

Clawbacks: New Listing Standards for Public Companies

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On June 9, 2023, the United States Securities and Exchange Commission (SEC) approved new listing standards for public companies listed on The Nasdaq Stock Exchange (Nasdaq) and the New York Stock Exchange (NYSE). The new standards will take effect on October 2, 2023, and require listed companies to adopt written clawback policies by December 1, 2023. The new standards will be codified in Nasdaq Listing Rule 5608 and NYSE Listed Company Manual Section 303A.14.

What do the new listing standards require?

Clawback Policy Requirements

Listed companies are required to adopt a written clawback policy that, in the event of a restatement of a company's financial statements, recoups excess incentive-based compensation awarded to current and former executive officers. The clawback policies must apply to any erroneously awarded incentive-based compensation received on or after October 2, 2023.

The company's clawback policy must be triggered by both "Big R" and "little r" restatements. A Big R restatement corrects an error that is material to a previously issued financial statement. A little r restatement corrects an error in the current period that would result in a material misstatement if not corrected.

The 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." This includes compensation derived in whole or in part from measures such as EBITDA, stock price, or total shareholder return. This does not include compensation based solely on continued employment, such as salaries or discretionary bonuses that are not based on financial reporting measures, or time-based equity awards.

For purposes of the clawback policy, compensation will be deemed received by the executive officer when the financial reporting measure is attained, even if the executive officer is actually paid or granted the

incentive-based compensation at a later date.

The amount of incentive-based compensation that must be recoverable under the clawback policy is the amount of incentive-based compensation that exceeded the amount of incentive-based compensation that would have been received had it been determined based on the amounts in the restated financial statements.

Filing Requirements

Listed companies must file their clawback policy as an exhibit to their annual report.

Listed companies must also indicate on the cover page of the annual report, via a check box, whether there has been any restatement that triggered the clawback policy. If the company makes a little r or Big R restatement, the company must disclose how much incentive-based compensation was subject to recovery, how much has remained outstanding for at least 180 days since the company determined the amount owed, and, if applicable, details regarding any reliance on an impracticability exception.

These disclosures are required to be Inline XBRL tagged.

What time period must be covered by the clawback policy?

In the event of a Big R or little r restatement, incentive-based compensation must be subject to recoupment if it is "received" during the three completed fiscal years prior to the date the company was required to prepare a financial restatement.

What companies are covered by the new listing standards?

Companies with securities listed on Nasdaq or the NYSE are required to comply with the new listing standards, including smaller reporting companies, emerging growth companies, foreign private issuers, and newly listed issuers.

The only companies exempted from the new listing standards are issuers of security futures products, standardized options, unit investment trust securities, and certain registered investment company securities.

Which executives are covered by the new listing standards?

The clawback policy must apply to current executive officers and executive officers serving in the past three years who received incentive-based compensation, including a company's president, principal financial officer, principal accounting officer, any vice president in charge of a principal business unit, and any other person with a policy-making function for the company.

The new listing standards require that companies recoup incentive-based compensation erroneously awarded to all covered executive officers, even if the executive officer did not engage in misconduct and did not know the incentive-based compensation was erroneously awarded.

Can a company indemnify executive officers?

No. Listed companies cannot indemnify or reimburse any executive officer for erroneously received compensation. Listed companies likewise cannot pay or reimburse executive officers for paying insurance premiums on a policy that covers potential recovery obligations.

What should companies do now?

- Draft and approve a compliant clawback policy or review your existing clawback policy to ensure compliance.
- Review any existing compensation recovery policies and consider whether they are consistent with the new listing standards.
- Identify covered officers.
- Take steps to ensure effective controls exist to track incentive-based compensation that has been awarded.
- Review indemnification and insurance obligations.

The listing standards have very limited exceptions in the case of extreme hardship and impracticability. Listed companies should anticipate needing to carefully comply with the new listing standards and must adopt written clawback policies by December 1, 2023. Companies that fail to comply with the new listing standards will be subject to delisting.

The Lowenstein Sandler Capital Markets & Securities practice group and Employee Benefits & Executive Compensation practice group regularly counsel companies on the complexities of listing requirements. Please contact the Lowenstein Sandler attorney with whom you regularly work if you have any question about how to comply with the new listing standards.

Contacts

Please contact the listed attorneys for further information on the matters discussed herein.

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