



# New SEC Rule Highlights Need to Understand Tax Implications of Clawbacks

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In late October, the Securities and Exchange Commission approved a rule to require public companies to recover - or "claw back" - certain executive bonus pay later determined to have been awarded based on materially misstated financial information, regardless of whether the recipient was at fault. Previously proposed versions of the rule had called for clawbacks in cases of major accounting errors that caused restatements of previous annual financial results; the newly finalized version also covers smaller mistakes that can be corrected in current year reporting.

According to the *Wall Street Journal*, "SEC economists estimate the lesser category of accounting errors covered by the final rule are about three times as common as the more serious type." Many companies have voluntarily included clawback provisions in their executive compensation agreements for years, although enforcement can prove to be complex. Companies will now be required to file their clawback policies as an exhibit to their annual reports.

Ivins, Phillips & Barker has years of experience in examining the tax treatment of compensation clawbacks and the tax questions raised by the many special cases likely to arise. These include:

- compensation setoffs, or holdbacks, and their issues under sections 61 and 409A;
- the tax treatment of repaying employer stock under section 83;
- the special issues under section 162 or 165 and section 1341 raised by retroactive clawbacks imposed on amounts paid before the clawback policy was in place;
- "bad boy" clawbacks and clawbacks from former employees; and



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- the employment tax and information reporting issues of clawbacks.

IPB partner Kevin O'Brien co-authored the seminal chapter on clawbacks in the New York University Review of Employee Benefits and Executive Compensation and subsequently wrote about the key issues for *Tax Notes* in "Taxing Clawbacks: Theory and Practice."