CtW Investment Group

October 16, 2017

Honorable Jay Clayton
Chairman
U.S. Securities and Exchange Commission
110 F St. NE
Washington DC, 20549

Re: Human Capital Management Disclosures Rulemaking Petition

Dear Chairman Clayton,

We write on behalf of the pension funds sponsored by the unions affiliated with Change to Win, which provide retirement security to over three million workers and which invest over $250 billion globally. These pension funds have periodically suffered substantial losses as a result corrupt corporate practices, excessive risk taking, and inadequate investor accountability. In order to protect our members' retirement savings, the CtW Investment Group works with these funds to help them detect improper and aggressive accounting, recognize unwise mergers and acquisitions, and insist on corporate governance practices that enable investors to accurately assess the risks and opportunities presented by the companies offering securities in the capital markets.

Over the past decade and a half corporate governance practices in the US markets have improved as a result of both private activism by investors and changes in public policy, including changes in disclosure requirements mandated by federal statute and regulation. These changes have made shareholder votes meaningful, improved board accountability, and increased the range of critical information available to shareholders looking to formulate a clear understanding of the future prospects of firms and industries free from the self-serving spin of conflicted intermediaries. We believe that the recently submitted rulemaking petition on human capital management is the critical next step in this process of improving corporate governance, and that if implemented such disclosure would greatly improve the ability of investors to identify well-managed companies, while creating appropriate, market-conforming incentives consistent with increased productivity and sustainable, long-term shareholder returns.

As you no doubt know, and despite the healthy recovery of share prices since 2009, the annual rate of productivity growth has declined sharply after the decade-long rise from 1994-2004. These very low rates of productivity growth limit future shareholder returns: while share prices may temporarily rise due to changing risk preferences, and while firms may increase the share of revenue returned to securities holders, neither of these alternative sources of shareholder value is sustainable for the long time horizons over which pension funds must invest.[1] Moreover, multiple large-scale, highly detailed economic research projects have demonstrated that both productivity levels and rates of productivity growth vary enormously by workplace – even establishments operating in the same industry and under the ultimate control of the same corporate parent exhibit large productivity differences.[2] The

[1] Daniel L. Greenwald, Martin Lettau, & Sydney C. Ludvigson, "Origins of Stock Market Fluctuations" June 2014.
[2] Nicholas Bloom, Erik Brynjolfsson, Lucia Foster, Ron Jarmin, Megha Patnaik, Itay Saporta-Eksten, & John Van Reenen, "What Drives Differences in Management?" June 2016.; Barth E, Bryson A, Davis JC, Freeman RB. It's

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economists conducting and reporting on this research uniformly point to workplace-specific managerial efforts to increase morale and engage employees as the critical driving force behind these variations in productivity. Consequently, effective human capital management has the potential to play a large role in reversing the productivity slump and establishing a sound basis for sustainable increases in shareholder value.

Other research strongly supports this conclusion:

- Gallup reports that in 2016 only 33% of US workers were engaged at work, compared to 70% for leading global firms. Gallup notes that disengaged workers "are more likely to steal from their company, negatively influence their coworkers, miss workdays and drive customers away."
- Gallup estimates that actively disengaged employees cost the U.S. between $483 billion to $605 billion each year in lost productivity, equal to between 2.6% and 3.25% of GDP.
- Experts on operations management report that in many US industries, including long-distance trucking, retail stores, and fast-food restaurants, employers typically understaff and undertrain their workforce, resulting in high levels of stress, burnout, and turnover, while nevertheless leaving the company unable to respond flexibly to fluctuations in demand.
- Conversely, this same literature has found that companies in these industries that staff adequately, pay reasonable salaries, train workers in multiple tasks, and empower staff to flexibly shift between job tasks in response to customer needs, enjoy superior growth, productivity, and profitability.[3]
- The RAND Corporation's 2015 report *Working Conditions in the United States* found that one in three workers has no control over their schedule, that one in five workers must manage frequent changes in their work schedule with minimal notice, one half report unpleasant or hazardous working conditions, and nearly one in five workers report facing a hostile work environment, including unwanted sexual attention and verbal abuse.

When companies fail to establish sound practices for human capital management, the result can be even more dire for investors than stagnant sales or earnings:: as the recent examples of Uber, 21st Century Fox, and Wells Fargo demonstrate, poor management of the workplace can quite suddenly result in significant regulatory and litigation costs, as well as potentially long-term reputational damage.

Unfortunately, current law and regulation provide only scant disclosure of a company's strategy and approach to managing and investing in its human capital. It is impossible for readers of the financial statements of publicly traded US companies to determine, for instance, which company in an industry has the lowest turnover, the highest absenteeism, the most effective training programs, or a more successful approach to scheduling than its competitors. The absence of required reporting on human

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"Where You Work: Increases in the Dispersion of Earnings across Establishments and Individuals in the United States." *Journal of Labor Economics*, 2016;34 (S2) :S67-S97; Peter Orszag, "People are not unequal, companies are" *Bloomberg View*, October 16, 2015.

[3] Zeynep Ton, *The Good Jobs Strategy* (New Harvest, 2014).

capital management may even be having more significant negative effects: a study published in *The Journal of Accounting and Economics* found that rates of workplace injury are 5%-15% higher among companies that just meet or beat analyst estimates for their quarterly earnings, suggesting that the understandable focus of many shareholders on the information they have access to induces company managers to misallocate resources in a manner that is harmful both to workers and to the kind of long-term productivity growth that ultimately underpins shareholder value.

In our view, it is no longer credible to argue, as some commentators have in the past, that workplace conditions and employee engagement are not appropriate or relevant topics for disclosure in a publicly-traded company's reports to investors. Both the risks posed by poorly managed workplaces and the opportunities presented by introducing more effective human capital management practices are too large for shareholders to ignore. But, in order for investors to incorporate these elements of company strategy into their analysis, they need to have access to the relevant information in a reasonably comprehensive, uniform, and timely manner. We believe that the human capital management rulemaking petition provides a modest, thoughtful, and appropriate entry point for the Commission to recognize the importance of human capital management for investors, and to ensure that investors have access to the information they need in order to properly assess this element of corporate strategy. We urge you and the Commission to take up this rule making process expeditiously.

Sincerely,

Dieter Waizenegger
Executive Director, CtW Investment Group