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## Designing and Implementing Executive Compensation Clawbacks



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*An Expert Q&A with Deb Lifshey, providing critical insights into designing and implementing executive compensation clawbacks. In a conversation with Practical Law's Jessica Cherry, Deb addresses the scope of SEC Rule 10D-1, the mandatory clawback rule that was promulgated under Section 954 of the Dodd-Frank Act (Dodd-Frank), outlines the widespread criticism the rule has received, including that it is overly onerous and extends beyond Dodd-Frank's mandate, and details clawback trends, including the common practice of adopting both a mandatory Dodd-Frank-compliant policy and a supplemental policy that gives discretion to the board of directors to determine whether and how to recover erroneously received compensation in situations not covered by the Dodd-Frank-compliant policy. Deb also addresses the importance of preparing for a potential restatement that triggers a clawback by establishing formal processes and testing those processes using hypothetical restatement scenarios.*

Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) in response to the 2008 financial crisis. Its purpose was to restructure the financial regulatory system to restore public confidence and prevent another crisis from occurring. One component of this restructuring initiative was to impose compensation-related measures that were designed to promote transparency and ensure that compensation does not reward excessive risk-taking.

Section 954 of Dodd-Frank added a new Section 10D to the Securities Exchange Act of 1934, under which listed companies must adopt a policy that provides for recoupment of executive incentive compensation if an accounting restatement is required due to material non-compliance with any financial reporting requirements (that is, a clawback policy). The clawback policy must require the company to recover from any current or former executive officer any incentive compensation received during the three-year period preceding the accounting restatement that is in excess of what would have been paid based on the

restated financial information.

The clawback requirement is triggered by the need for an accounting restatement, without regard to:

- Whether any misconduct occurred.
- An executive officer's responsibility for the erroneous financial statements.

Section 10D requires the Securities and Exchange Commission (SEC) to adopt rules implementing this clawback requirement. In October 2022, over 12 years after Dodd-Frank was signed into law, the SEC adopted Rule 10D-1 (the Clawback Rule), which became effective on January 27, 2023.

While waiting for the SEC to act (and in some cases even before Dodd-Frank was enacted), many companies voluntarily adopted tailored clawback policies, which:

- Often were tied to misconduct.
- Typically gave discretion to the board of directors or compensation committee to decide whether and how to recoup erroneously received compensation in various circumstances.

These policies were quite different from the policies that companies would eventually be required to adopt and implement under the Clawback Rule, which has been widely criticized for:

- Going well beyond Dodd-Frank's mandate.
- Being overly prescriptive, rigid, and inflexible.
- Creating unnecessary and overly burdensome costs to companies.

In June 2025, the SEC held a roundtable discussion on executive compensation disclosure requirements (Roundtable), which included substantial commentary on certain rules promulgated under Sections 953 (which addresses pay ratio and pay-versus-performance disclosure) and 954 of Dodd-Frank (the Dodd-Frank Rules). The Clawback Rule, among other items, received considerable criticism from participating panelists, many of whom lamented that the Clawback Rule will:

- Incentivize the wrong kind of behavior (for example, by encouraging companies to adopt programs that do not align with shareholder interests and/or are not incentive-based).
- Ultimately hurt both companies and investors by creating significant compliance costs without attendant benefits.

The SEC has also received comment letters from law firms and others recommending changes to the executive compensation disclosure rules and the Dodd-Frank Rules, including the Clawback Rule.

It is impossible to foretell what action, if any, the SEC will take in response to the Roundtable and submitted comments. While some practitioners predict that a wholesale

revision of the executive compensation disclosure rules is imminent, others believe that, at least in the near-term, the SEC will focus only on those rules that are currently having a significant, adverse impact on companies while providing little or no upside to investors. For example, the pay-versus-performance rule, which became effective in October 2022, has been nearly universally criticized for its high complexity and compliance costs as well as its limited usefulness to investors.

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Jessica Cherry of Practical Law asked Deb Lifshy of Pearl Meyer to address:

- The breadth of the Clawback Rule, including ways in which it requires companies to go beyond the specific legislative Dodd-Frank mandate.
- The most substantial negative implications and unintended consequences of the Clawback Rule.
- The likelihood that the SEC will significantly revise the Clawback Rule in response to the Roundtable and other feedback.
- Issues that companies should consider when adopting and maintaining a tailored supplemental clawback policy in addition to a mandatory Dodd-Frank-compliant policy (including the importance of coordinating these policies).
- Current clawback policy trends, including the types of triggers that companies are including in their policies.
- Key elements companies should consider when designing a clawback policy.
- What processes companies should establish to prepare for a potential accounting restatement that triggers a clawback obligation.

Do you agree with critics who assert that the Clawback Rule is overly prescriptive and requires companies to go far beyond Dodd-Frank's mandate?

Deb: I agree that the Clawback Rule is generally overbroad, rigid, and inflexible. Some of the criticism that the Clawback Rule has received relates to Section 10D, which is a very general mandate from Congress that the SEC has no authority to change, and some criticism relates to the way the SEC has applied it, which many view as expanding the scope beyond what Congress intended.

## Overall Critique

While there is nearly universal agreement that executives should repay compensation that never should have been paid in the first place, the SEC took this relatively simple and non-

controversial concept and created an overly prescriptive rule from the legislation.

The general consensus among practitioners is that the Clawback Rule is:

- Confusing.
- Onerous.
- Stringent in nature.

It is important to remember that Dodd-Frank was intended to:

- Respond to the financial crisis of 2008 and prevent similar occurrences.
- Prevent excessive risk-taking.
- Address misconduct by bad actors.

The critical question is, therefore, “Does the Clawback Rule effectively address these concerns?” And I do not think it does, due to both:

- The wording of the mandate set out in Section 10D, which is simultaneously vague and rigid.
- The SEC’s overbroad application of this mandate in the Clawback Rule.

Under Section 10D:

- There is no misconduct required to trigger a clawback obligation. Rather, the clawback can be triggered even for executives that have no:
  - responsibility for the initial, flawed financial statements; and
  - reason to know that their incentive compensation was overstated.
- Boards and compensation committees are generally prohibited from exercising their judgment regarding whether or not to pursue a clawback based on the circumstances before them.

Companies may, therefore, be forced to pursue clawbacks in circumstances where doing so may not be in the best interests of the company and its shareholders.

Additionally, while constrained by the parameters of Section 10D, there are several aspects of the Clawback Rule that:

- Are overly restrictive (by not permitting greater board and securities exchange discretion).
- Illustrate the SEC’s intent to apply Section 10D as broadly as possible (for example, by requiring clawbacks even in the case of “little r” restatements).

## Specific Examples

Individual coverage under the Clawback Rule is quite broad. Rather than limiting recoupment to the chief executive officer (CEO) and chief financial officer (CFO), Section 10D mandates that clawback policies apply to “any current or former executive officer.” The Clawback Rule could therefore potentially impact individuals who are rather far

removed from all decision-making processes.

While it is certainly true that anyone who receives excess compensation as a result of misstated financials should never have received that compensation in the first place, recoupment can be a harsh result, especially for someone who, for example:

- Left the company three years before an accounting restatement was contemplated.
- Was in no way connected to the reason for the accounting restatement.

Additionally, from the company's perspective, it can be onerous to find people who left the company two to three years earlier and hold them accountable for repayment.

While not specifically mandated by Dodd-Frank, the Clawback Rule defines accounting restatement to include both "Big R" and "little r" restatements. In contrast to "Big R" restatements, where errors are material to the previously issued financial statement, rendering it unreliable to investors (and, therefore, the financial statement must be reissued), "little r" restatements involve only immaterial errors that do not cause the financial statement to be misleading to investors at the time it is filed (and, therefore, it must be corrected in current filings but not in past filings).

Despite an absence of any investor harm tied to the historical disclosures, companies are nevertheless required to claw back compensation that was awarded on the basis of those statements. This creates a disconnect between the policy objective of the clawback requirement—ensuring that executives do not retain pay tied to materially misstated results—and the reality that little r restatements reflect technical adjustments that, when reported, do not rise to that level.

The Clawback Rule's definition of incentive-based compensation, a term that is largely undefined in Section 10D other than to indicate that it includes certain stock options awarded as compensation, is also overly broad and somewhat arbitrary, referring to "any compensation that is granted, earned, or vested based wholly or in part upon the attainment of a financial reporting measure." This definition could:

- Potentially pick up compensation that is only peripherally tied to financial metrics.
- Encourage a shift away from awards that emphasize pay-for-performance.

Finally, under the Clawback Rule, clawback recovery is required on a pre-tax (rather than a net) basis, which:

- Unfairly forces executives to return amounts they never actually retained after taxes.
- Could create a disproportionate burden.

Practically, this often means that companies must plan for potentially large gross recovery demands and may need to build in mechanisms to mitigate the tax impact on executives, such as:

- Deferral structures.
- Gross-up adjustments.

The rigid pre-tax requirement is another example of how the Clawback Rule overreaches beyond Dodd-Frank's intent.

What are the most significant negative implications and unintended consequences of the Clawback Rule?

Deb: The Clawback Rule has many adverse and unintended consequences, including that:

- No-fault clawbacks do not drive the intended behavior. Recouping compensation from individuals irrespective of fault may not drive positive (or deter negative) behavior, especially when the accounting restatement triggering the clawback was the result of one bad actor.
- The definition of "accounting restatement" injects uncertainty into compensation practices. By applying the Clawback Rule to circumstances where prior filings remain intact, the SEC has injected uncertainty into compensation practices, exposing executives and companies to recovery obligations in situations where the underlying disclosure was not considered materially misleading.
- The definition of incentive compensation creates negative incentives. By excluding time-based stock options and restricted stock from the definition of incentive-based pay and, therefore, from the clawback requirement, the Clawback Rule could incentivize companies to use time-based, rather than performance-based, awards. Similarly, while it may raise the ire of proxy advisors (creating some guardrails), to mitigate the risk of clawbacks, there is a clear incentive to make discretionary bonus or spot awards that are not tied to the company's financials, rather than performance-based awards. This has the unintended consequence of creating misalignment between executive officer and shareholder interests and runs counter to most companies' compensation philosophies, which emphasize pay-for-performance.
- Boards feel their authority has been diminished. Under the business judgment rule, boards are given broad latitude to guide the company and make appropriate decisions to address poor or irresponsible behavior in ways that are consistent with their fiduciary duties and corporate governance principles. Most boards feel they are better equipped to address erroneous financial reporting and instances of bad behavior than an overly draconian, inflexible rule.
- Compensation committees have unwelcome new responsibilities. Compensation committees are already overextended, and the Clawback Rule adds a host of additional responsibilities, including the need to:
  - assess what compensation is subject to clawback;
  - determine the amount of the clawback;
  - decide how to enforce the clawback policy;
  - educate executives on how the clawback will operate;
  - communicate the potential impact on performance-based awards (notwithstanding situations where there is no executive misfeasance);
  - balance the potential impact of the Clawback Rule with corporate governance concerns (for example, committee members may be faced with decisions that could fly in the face of good corporate governance, such as whether to pull back

on performance-based awards subject to clawback in favor of time-based options and restricted stock, or award more discretionary bonuses not tied to financials that could trigger a restatement); and

- ensure that the company makes proper disclosures about the clawback policy and any actions taken to recover compensation pursuant to the policy.
- Clawbacks are expensive. For companies that are required to recover compensation from executives, the expense is significant. For example, the Clawback Rule's definition of incentive-based compensation may include, in addition to financial accounting measures, stock price and total shareholder return (TSR). To determine how an accounting restatement would have impacted stock price or TSR, companies must make reasonable estimates. Most hire third-party experts to conduct valuations, and the SEC has acknowledged that in the case of stock price and TSR, where it can be difficult to isolate the impact of an accounting restatement, the cost of recovery may be high. While the Clawback Rule contains a narrow 'impracticability' exception for cases where the compensation committee determines that the direct costs paid to a third party to assist in enforcing recovery would exceed the amount to be recovered, the company must thoroughly document its recovery efforts, and any decision to forego recovery will be subject to extensive scrutiny. Additionally, companies:
  - must work with their legal counsel to prepare extensive disclosure regarding the reason for the clawback and how they are implementing the clawback; and
  - may have to go through an arduous process of tracking down former executives.
- Clawbacks raise complicated tax withholding and reporting issues. The tax laws governing clawbacks of compensation are complex and somewhat subject to uncertainty. Additionally, impacted executives may need to have their income taxes redone for the affected period, and the Clawback Rule prohibits companies from indemnifying the executives for this expense.
- Clawbacks are unpopular with executives. Executives view clawbacks as punitive, especially when applied without fault, which can:
  - impede recruiting, especially where executives are considering transitioning from the private to the public sector (the Clawback Rule's prohibition against indemnification of executives may be particularly disconcerting to executives considering roles that are unrelated to financial restatements);
  - hinder retention, because executives are put off by clawback language in employment and award agreements; and
  - encourage executives to re-negotiate their compensation terms (for example, by advocating for higher salaries to make up for the clawback risk).

Can you describe the recoupment process of a company required to recover compensation in compliance with the Clawback Rule?

Deb: In a November 2024 press release, Macy's announced that it had discovered a significant accounting issue during the preparation of its third-quarter financial statements. An independent investigation revealed that a single employee had intentionally made

erroneous accounting accrual entries, concealing approximately \$150 million in delivery expenses from the fourth quarter of 2021 through the third quarter of 2024, which resulted in an understatement of expenses across multiple reporting periods.

In compliance with the Clawback Rule, Macy's adopted a compensation clawback policy effective October 2, 2023, which was disclosed to investors in an exhibit to its Form 10-K filed in March 2024. Subsequently, in its annual proxy statement filed in April 2025, Macy's disclosed that it sought to recover from certain executives approximately \$600,000 in incentive-based compensation awarded under the company's 2021 to 2023 performance restricted stock unit plan where amounts paid had been inflated due to the accounting misstatement.

To accurately determine this erroneously awarded compensation amount, Macy's engaged a third-party financial advisory firm. The executives' compensation during the affected period was based, in part, on performance metrics such as EBITDA and sales as well as shareholder returns over a multi-year period. The advisory firm calculated a hypothetical "but-for" stock price, estimating what the stock price would have been absent the misstatement, and used this to estimate the differential in incentive payouts to claw back. Macy's described the amount as a "reasonable estimate of the effect of the accounting restatement" on executive compensation, consistent with the requirements of the Clawback Rule.

While the aggregate cost of the recovery efforts was not disclosed, the process of recovering \$600,000 from various executives (due to the actions of one person) likely cost Macy's well over the \$600,000 that it sought to recover.

The outcome in this case illustrates the problem with the Clawback Rule's breadth. The triggering misconduct was attributable to a single employee, yet the clawback obligation had a harsh result for multiple executives who had no involvement in, or knowledge of, the underlying misstatement. Moreover, the process of engaging valuation experts and preparing detailed disclosures almost certainly exceeded the \$600,000 recovery amount, underscoring the inefficiency of a framework that prioritizes rigid compliance over practical governance. This example captures the heart of the criticism that the SEC has gone well beyond Dodd-Frank's intent in that the Clawback Rule:

- Imposes costly, mechanical recovery obligations in situations where investor harm is minimal.
- Curtails board discretion.
- Requires executives to bear consequences that have no relationship to their culpability.

What changes to the Clawback Rule would you like to see?

Deb: There is widespread consensus that the Clawback Rule in its current form is overly prescriptive and complex and requires companies to go well beyond Dodd-Frank's mandate. Putting this into context, consider that:

- Most public companies have adopted:
  - strong corporate governance frameworks; and
  - tailored clawback policies.
- Boards and compensation committees have substantial expertise in determining what may be in the best interests of their company and its shareholders.

Given those considerations, and the potential unintended consequences of the current Clawback Rule, I believe a better approach would be to:

- Limit the application of the Clawback Rule to Big R restatements.
- Revisit a materiality threshold for recovery amounts.
- Allow for after-tax rather than pre-tax recovery.
- Expand the impracticability exception.
- Allow the board or compensation committee significant discretion in adopting a clawback policy that:
  - is tailored to the company's circumstances, including its business strategies and the unique features of its executive compensation programs; and
  - aligns with the company's corporate governance principles.
- Promote transparency by requiring detailed disclosure about the exercise of this discretion.

Do you expect the SEC to make changes to the Clawback Rule based on the feedback it has received?

Deb: It is certainly possible that the SEC will amend the Clawback Rule at some point, but it currently has more immediate disclosure storms to weather. While the sentiment at the Roundtable was that the Clawback Rule is overly complicated and does not provide helpful information to investors, the SEC staff's highest priorities are likely:

- Simplifying the pay-versus-performance rule.
- Scaling back requisite disclosure requirements to protect executive safety.

While clawbacks were a hot topic at the Roundtable, they do not seem to be causing imminent pain to investors or filers. That said, this may change as more clawbacks are triggered over time and companies struggle to implement the Clawback Rule.

We may also see changes if there is a complete overhaul of the executive compensation disclosure rules generally. Many remarks were made at the Roundtable and in subsequent comments about the length, detail, and breadth of Item 402 of Regulation S-K and the comparatively small benefit to investors in making decisions. If there is a drastic cutback to the rules overall, it is possible that the SEC will examine the nuances of the Clawback Rule and scale back certain requirements. For example, to address criticisms that the rule

requires recoupment of amounts that are immaterial to investors, the SEC could add a minimum threshold that must be met before the clawback obligation is triggered. But I would not bank on that today.

At this juncture, we understand that any changes made to the Clawback Rule will not become effective until 2026 proxies are filed (at the earliest), so for now, companies must stay the course and adhere to current compliance requirements.

Many companies already had longstanding clawback policies in place before Dodd-Frank or voluntarily implemented clawback policies while waiting for the SEC to finalize the Clawback Rule. What features did those policies have, and how did companies handle them once the SEC issued the Clawback Rule?

Deb: Pre-Dodd-Frank, in practice most clawbacks were found in equity plans and award agreements, and they generally applied only to unvested equity. While all participants in those programs were potentially subject to clawbacks, they were usually triggered by a narrow set of circumstances that involved either:

- Bad behavior (often called "bad boy" clauses).
- Breach of a restrictive covenant (such as a non-solicit or non-compete).

From time to time we would also see clawbacks in an employment contract, but it was rare. Even in those cases, it typically only applied to equity, not performance-based cash awards.

When the Clawback Rule was released, companies that had broader clawback policies in place (such as those that allowed discretionary clawbacks or clawbacks for compensation that was not incentive-based under Dodd-Frank) performed side-by-side comparisons of what they had versus what the rule required. One of the unintended consequences of the Clawback Rule was that initially, in most cases, companies abandoned their broader policies in favor of narrower policies that conformed to Dodd-Frank requirements. This changed over time, however, as proxy advisors and others began penalizing companies with clawback policies that merely adhered to the Dodd-Frank standard.

Today, most of our larger public clients and some of our smaller clients (and even some private clients that wish to track good public company governance practices) maintain two clawback policies:

- A Dodd-Frank boilerplate policy (that allows no discretion).
- A supplemental policy that gives either the board or compensation committee broad discretion in recouping compensation. There is significant variation among these supplemental policies regarding:
  - the specific populations to which they apply (for example, the CEO and CFO versus other executives);

- the different types of compensation covered (for example, time-vested versus performance-based equity); and
- the clawback triggers (for example, an accounting restatement, misconduct, or a violation of a restrictive covenant).

## Have the views of proxy advisors and institutional investors influenced clawback policy design?

Deb: In 2024, Institutional Shareholder Services (ISS) clarified in its FAQs on executive compensation policies that, for purposes of ISS's say-on-pay vote recommendation, clawback policies must explicitly cover all time-vesting equity awards to receive credit as a robust clawback policy. This is consistent with the view ISS has already taken for purposes of analyzing equity-based incentive program proposals under its Equity Plan Scorecard (EPSC) policy, but inconsistent with Dodd-Frank, which covers only performance-based awards.

Under ISS's FAQs on equity compensation plans, to receive EPSC points for the clawback policy factor, an issuer's clawback policy must:

- Authorize recovery upon a financial restatement.
- Cover all or most equity-based compensation for all named executive officers (NEOs), including both time- and performance-vesting equity awards.

Glass Lewis's view on clawback policies, as set out in its 2025 Benchmark Policy Guidelines, is that effective clawback policies should provide companies with the authority to recoup incentive compensation (whether time-based or performance-based) in the event of a restatement of financial results or similar revision of performance indicators on which the awards were based. Additionally, Glass Lewis states that recovery should be available when there is evidence of problematic decisions or actions, such as material misconduct, a material reputational failure, a material risk management failure, or a material operational failure, the consequences of which have not already been reflected in incentive payments and where recovery is warranted. Glass Lewis expects that this authority to recoup will be provided regardless of whether the executive officer's employment was terminated with or without cause.

Some large institutional investors also address clawbacks in their voting policies. BlackRock states in its 2025 Benchmark Policies for US Securities that it favors prompt recovery from any senior executive whose compensation was based on faulty financial reporting or deceptive business practices. This includes Dodd-Frank-compliant policies and broader policies requiring recovery from (or the forgoing of) the grant of any awards by any senior executive whose behavior caused material financial harm to shareholders, caused material reputational risk to the company, or resulted in a criminal investigation, even if these actions did not ultimately result in a material restatement of past results. BlackRock generally supports shareholder proposals on these matters unless the company already

has a robust clawback policy that sufficiently addresses BlackRock's concerns.

To avoid negative vote recommendations, companies designing clawback policies should consider shareholder advisory firm and institutional investor guidelines. Companies should also clearly communicate the rationale for their clawback policies in their proxy statements to address shareholder concerns and secure support during say-on-pay votes.

Based on your latest review of S&P 500 proxy statements, what types of clawback policies do companies currently maintain?

Deb: Based on our review of proxy statements filed in 2024, in addition to the required Dodd-Frank-compliant policy, roughly 67% of filers disclosed a supplemental clawback policy. (Note that companies may have other clawback procedures in place that were not required to be publicly disclosed.)

In examining the combined clawback policies maintained by S&P 500 companies, we observed that:

- 100% of companies specifically covered NEOs (as required by Dodd-Frank).
- 57% of companies specifically covered Section 16 officers.
- 23% of companies specifically covered other individuals (either non-executives or employees generally).

The most common triggers of combined policies (other than the required accounting restatement) included:

- Fraud or misconduct (65%).
- A violation of company policy or a code of conduct (50%).
- Reputational or financial harm to the company (50%).
- A violation of a restrictive covenant (14%).
- Termination for cause (12%).
- Criminal conduct (12%).
- A breach of fiduciary duty (6%).
- General inappropriate conduct (5%).

(The above data is from [Main Data Group](#), a data and analytic platform for executive compensation and corporate governance.)

What are the key considerations for companies when designing a clawback policy?

Deb: There are several issues that a company designing a clawback policy should consider, including:

- Whether the company should adopt both a Dodd-Frank-compliant policy and a supplemental policy.

- Who should administer the clawback policy.
- How the company will document that covered executives received the policy.
- What the impracticability standard should be and how the company will document any decision not to pursue recovery.

## Adopting Both a Dodd-Frank Policy and a Supplemental Clawback Policy

Deb: Because Dodd-Frank clawback recovery is mandatory, a company that wants discretion to seek recoupment in other circumstances must introduce a separate, supplemental policy.

Some companies have tried to tweak their Dodd-Frank policy to expand it into a discretionary policy, but we advise against this. To ensure compliance with the Clawback Rule, the Dodd-Frank policy should be pure boilerplate.

Most large companies that focus on best governance practices have both a Dodd-Frank policy and a supplemental policy, and best practice is to keep them separate and distinct.

When designing a supplemental policy, the company must consider:

- What the clawback triggers will be.
- Who will be covered by the policy.
- What types of compensation will be covered by the policy.
- What the look-back period should be.
- Who will decide how to enforce the policy.

Most of the supplemental policies we see today:

- May be triggered by:
  - misconduct;
  - a violation of company policy;
  - reputational harm;
  - a breach of restrictive covenants; or
  - government actions (if penalties are required due to executive actions).
- Apply to:
  - a broader spectrum of individuals (for example, individuals involved in risk-taking roles); or
  - current, but not former, executives.
- Reach a broader range of compensation, such as:
  - time-vesting equity;
  - discretionary cash payments;
  - deferred compensation; and
  - retention bonuses.
- Include a flexible look-back period (most often fewer than three years since the administration of a longer look-back period is complex, but some policies have extended the period to five years and beyond).

- Provide the board with significant discretion in determining whether the policy applies and, if so, whether a clawback is warranted given all of the facts and circumstances.

If the company decides to maintain both a Dodd-Frank policy and a supplemental policy, it is important to make sure that the two policies can run in tandem and do not conflict or overlap. For example, if the Dodd-Frank policy provides for a look-back of three years and applies to incentive compensation as defined by the SEC, but the supplemental policy has an unlimited look-back and also applies to incentive compensation, it can be unclear which policy governs. We generally recommend that each policy contain a conflicts clause, which clarifies that in the event of ambiguity, the Dodd-Frank policy will govern unless the supplemental policy is more onerous.

## Administering the Clawback Policies

While ultimately the board is responsible for ensuring compliance with Dodd-Frank, most companies designate the compensation committee as the administrator of the policies. This is because the compensation committee:

- Oversees executive compensation design and implementation and, therefore, has the subject-matter expertise to determine how recovery should be calculated and enforced.
- Is a body composed of independent directors who can provide the objectivity needed to:
  - assess potential triggers, such as misconduct or accounting restatements; and
  - make recovery decisions without management conflicts.
- Has a fiduciary responsibility to protect shareholder interests and ensure consistency across compensation arrangements. Therefore, administering clawback policies generally falls under its oversight.
- Is expected (by investors, proxy advisors, and regulators) to take full ownership of pay practices, including enforcement mechanisms like clawbacks, thereby reinforcing both credibility and accountability in governance.

## Documenting Covered Executives' Receipt of the Clawback Policy

The company should draft a stand-alone acknowledgment form that all covered executives must sign after being provided with a copy of the clawback policy (or policies). The acknowledgement form both:

- Evidences the executives' receipt and understanding of the policy.
- Bolsters the enforceability of the policy under state contract law.

Executives should acknowledge that they:

- Have received a copy of the clawback policy, read it, and understand that they are bound by all of the terms of the policy.

- Understand that if there is an inconsistency between the clawback policy and the terms of their employment agreement or any other compensation program or arrangement, the clawback policy will govern.
- Understand that if the company determines that any incentive compensation (and any other covered compensation) received must be forfeited, recovered, or repaid, they must take whatever action is necessary to effectuate the forfeiture, repayment, or recovery.
- Will cooperate with the company in effectuating any recovery and waive any claims or defenses that would conflict with the company's rights.
- Are not entitled to indemnification in connection with the company's enforcement of the clawback policy.

## Determining the Impracticability Standard and Documenting When Not to Pursue Recovery

The clawback policy should set out the standard for impracticability and require specific board-level documentation in connection with any decision not to pursue recovery due to impracticality. For example, the policy should:

- Clarify the circumstances under which enforcement costs will be considered excessive (such as when the company can demonstrate that the expense of enforcement will far exceed the amount of compensation to be recovered). Recovery would not be required where, for example:
  - the estimated legal fees and collection costs are expected to exceed 200% of the amount subject to recovery (a ratio test); or
  - the recoverable amount is below a *de minimis* threshold (for example, \$10,000) (a bright-line *de minimis* floor).
- Identify the types of legal impediments that would make recovery impracticable. This could include situations where, for example:
  - recovery would violate an executive's home country law;
  - recovery would violate tax-qualified retirement plan rules or other statutory benefit protections; or
  - the executive is deemed judgment-proof due to insolvency.

The company should also ensure that all ancillary documents (such as employment agreements, change-in-control plans and agreements, and equity plans and agreements) cross reference all clawback policies and specifically incorporate them by reference.

Where inconsistencies exist, companies should consider either:

- Amending those agreements.
- Obtaining employee acknowledgements.
- Implementing interpretive provisions to ensure that the clawback policy governs.

These proactive steps reduce the risk of disputes over enforceability and demonstrate the company's commitment to robust recovery mechanisms. Most importantly, the company should adopt clawback policies that collectively:

- Comply with the Clawback Rule.
- Are appropriate for their company's circumstances and consistent with their corporate governance principles.

## Are private companies adopting clawback policies?

Deb: Yes. A growing number of private companies are adopting clawback policies, particularly if an initial public offering (IPO) is or could be on the horizon. These policies do not, however, track the formulaic Dodd-Frank standards. Instead, since private companies are not subject to Dodd-Frank, they generally establish policies that grant broad discretion to the board to enforce recovery in situations where the board determines that doing so would:

- Be in the company's best interests.
- Deter bad behavior.

## What processes should companies establish to ensure that they are prepared in the event of an accounting restatement that triggers a clawback?

Deb: To ensure they are prepared in the event a clawback is triggered, and to mitigate the risk of non-compliance with the Clawback Rule, companies should establish formal processes for executing clawbacks. For example, companies should:

- Adopt written clawback policies. Companies should implement a Dodd-Frank-compliant clawback policy and a thoughtfully considered supplemental policy that gives discretion to the board or compensation committee, is tailored to the company's circumstances, and reflects its corporate governance principles. Companies must obtain board or compensation committee approval of the policies.
- Harmonize contract and exit procedures. Companies should audit all existing contracts, equity plans, bonus plans, and change in control agreements to confirm that these reference and incorporate the clawback policy. Where necessary, companies should:
  - amend older agreements to prevent conflicts;
  - formalize protocols to address clawbacks in separation agreements and exit interviews, including obtaining updated contact details and reaffirming continuing obligations; and
  - verify that directors and officers liability insurance exclusions and company indemnification policies are consistent with clawback requirements and do not create conflicting obligations.
- Educate board members and covered executives about the Dodd-Frank policy and any supplemental policy. This education should include explaining:
  - the mandatory nature of the Dodd-Frank policy and how the policy works;

- the details of any supplemental policy; and
- how the two interact.
- Assign a team responsible for overseeing the recovery process. Companies should also assign an individual or department—often a compensation committee member or the human resources (HR) department—to have primary responsibility for coordinating people, workflows, and deadlines. The oversight team should comprise a broad cross section of individuals, including:
  - the CFO;
  - members of the HR department, the compensation committee, the audit committee, the legal department, the finance team, and the communications team; and
  - outside advisors (which typically includes a compensation consultant).
- Clearly delineate responsibilities. It is essential to coordinate across departments (legal, finance, HR, and internal audit), and companies should ensure that:
  - each team has access to all necessary data in a timely manner;
  - team members have a clear understanding of their roles, workflows, and applicable deadlines; and
  - each team has a checklist that sets out each item they are responsible for and applicable timelines.
- Track executive officers. Companies should maintain a list of current executive officers and identify individuals who were executive officers for each impacted award within the three-year (or other applicable) look-back period. Companies should also establish processes for locating former executive officers, including addressing potential clawbacks and related practical considerations during exit interviews.
- Maintain records. Companies should maintain detailed, accurate records of incentive-based compensation received (granted, earned, vested, and paid) by each covered executive based on financial reporting measures in the three-year look-back period. This typically includes performance-based equity, bonus plans with financial key performance indicators, and stock-price or TSR metrics. The recordkeeper should always have updated information on hand to avoid eleventh-hour searches.
- Integrate systems. Companies should ensure that HRIS (Human Resources Information System), payroll, and equity administration platforms can flag and track compensation subject to clawback (for example, by award type, performance metric, or vesting date).
- Establish clear channels for internal communication in the event that a clawback is triggered. Companies must provide communications teams with the information needed to clearly explain to affected individuals:
  - the reason for the clawback;
  - the amount of the clawback; and
  - what the recovery process will entail.
- Establish disclosure and shareholder communication procedures. Companies should create procedures for accurately disclosing clawback information in Form 8-K filings, proxy statements, and Form 10-K filings.
- Regularly review and update all clawback policies. Specifically, companies should:
  - confirm that all clawback policies work separately from each other and serve their intended purposes (for example, the Dodd-Frank policy complies with the

- review the supplemental policy every year to ensure that it reflects best corporate governance practices, which are fluid;
  - closely monitor regulatory guidance, including potential changes to the Clawback Rule in response to feedback from the Roundtable and submitted comments; and
  - incorporate clawback education into the onboarding process and provide ongoing training to all relevant staff.
- Implement integration and downstream enforcement. Companies should integrate these processes with other company policies and procedures (for example, financial reporting procedures and proxy statement review). This includes:
    - establishing clear procedures for repayment, including timing (for example, lump sum or installments) and method (for example, cash repayment, share return, share cancellation, or netting against future awards), identifying tax impact and reporting obligations, coordinating with the payroll department, and adjusting payroll records; and
    - creating a formal escalation path for disagreements with executives over amounts owed, including mediation or arbitration provisions, to minimize litigation risk.
  - Conduct testing. Test these processes by running hypothetical accounting restatement scenarios.

## Example 1: Cash Bonus (EBITDA-based award).

Assume the executive has a \$1 million target bonus tied to EBITDA performance. Payout equals 100% of target if EBITDA  $\geq$  \$500 million (with \$500 million also being threshold, below which there is \$0 payout); 150% of target if EBITDA  $\geq$  \$550 million; with straight-line interpolation in between. The EBITDA reported results (pre-restatement) are \$540 million, resulting in a payout of 140% of target (\$1.4 million).

Restated results (post-clawback) result in EBITDA corrected to \$495 million - below the \$500 million threshold – so the correct payout = 0. The clawback obligation is the full \$1.4 million. If restated EBITDA were \$510 million, the correct payout would be \$1.1 million. The overpayment, and thus the clawback amount, would be \$300,000.

## Example 2: Stock Price/TSR-Based Equity Award.

Assume that the executive received a performance stock unit (PSU) award with a target value of \$1 million. Under the equity plan, a 50% stock price increase results in a 150% payout, a flat stock price yields a 100% payout, and a 20% decline results in no payout.

In one scenario, the company reported a 40% increase, which produced a payout of 140% of target (or \$1.4 million). After an accounting restatement, however, the "but for" increase was determined to be only 20%, meaning that the correct payout should have been 120% of target (or \$1.2 million), requiring a \$200,000 clawback.

In another scenario, the company reported a 60% increase and paid \$1.5 million, but following an accounting restatement, the "but-for" increase was only 10%, which equated to 110% of target (or \$1.1 million), triggering a \$400,000 clawback.

These simplified numbers illustrate how quickly clawback obligations can add up when stock performance is adjusted after a restatement.

- Establish protocols to address anticipated challenges. There will undoubtedly be challenges related to recovery. Companies must anticipate these challenges and establish protocols for addressing issues such as:
  - locating former executives;
  - reconciling inconsistencies between pre-existing binding contracts (such as employment and equity agreements) and the clawback policy;
  - managing ongoing disputes with executives;
  - addressing state law limitations; and
  - enforcing recovery where policies may not have been in place at the time of grant.

## What framework should public companies follow when developing a clawback policy?

Deb: In practice, the most effective approach for public companies has been to maintain a boilerplate Dodd-Frank-compliant policy alongside a more rigorous supplemental policy that allows judgment and discretion. This dual framework ensures compliance with SEC rules and permits boards to respond to circumstances in a way that aligns with sound governance principles and shareholder interests.

Although the SEC has signaled possible refinements to the Clawback Rule (while remaining compliant with Dodd-Frank mandates), nothing is likely to change before the 2026 proxy season. Until then, companies that balance strict compliance with thoughtful supplemental measures will be best positioned to manage both regulatory demands and the broader challenges of executive compensation oversight.

## About the Author

Deb advises on executive compensation from a legal and regulatory perspective, including securities disclosure, tax and governance matters, contract negotiation, and reasonableness opinion letters.

## About Pearl Meyer

Pearl Meyer is the leading advisor to boards and senior management helping organizations build, develop, and reward great leadership teams that drive long-term success. Our strategy-driven compensation and leadership consulting services act as powerful catalysts for value creation and competitive advantage by addressing the critical links between people and outcomes. Our clients stand at the forefront of their industries and range from emerging high-growth, not-for-profit, and private organizations to the Fortune 500.