are later proven false should be recovered—clawed back. If executives receive a bonus based on a reported increase in sales, for example, and a subsequent audit finds that sales did not increase, that bonus should be returned.

We appreciate that the SEC will consider our comment from 2015 as it looks to finalize this rule.[1] Our comments here relate to additional questions asked by the SEC, along with additional information and research that has emerged since 2015.

Generally, the number of reported restatements has declined steadily in the half decade, from roughly 300 in 2014 to less than 100 in 2020.[2] A restatement is a formal revision of a firm's financial results. Ideally, this represents more honest and accurate accounting as well as stricter oversight by independent audit firms, although this circumstance may be debated.[3] Claw backs, even in the face of misstatements due to fraud, have been rare.[4] But without implementation and enforcement of a robust SEC rule on claw backs, corporate overseers may continue to fail in their obligation to recoup ill-gotten gains.

Several companies have opted to issue "revisions" instead of wholesale restatements when they detect material errors.[5] We believe the SEC's final rule requiring a claw back should cover all such corrections of past reporting errors. We support the SEC's proposal that restatements to correct errors that are material to the previously issued financial statements would be considered "an accounting restatement due to material noncompliance" and result in a claw back recovery analysis.[6]

In its materials regarding this comment opportunity, the SEC asks whether it should change certain language regarding the three-year lookback period. In the 2015 proposed rule, the SEC proposed that the date tripping this look-back period would be when corporate official concluded, or "reasonably should have concluded," that a restatement was required. In its October 2021 comment solicitation, the SEC asks if the "reasonably should have concluded" standard should be removed. We believe this standard should be sustained because it would

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[1] Bartlett Naylor, *Comment,* SECURITIES AND EXCHANGE COMMISSION (Sept. 1`4, 2015) https://www.sec.gov/comments/s7-12-15/s71215-9.pdf

[2] Amanda Iacone, *Companies Fixing More Errors by Revisions Than Restatements,* BLOOMBERG, (Jan. 30, 2020) https://news.bloombergtax.com/financial-accounting/companies-fixing-more-errors-by-revisions-than-restatements

[3] In a 2013 speech regarding the reduction in restatements, then SEC enforcement officer Andrew Ceresney said: "But I have my doubts about whether we have experienced such a drop in actual fraud in financial reporting as may be indicated by the numbers of investigations and cases we have filed. It may be that we do not have the same large-scale accounting frauds like Enron and Worldcom. But I find it hard to believe that we have so radically reduced the instances of accounting fraud simply due to reforms such as governance changes and certifications and other Sarbanes-Oxley innovations. The incentives are still there to manipulate financial statements, and the methods for doing so are still available. We have additional controls, but controls are not always effective at finding fraud." Andrew Ceresney, *Financial Reporting and Accounting Fraud,* SECURITIES AND EXCHANGE COMMISSION (Sept 19, 2013), https://www.sec.gov/news/speech/spch091913ac

[4] Patrick Velte, *Determinants and Consequences of Claw back Provisions in Management Compensation Contracts: A Structured Literature Review On Empirical Evidence*, BUSINESS RESEARCH (Nov. 2020) https://link.springer.com/article/10.1007/s40685-020-00135-9#Sec1

[5] Amanda Iacone, *Companies Fixing More Errors by Revisions Than Restatements,* BLOOMBERG, (Jan. 30, 2020) https://news.bloombergtax.com/financial-accounting/companies-fixing-more-errors-by-revisions-than-restatements

[6] *Reopening of Comment Period for Listing Standards for Recovery of Erroneously Awarded Compensation*, SECURITIES AND EXCHANGE COMMISSION (Oct. 2021) https://www.sec.gov/rules/proposed/2021/33-10998.pdf

allow litigants to hold the company to this higher standard when the corporate officials failed to take appropriate responsibility for its errors. While some errors may have been made in good faith, others may be due to misconduct.

We support the new proposal to require disclosure of how companies calculate the amount to be recovered following the restatement. This should require no additional cost as the company would have itself calculated the value to recoup the compensation.

The SEC asks about claw backs at companies that award discretionary compensation not directly tied to a quantifiable formula following a restatement. For example, some companies are beginning to include environmental, social and governance (ESG) issues in establishing executive compensation. One analysis shows that more than 10 percent of European companies and about 2 percent of US companies link improvements in CO2 emissions to incentive plans.[7] As world attention-- including shareholder interest-- in climate change becomes more intense, we imagine an increase in the motivation to exaggerate some claims of success, claims that may need to be revised, and therefore subject to a claw back. Volkswagen, for example, manipulated its engines when owners had them inspected for emissions so as to show an improved performance.[8] The manipulated test results showed such low emissions that the car won a "Green Car of the Year" award. The company's bonus system, according to one analysis, contributed to the culture that led to the manipulation.[9] Separately, a study of power utilities showed that most failed to live up to their pledges of adapting to clean energy.[10] In fact, false claims about corporate environmental responsibly has a common name: greenwashing. [11]

Other firms tie compensation to such standards as customer satisfaction.[12] These may involve qualitative standards. In fact, companies commonly use qualitative versus quantitative factors in awarding executive compensation.[13] We believe that companies should disclose publicly any discretionary compensation they do or do not chose to recoup. Ideally, such disclosures will prompt recoupment officers to oblige shareholders rather than executive peer pressure. Public

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[7] Shai Ganu, *Combating climate change through executive compensation*, WillisTowersWatson (Sept. 30, 2020) https://www.willistowerswatson.com/en-US/Insights/2020/09/Combating-climate-change-through-executive-compensation

[8] Russell Hotton, *Volkswagen, the Scandal Explained*, BBC (Dec. 10, 2015) https://www.bbc.com/news/business-34324772

[9] Leah Goodman, *Why Volkswagen Cheated*, Newsweek (Dec. 15, 2015) https://www.newsweek.com/2015/12/25/why-volkswagen-cheated-404891.html

[10] John Romankiewicz, *The Dirty Truth about Utility Climate Pledges,* Sierra Club (January 2021) https://coal.sierraclub.org/the-problem/dirty-truth-greenwashing-utilities

[11] Bruce Watson, *The Troubling Evolution of Corporate Greenwashing*, The Guardian (Aug 20), 2016) https://www.theguardian.com/sustainable-business/2016/aug/20/greenwashing-environmentalism-lies-companies

[12] Camila Domonoske, *Some CEOs Are Hearing A New Message: Act On Climate, Or We'll Cut Your Pay*, NPR (April 20, 2021) https://www.npr.org/2021/04/20/988686847/some-ceos-are-hearing-a-new-message-act-on-climate-or-well-cut-your-pay

[13] Ahmet Kurt, *Don't Base Exec Bonuses on Subjective Criteria,* CFO (Jan. 18, 2019) https://www.cfo.com/compensation/2019/01/dont-base-exec-bonuses-on-subjective-criteria/

disclosure should help hold officers accountable when they decide whether or not to claw back compensation based on qualitative measures that subsequently prove unfounded.

The SEC asks for comments about the costs of implementing the claw back rule. Many companies have already adopted such policies. Moreover, claw backs are considered basic good corporate governance. We believe the SEC should also consider the benefits. Some of these are clearly quantifiable. For example, the amount of the claw back itself represents a benefit, as it would increase the value of the firm and shareholder wealth. Further, the existence of a strong claw back policy can help promote management accountability, reducing the level of future penalties from misconduct. The banking industry alone paid more than $100 billion stemming from mortgage frauds connected to the 2008 financial crash.[14] If even a fraction of this would be calculated as a benefit of a robust claw back rule, it would surely outweigh the administrative costs of instituting Section 954.

Again, we applaud the SEC for moving this important rule to finalization. Executive compensation figures at the center of corporate behavior—both laudable and illicit-- and must be governed zealously. It is imperative that compensation granted for outcomes that prove illusory should be returned.

For questions, please contact Bartlett Naylor at [redacted].

Sincerely,

Public Citizen

[14] *Wall Street's Crime Spree,* BETTER MARKETS (Jan 13, 2021) https://www.bettermarkets.org/sites/default/files/documents/Details_Report_Wall_Street's_Six_Biggest_Bailed-Out_Banks_2021.pdf