



THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
SCOTT M. STRINGER

November 22, 2021

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

Re: File No. S7-12-15

Dear Ms. Countryman:

I write to express support for the SEC's proposed rule to implement Section 954 of the Dodd-Frank Act, *Listing Standards for Recovery of Erroneously Awarded Compensation* (the "Proposed Rule"). I also write to recommend additions to the Proposed Rule based on my office's extensive experience negotiating policies with portfolio companies for compensation recovery from their senior executives ("Clawback Policies"). As Comptroller of the City of New York, I am a trustee of four of the City's five retirement systems and investment adviser to all five systems (collectively the "New York City Retirement Systems" or "NYCRS"). NYCRS had \$273 billion in assets as of August 30, 2021, including \$83 billion invested in more than 3,000 publicly traded U.S. companies.

I strongly encourage the SEC to extend the Proposed Rule to require listed U.S. companies to adopt Clawback Policies that authorize their boards of directors to claw back incentive compensation from Section 16 executives who are responsible for detrimental conduct, including misconduct, excessive risk taking or other actions, such as failure to supervise others, that causes significant financial or reputational harm to the company ("Detrimental Conduct Trigger"). These changes will align the Proposed Rule with market practices in the United States, U.K. regulatory standards, as well as the direction of regulation in other jurisdictions outside the United States.

Additionally, the SEC should revise the Proposed Rule to require disclosure of a company's Clawback Policy or its key terms (e.g., triggering events) in the company's annual proxy statement, as well as any actions taken pursuant to the Clawback Policy, including but not limited to clawbacks arising out of financial restatements. Such disclosure will allow investors to monitor a board's application of the Clawback Policy and provide investors with decision useful information that is critical to informed proxy voting.

Clawback Policies that include a Detrimental Conduct Trigger (and apply to supervisory failures), along with appropriate disclosure, will increase financial accountability for senior executives, and encourage ethical conduct and more effective legal and regulatory compliance throughout the organization. It will also enable a board of directors to discourage excessive risk-taking, lax compliance oversight and short-termism, and align executive compensation with *sustainable* performance. Without such changes, a board of directors can allow senior executives to retain incentive compensation that turns out to have been based on detrimental conduct by them or their subordinates, creating a perverse incentive for executives to "look the other way."

Clawback Policies Should Include a Detrimental Conduct Trigger

As the Economist reported earlier this year, “[t]he most striking change of recent years has been the rise of the ‘clawback.’ What initially applied solely to criminal financial conduct now extends to almost anything that might damage a firm’s reputation. That includes creating a toxic corporate culture, sexual harassment and ‘inappropriate’ personal relationships.”¹

Corporate Clawback Policies have evolved since the Proposed Rule was issued in 2015, and most companies now include triggering events beyond financial restatements because significant damage to a company can be caused by executive misconduct that does not necessitate a financial restatement. In addition, under certain circumstances, it may be appropriate for a board to claw back *more* compensation than would be recovered under an accounting restatement.

Some of the most noteworthy examples of executive compensation clawbacks since the 2010 enactment of the Dodd Frank Act — at Goldman Sachs, JP Morgan Chase, and Wells Fargo — were facilitated by the provisions of their respective Clawback Policies, which included a Detrimental Conduct Trigger. Significantly, prior to their clawback actions, my office negotiated new or enhanced detrimental conduct provisions in Clawback Policies with each of the three financial firms, among others.²

Clawback Policies Negotiated at Leading Companies

Since 2012, my office has negotiated enhanced Clawback Policies with 27 leading companies in response to NYCRS’ shareholder proposals.³ In addition, my office participated in a working group comprised of 13 institutional investors and six pharmaceutical companies convened by the UAW Retiree Medical Benefits Trust, which issued “Principal Elements of the Leading Practices Recoupment Policy” (“Principal Elements”),⁴ as described in the September 14, 2015 comment letter on the Proposed Rule submitted by the working group’s investor members.⁵

Consistent with the Principal Elements and the specific request in NYCRS’ shareholder proposals, the Clawback Policies my office negotiated generally provide the companies’ boards with broad discretionary authority to claw back compensation from senior executives based on the following:

1. Violation of law or company policy that causes significant financial or reputational harm to the company, including conduct that may not rise to the level of criminality or cause for dismissal; in most cases, there is no requirement for a finding of intentional misconduct or gross negligence.

¹ “How to design CEO pay to punish iniquity, not just reward virtue,” The Economist, February 18, 2021; at <https://www.economist.com/business/2021/02/20/how-to-design-ceo-pay-to-punish-iniquity-not-just-reward-virtue>.

² Moyer, Liz, “Banks Bow to New York on Clawbacks,” The Wall Street Journal, March 13, 2013; <https://www.wsj.com/articles/SB10001424127887324077704578358791840450814>.

³ The 27 companies include Abbvie, Allergan, Assertio Holdings, BB&T Corporation, Boeing, Boston Scientific Corporation, Capital One Financial Corporation, Citigroup Inc., CVS Health Corp, Encore Capital Group, Equifax, Gilead Sciences, Goldman Sachs, Halliburton, Insys Therapeutics, Johnson & Johnson, JPMorgan Chase, Lockheed Martin, Merck & Co., Inc., Morgan Stanley, Navient Corporation, Northrop Grumman, Pfizer Inc., PNC Financial Services, United Continental Holdings, Inc., United Technologies, and Wells Fargo & Company.

⁴ “Pharmaceutical Companies, Investor Coalition Develop Industry Standard-Setting Principles for Recoupment Policies Covering Major Compliance Failures,” UAW Retiree Medical Benefits Trust Press Release, April 4, 2013; at <https://www.prnewswire.com/news-releases/pharmaceutical-companies-investor-coalition-develop-industry-standard-setting-principles-for-recoupment-policies-covering-major-compliance-failures-201421791.html>

⁵ Available at <https://www.sec.gov/comments/s7-12-15/s71215-18.pdf>.

2. Failure to manage or monitor employees who committed the detrimental conduct.

In addition, some of the negotiated Clawback Policies reference other policies or specific conduct that the board is seeking to deter. For example, following a NYCERS shareholder proposal and engagement by NYCERS and the working group's investor members, Assertio Holdings (formerly Depomed) adopted a policy in 2018 that allows its board to claw back compensation from an executive for a "material violation of the company's code of conduct," as well as for misconduct "resulting or likely to result in the creation or perpetuation of a *hostile work environment*."⁶

Finally, most of the Clawback Policies require disclosure, under certain circumstances, of the company's claw back actions, thereby allowing investors to monitor the board's application of the Clawback Policy.

Case Studies: Goldman Sachs, JP Morgan Chase and Wells Fargo

Clawback Policy provisions like those recommended above enabled the boards at three major banks to claw back substantial compensation from senior executives responsible for misconduct that was costly for the company. Moreover, the ability of the boards to require executive accountability under these circumstances was critical to setting a strong tone at the top and encouraging future ethical conduct, as well as more effective legal and regulatory compliance throughout the organization. The companies sent an important message to investors and regulators through the following enhancement and subsequent application of their Clawback Policies:

- Goldman Sachs announced in October 2020 that it would attempt to claw back approximately \$174 million from a dozen current and former executives after the company agreed to pay \$2.9 billion in penalties and fees to settle federal charges over its involvement in a Malaysian bribery scheme. Goldman Sachs enhanced its Clawback Policy in 2012 in response to a NYCERS shareholder proposal.⁷
- Wells Fargo announced in September 2016 that it would claw back \$41 million from CEO John Stumpf and \$19 million from former senior vice president Carrie Tolstedt. The bank agreed to pay \$185 million to settle federal and local charges for fraudulently opening thousands of deposit and credit card accounts without customers' knowledge. Significantly, Ms. Tolstedt's 2015 incentive compensation was based on "continued growth in primary checking customers and continued success in increasing online and mobile banking customers," metrics which proved erroneous but did not require a financial restatement. Wells Fargo enhanced its Clawback Policy in 2013 in response to a NYCERS shareholder proposal, which enabled the company to claw back substantial incentive compensation from the senior executives responsible for the fraudulent accounts.⁸

⁶Assertio Holdings, Inc. Executive Compensation Clawback Policy; at

https://s28.q4cdn.com/742207512/files/doc_downloads/gov-docs/Executive-Compensation-Clawback-Policy.pdf

⁷ Goldman Sachs agreed in 2012 to clarify that its clawback policy can be triggered when excessive risk taking or improper conduct causes, or could reasonably be expected to cause, a material adverse impact on a particular business unit, and not just on the firm as a whole. It also agreed to clarify that the policy covers all employees involved in the underlying product, service, or transaction, including those who participated in a supervisory role.

⁸In March 2013, Wells Fargo's board adopted a policy that, among other provisions, includes a detrimental conduct trigger with reasonable threshold and that may be applied to employees who improperly, including in a supervisory capacity, failed to identify, escalate, monitor, or manage risks material to the company or the employee's business group. Subsequently, in a September 22, 2016 letter, I called on Wells Fargo's board to enforce its clawback policy and estimated that the board could claw back up to \$41 million from John Stumpf and up to \$19 million from Carrie Tolstedt; the letter is available at https://comptroller.nyc.gov/wp-content/uploads/2017/02/Comptroller-Stringer-To-Wells-Fargo_9.22.2016.pdf.

- JPMorgan announced in July 2012 that three executives responsible for the “London Whale” trading loss, which had grown to as much as \$5.8 billion, would be subject to maximum clawbacks, reportedly equal to about twice their annual compensation. In response to a NYCRS shareholder proposal, JPMorgan strengthened its Clawback Policy before announcing its London Whale clawback actions.⁹

Unlike Wells Fargo, Goldman Sachs and JPMorgan restated earnings as a result of the reported misconduct, in each case for one quarter. However, both boards had broad discretionary clawback authority that permitted the magnitude of their clawback, which appears to have exceeded the amount of compensation that would have been clawed back under the accounting restatements.

Clawback Policies are Now Universal and Detrimental Conduct Triggers are the Norm and Supported by Institutional Investors

Clawback Policies are more prevalent than when the SEC issued the Proposed Rule in 2015, and today nearly all U.S. listed companies have some form of Clawback Policy. While in the Proposed Rule (p. 108), issued in 2015, the SEC estimated that approximately 23% of all filers then disclosed some form of an executive compensation recovery policy, 100% of S&P 500 companies, and 99.7% of the remaining 2500 companies in the Russell 3000 index, now have some form of Clawback Policy, according to the ISS QualityScore database. ISS defines clawback as “the company’s ability to recoup performance-based awards in the event of a fraud, restatement of results, errors/omissions or other events as may be determined.”

Clawback Policies that authorize claw back of compensation in the context of both the restatement of financial statements and Detrimental Conduct Triggers are now the norm in the U.S. A 2017 study provided a detailed analysis of 4,103 compensation clawback provisions used by S&P 1,500 firms through 2013¹⁰ and found that most (51.8%) companies included “misconduct and negligence of fiduciary duty” as triggering events.¹¹ At larger companies, it was already the leading practice by 2013. According to the Equilar report, cited in the Proposed Rule (footnote 269) regarding the prevalence of Clawback Policies, most (71.8%) of the more than 89% of Fortune 100 companies that had Clawback Policies in 2013 permitted recovery of compensation from executives in the event of a financial restatement or ethical misconduct.

Continued adoption of Detrimental Conduct Triggers is consistent with NYCRS’ extensive experience engaging our portfolio companies and reviewing proxy statements when casting proxy votes at roughly 3000 U.S. companies. It is also consistent with widespread institutional investor support for Clawback Policies that include Detrimental Conduct Triggers. This support is reflected in the Council of Institutional Investors’ member-approved Policies on Corporate Governance,¹² and in institutional investors’ proxy voting policies. According to “The State of Play on Clawbacks and Forfeitures Based on

⁹JPMorgan agreed to disclose that the materiality threshold required to trigger its clawback provisions is not limited to an impact on the firm as a whole, but also on a business or sub-business. The firm also agreed to clarify that its clawback provisions would apply to acts or omissions and that they could apply to persons in a supervisory role.

¹⁰Babenko, Ilona, Benjamin Bennett, John M. Bizjak and Jeffrey L. Coles, “Clawback Provisions,” July 14, 2017; at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2023292.

¹¹Ibid. p. 47

¹² According to CII policies, “Clawback policies should ensure that boards can refuse to pay and/or recover previously paid executive incentive compensation in the event of acts or omissions resulting in fraud, financial restatement or some other cause the board believes warrants recovery, which may include personal misconduct or ethical lapses that cause, or could cause, material reputational harm to the company and its shareholders. Companies should disclose such policies and decisions to invoke their application;” at https://www.cii.org/corp_gov_policies

Misconduct,”¹³ large institutional investors (e.g., BlackRock, CalPERS, and JPMorgan) are using their proxy voting policies to increasingly encourage companies to expand their Clawback Policies “to provide discretion covering management misconduct that results in significant reputational harm or adverse publicity unrelated to a financial restatement and executives who supervise employees who engaged in misconduct.”

Detrimental Conduct Triggers Will Bring the U.S. Regulatory Regime into Line with UK Regulatory Standards and other International Regulations

Including Detrimental Conduct Triggers in the Proposed Rule will bring SEC regulation in line with market practice in the United States, as well as the UK Corporate Governance Code and regulations in other jurisdictions. Currently, the UK Code recommends that companies subject to Financial Reporting Council (FRC) regulation include malus¹⁴ and clawback provisions in certain specified circumstances, which it states, “might include payments based on *erroneous or misleading data, misconduct, misstatement of accounts, serious reputational damage and corporate failure.*”

The clawback provisions contained in the UK Code may be amended and strengthened with respect to triggering events. In a March 2021 white paper, “Restoring Trust in Audit and Corporate Governance,”¹⁵ the UK government proposed asking the FRC to amend the UK Code to strengthen malus and clawback provisions and proposed “minimum conditions within which clawback provisions can be triggered.” The minimum conditions include the following:

- Material misstatement of results or an error in performance calculations
- Material failure of risk management and internal controls
- Misconduct
- Conduct leading to financial loss
- Reputational damage; and
- Unreasonable failure to protect the interests of employees and customers.

In addition to the UK Corporate Governance Code, bank regulations in some foreign jurisdictions also provide for misconduct triggers, including:

- The Dutch Financial Supervision Act specifies that a financial business must reclaim variable remuneration from a natural person if that person's conduct has had a *significantly adverse impact on the business*; and
- The German Ordinance regarding Remuneration in Financial Institutions (GORFI) provides for a mandatory clawback of variable remuneration already paid out if a risk-taker proved to have a *negative impact on the overall success of a company*.

¹³ Ocker, Jonathan, Justin Krawitz, and Ben Gibbs, “The State of Play on Clawbacks and Forfeitures Based on Misconduct,” Pillsbury Winthrop Shaw Pittman LLP, July 7, 2019; at <https://corpgov.law.harvard.edu/2019/07/07/the-state-of-play-on-clawbacks-and-forfeitures-based-on-misconduct/>.

¹⁴ Malus provisions allow a company to reduce or cancel a senior executive's bonus or share award before it has been paid out (or the shares issued or transferred)..

¹⁵ Available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/970676/restoring-trust-in-audit-and-corporate-governance-command-paper.pdf.

Requiring Clawback Disclosures in the Proxy Statement Will Better Enable Investors to Apply Their Proxy Voting Guidelines

The disclosure provisions in the Proposed Rule will be most decision-useful to investors if disclosure of the Clawback Policy, or at least its key terms (e.g. triggering events), and any actions taken pursuant to that policy (including but not limited to clawbacks arising out of restatements of company financial statements), are also included in the Compensation Discussion and Analysis (“CDA”) in the annual proxy statement. While the Proposed Rule requires issuers to file their written recovery policy, and any actions taken pursuant to that policy, as an exhibit to their annual report, the CDA is generally where companies describe their Clawback Policies.

Importantly, these disclosures can inform investors’ proxy voting decisions, particularly on “Say-on-Pay” and the election of directors. For example:

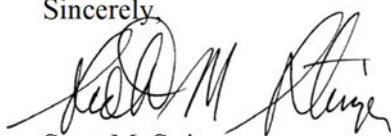
- According to its Proxy Voting Guidelines, CalPERS, will consider an against vote for the Say-on-Pay proposal for “[l]ack of a comprehensive clawback policy,” among other problematic pay features,¹⁶ and believes that “companies should develop and disclose policies to recoup compensation made to executives during periods of fraudulent activity, inadequate oversight, misconduct including harassment of any kind such as sexual harassment, or gross negligence, which impacted or is reasonably expected to impact financial results or cause reputational harm.”
- According to a report by Georgeson, JPMorgan updated its Global Proxy Voting and Policy Guidelines in 2020 to add “the issue of clawback of compensation to its list of reasons to generally withhold votes from directors. As included in its updated policy, JPM will generally withhold votes from the chair of the board, the lead independent director or the chair of the governance committee at a company where the board failed to recoup compensation from employees who departed due to significant misconduct.”¹⁷

In sum, the Proposed Rule should be expanded to include a Detrimental Conduct Trigger that will align executive compensation with ethical conduct, legal and regulatory compliance, and long-term sustainable business practices. In addition, the Proposed Rule should require relevant disclosure in the proxy statement. These measures will give boards the tools they need to deter misconduct and hold executives accountable, consistent with investor expectations, and give investors the information they need to make informed proxy voting decisions.

I believe my recommendations will meaningfully strengthen the Proposed Rule. Please contact Michael Garland, Assistant Comptroller for Corporate Governance and Responsible Investment ([REDACTED]) if you have questions.

Thank you for your consideration.

Sincerely,



Scott M. Stringer
New York City Comptroller

¹⁶ CalPERS Proxy Voting Guidelines, April 2021; at <https://www.calpers.ca.gov/docs/proxy-voting-guidelines.pdf>

¹⁷ Kumar, Rajeev, “2020 J.P. Morgan Policy Updates,” Georgeson, May 11, 2020; at <https://www.georgeson.com/us/2020-jp-morgan-policy-updates>.