215 Pennsylvania Avenue, SE • Washington, D.C. 20003 • 202/546-4996 • www.citizen.org

October 22, 2019

Jay Clayton
Chair
Robert Jackson, Hester Peirce, Elad Roisman, Allison Lee
Commissioners
Securities and Exchange Commission
100 F St. NE
Washington, D.C.
20549

Re: Modernization of Regulation S–K Items 101, 103, and 105

File Number S7– 11–19

Dear officers,

On behalf of more than 500,000 members and supporters of Public Citizen, we offer the following comments on the proposed rule described by the Securities and Exchange Commission (SEC) as "Modernization of Regulation S-K, items 101, 103, and 105." In brief, we are disappointed that the SEC has failed to acknowledge and incorporate the many ideas submitted by a plethora of investors to improve disclosures regarding environmental, social and governance (ESG) issues.

Background

Regulation S–K was adopted in 1977. The SEC explained that its effort would foster uniform and integrated disclosure for registration statements under both the Securities Act and the Exchange Act, and other Exchange Act filings. This document rules subsequently approved requires both financial and non-financial filings. A financial filing describes, in quantitative terms, the business results by quarter and by year, as well as the balance sheet describing the basic value of the firm, including assets, liabilities, and net worth. A non-financial filing describes in qualitative terms the nature of the business, various transactions.[1]

Much has changed in the business world in the last four decades since S-K was formulated. For example, the internet emerged, revolutionizing not only the conduct of prevailing businesses, but creating new industries. The most valuable companies as measured by market capitalization today are not car

[1] The SEC uses the letter "S" to describe foundational securities filings. The SEC uses the letter "K" to show that the filing is required annually. (It uses the letter "Q" to denote a quarterly requirement.)

manufacturers or beverage-makers, but internet search engines (Google), photograph-sharing services (Facebook), and computer software developers (Microsoft). Where an investor previously focused on hard assets such as new factories, investors in computer and internet-based companies must pay closer attention to the human capital of a firm.

In another example of major change, environmental concerns have become the greatest danger to the planet. Global warming not only threatens to transform weather patterns, increase the frequency and intensity of hurricanes, foster the proliferation of insects, raise ocean levels that may invade the majority of major cities located on coastlines and much more, it also threatens business. Real estate values will change. Loss of forests to insects will affect timber companies. An investor must know much more about how a firm plans to address and adapt to these myriad changes.

And in a final example, corporate political spending has also grown in the last four decades. With problematic Supreme Court decisions such as the 1976 *Buckley v. Valeo* and then the 2010 *Citizens United v. FEC* which stripped spending restrictions, corporations now shape policy with unbridled secret spending. On Wall Street, for example, this spending helped terminate important safeguards that led to the financial crash of 2008. Even as the wreckage piled up, Wall Street's influence in Washington prevented needed sweeping reforms, and since passage of the modest 2010 Wall Street Reform and Consumer Protection Act, this money has insidiously worked to dilute the already weak tea of new rules. Investors in financial institutions, who saw their share values nearly erased from Wall Street's self-destruction, need to know better if their investment monies are being spent wisely.[2]

The proposed changes to the S-K form fail to recognize these four decades of change.

Equally troubling, these proposed rules fail to recognize the SEC's primary mandate, namely to protect investors and to protect them from manipulative corporate issuers of securities. As the SEC explains, the two mandates of the Securities Act of 1933 are "to require that investors receive financial and other significant information concerning securities being offered for public sale," and to "prohibit deceit, misrepresentations, and other fraud in the sale of securities."[3]

Bright Lines v. Principals

This failure is evident in the SEC's description of its basic approach to the changes it now proposes. Investors uniformly sought improved disclosure with prescriptive, bright line, quantitative results. These investors include the Council of Institutional Investors; the New York State Comptroller; the New York City Comptroller; the California Public Employees' Retirement System; the California State Teachers' Retirement System; the Pension Investment Association of Canada; the Medical Benefits Trust; Walden Asset Management; Domini Social Investments LLC; the AFL–CIO; the British Columbia Investment Management Corporation; the American Federation of State, County and Municipal Employees; and others. It also included the SEC's own Investor Advisory Committee. [4]

---

[2] Bartlett Naylor, *Wall Street Spending will make America Crater, not Greater*, PUBLIC CITIZEN (May 22, 2018) https://www.citizen.org/news/deregulating-wall-street-will-make-america-crater-not-greater/

[3] *The Laws that Govern the Securities Industry*, SECURITIES AND EXCHANGE COMMISSION (website visited Sept. 23, 2019) https://www.sec.gov/answers/about-lawsshtml.html

[4] *Modernization of Regulations S-K,* Securities and Exchange Commission, FEDERAL REGISTER (August 23, 2019) https://www.govinfo.gov/content/pkg/FR-2019-08-23/pdf/2019-17410.pdf

The only groups to oppose these improved prescriptive, bright line, quantitative results were corporate issuers. This included: the American Bankers Association; the U.S. Chamber of Commerce; the National Association of Manufacturers; the American Petroleum Institute; UnitedHealth Group; the Securities Industry and Financial Markets Association; PNC Financial Services Group; and other corporations and trade associations.[5]

Betraying its mandate to protect investors, the SEC sided with corporations and opted against prescriptive disclosure results.

Examining the Proposal

The SEC proposes amendments to three items of Reg S-K. These are Items 101, 103 and 105.

Item 101 requires the firm to describe its business, including industry segments, and a discussion of how it intends to do business in future, including how it will compete. This includes one item requiring the firm to disclose the number of employees of the firm.

Item 103 requires disclosure of any material pending legal proceedings[6] to which the registrant or any of its subsidiaries is a party or of which any of their property is the subject. This includes "environmental actions" and any (other) proceedings known to be under contemplation by governmental authorities. This section must include a description of the factual basis alleged to underlie the proceedings and the court action(s) sought.

Item 105 requires disclosure of the most significant risk factors and specifies that the discussion of the risk factors should be concise and organized logically. The highest risk factor is listed first, the second most serious factor is listed second, and so on.

Human Capital

The SEC's neglect of metrics much-sought by investors is conspicuous on the issue of human capital. The SEC takes this up as it addresses Item 101. To date, the SEC only requires two disclosures regarding its employees: their number, and the median pay. The former has been required since the beginning of the S-K form; the latter came in 2018 to fulfill a requirement under Section 953(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act. There has never been a requirement to enumerate how much is expended on wages; this figure is part of a larger categories, such as sales and general administrative expense.

The SEC received voluminous comment from investors asking for greater disclosure regarding human capital. These institutional investors sought information on worker recruitment, employment practices, and hiring practices; employee benefits and grievance mechanisms; Employee engagement, or investment in employee training; workplace health and safety; strategies and goals related to human capital management and legal or regulatory proceedings related to employee management; whether employees are covered by collective bargaining agreements; and employee compensation or incentive structures.

---

[5] *Modernization of Regulations S-K,* Securities and Exchange Commission, FEDERAL REGISTER (August 23, 2019) https://www.govinfo.gov/content/pkg/FR-2019-08-23/pdf/2019-17410.pdf

[6] This does not include ordinary routine litigation incidental to the business, such as lawsuits against an insurance company's customers.

In addition to these comments, the SEC received a petition signed by the Human Capital Management Coalition.[7] This coalition is composed of more than 20 institutional investors, such as CalPERS, the New York pension funds, and numerous labor union funds.[8] This report marshals dozens of studies demonstrating the material impact of various employment practices.

The SEC has also received public petitions and comments calling for more disclosure of other critical indicators of well- managed companies. These requests include calls for corporations to disclose gender pay ratios on an annual basis; human rights policies, practices, and impacts; and tax practices.[9] These calls for increased disclosure culminated in a rulemaking petition from investors with more than $5 trillion in assets under management asking the SEC to require comprehensive ESG risk disclosure. [10]

Instead of embracing this fact-based petition, the SEC actually proposes to delete a current requirement. No longer will the SEC require firms to enumerate the number of their employees. Regarding human capital, the SEC only invites firms to discuss the issue broadly. Specifically, the SEC asks firms for "A description of . . . human capital resources, including in such description any human capital measures or objectives that management focuses on in managing the business (such as, depending on the nature of the registrant's business and workforce, measures or objectives that address the attraction, development, and retention of personnel). The SEC requires no metrics. Under this proposed rule a firm can assert that its employees are its most important resources, and that it works diligently to attract and retain a high-quality workforce, and comply with this new disclosure requirement, without actually being held to account for these assertions. This open-ended invitation frustrates the ability of investors to compare human capital management between companies, as one firm might volunteer quantitative information, and a peer may not.

We believe this nebulous requirement will do little to inform investors and wastes an important opportunity to make disclosures relevant where human capital has become a determining factor in the fate of the average company. In this case, we believe that the SEC ignores emerging acknowledgement in the business community about the broader role of corporations. In August 2019, the Business Roundtable, which is an association of the CEOs of leading American companies, issued what it termed a "Statement on the Purpose of a Corporation." The second of five principles states that these CEOs are committed to "investing in our employees. This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect."[11]

For investors, some of whom may be wary that this and other commitments may subordinate shareholder interests, the least that the SEC could do is require more robust disclosure of human capital. If major U.S. companies are already moving in the direction of thinking more holistically about their workforce as the Business Roundtable letter suggests then it should be easy to disclose this information to shareholders.

---

[7] *Rulemaking petition to require registrants to disclose information about their human capital management policies, practices and performance*, File No. 4–711 HUMAN CAPITAL MANAGEMENT COALITION (July 6, 2017), available at https:// www.sec.gov/rules/petitions/2017/petn4-711.pdf

[8] *Members of the Human Capital Management Coalition*, HUMAN CAPITAL MANAGEMENT COALITION (website visited September 16, 2019)
http://uawtrust.org/AdminCenter/Library.Files/Media/501/About%20Us/HCMCoalition/hcmmembership2018.pdf

[9] *Petition,* Request for rulemaking on environmental, social, and governance (ESG) disclosure, SECURITIES AND EXCHANGE COMMISSION (October 1, 2018) https://www.sec.gov/rules/petitions/2018/petn4-730.pdf

[10] *Id.*

[11] *Our Commitment,* BUSINESS ROUNDTABLE, (August 19, 2019)
https://opportunity.businessroundtable.org/ourcommitment/

Environmental Record

In addressing changes under Items 101 and 103 that address environmental issues, the SEC again ignores glaring issues and proposes to reduce reporting.

In 2018, investors representing 5 trillion in assets under management submitted a new petition for a rulemaking at the SEC that would create a standard disclosure framework on all ESG issues for public companies.[12] Major investors who signed the petition include California Public Employees' Retirement System (CalPERS), New York State Comptroller Thomas P. DiNapoli, Illinois State Treasurer Michael W. Frerichs, Connecticut State Treasurer Denise L. Nappier, Oregon State Treasurer Tobias Read, and the U.N. Principles for Responsible Investment. It's clear from this petition and previous calls from investors for increased ESG disclosure that investors want more comprehensive, comparable data, not less. Global warming represents an existential threat to the planet, including the future of every public company.

In response to this, the SEC actually proposes to reduce environmental reporting. Specifically, it proposes to revise the $100,000 threshold for disclosure of environmental proceedings to which the government is a party to $300,000 to adjust for inflation. Ignoring the missed opportunity to provide needed disclosure, this reduction in reporting flies in the face of already inaccurate disclosures. A government agency found that "74 percent of publicly-traded companies had failed to adequately disclose the existence of environmental legal proceedings in their 10-K registration requirements."[13] The SEC should be increasing enforcement of its minimal disclosure requirements instead of reducing requirements in the vital arena.

Political Spending

Shareholders are especially interested in political spending. Each year, shareholder resolutions calling for such disclosure count among the most common within the ESG category. In 2019, there were more than 93 proposals filed on this issue. [14] Currently, 292 companies are disclosing some or all of their political spending with corporate money.[15] In 2011 a bipartisan committee of leading corporate and securities law professors, including now- Commissioner Robert Jackson, filed the petition requesting a rulemaking requiring all public companies to disclose their political expenditures.[16] Despite more than 1.2 million comments coming in to that petition, the SEC has never taken the rule up in a meaningful way.[17]

---

[12] https://www.sec.gov/rules/petitions/2018/petn4-730.pdf

[13] Lawrence Schnapf, "Managing Environmental Liability in Business Transactions and Brownfield Redevelopment," Juris Publishing, (2013), cited in Letter, Domini Trust, SEC (August 12, 2014) https://www.sec.gov/comments/disclosure-effectiveness/disclosureeffectiveness-13.pdf.

[14] *Corporate Political Activity,* PROXY PREVIEW (website visited Sept. 23, 2019) https://www.proxypreview.org/2019/report/social-issues/corporate-political-activity

[15] *A Distinguished Record of Impact,* CENTER FOR POLITICAL ACCOUNTABILITY, (website visited October 15, 2019) https://politicalaccountability.net/impact

[16] Petition, COMMITTEE ON DISCLOSURE OF CORPORATE POLITICAL SPENDING, (August 3, 2011) https://www.sec.gov/rules/petitions/2011/petn4-637.pdf

[17] *Comments on Rulemaking Petition*, SECURITIES AND EXCHANGE COMMISSION, (website visited Sept. 23, 2019) https://www.sec.gov/comments/4-637/4-637.shtml

Additional obstruction occurred when conservatives in Congress inserted a policy rider into the appropriations process that prohibits the SEC from finalizing--though not from working on--the rule.[18]

The SEC received over 26,000 comments to the original Concept Release on Reg S-K, the overwhelming majority of which supported increased disclosure regarding corporate political spending. [19] Yet, this proposed rule skews in favor of comments from issuers and their allies who want decreased disclosure. As an example of corporate favoritism, the SEC cited letters from delivery giant FedEx 20 times in this proposed rule. It's not surprising that in the letters cited by the SEC FedEx calls for a more principles-based disclosure given that FedEx has declined to be more transparent even when its own shareholders ask for it. At its September annual meeting, FedEx management recommended a vote against a proposal from its shareholders requesting more transparency around the company's lobbying activity.[20] The shareholder proposal specifically references FedEx's undisclosed payments to the U.S. Chamber, the nation's largest business lobby. The concern flagged by shareholders that FedEx is supporting the Chamber's policy positions but not disclosing the risk those positions pose to shareholders is validated in FedEx's letter cited in this proposed rule, which concurs fully with the views submitted by the Chamber and the Business Roundtable.[21] Given that both FedEx and the Chamber are pushing for less rigorous disclosure, it seems that FedEx shareholders have a right to be concerned about the company's influence in Washington. Additionally, heavily citing a company who has repeatedly rebuffed its shareholders over disclosure undermines the SEC's impartiality in this proposed rule. Naturally, the Chamber opposes such disclosure; it is to the Chamber that much of the undisclosed political spending is directed.

Public Citizen joins institutional investors who also believe that this spending axiomatically affects corporate results. As it affects corporate results, it should be disclosed. Current law already provides disclosure of direct lobbying expenses and spending through political action committees (PACs). But corporations can spend indirectly, such as with contributions to the US Chamber of Commerce that, in turn, lobbies Congress. In the years following the financial crisis, when the CEOs of major bailed-out Wall Street banks steered clear of public appearances in Washington, they were replaced by envoys of the Chamber. With a boilerplate introduction about the Chamber represents small business, these envoys would wax on the dangers of high capital requirements, margin for uncleared swaps, liquidity in the market for junk-rated bonds. None of these issues were of concern to small business; they were of concern to the large banks unwilling to make the case directly to Congress and the regulators.

Investors want and deserve to know the full extent of political spending by the companies they own. If a company chooses to engage in the policy making process for the sake of their business, there should be no reason why management would want to hide that critical information from their shareholders and customers.

Costs but no Benefits

[18] S. 2524, UNITED STATES SENATE (Sept. 19, 2019) https://www.congress.gov/bill/116th-congress/senate-bill/2524/text?q=%7B%22search%22%3A%5B%22financial+services+and+general+government%22%5D%7D&r=1&s=1

[19] Tyler Gellasch, *Towards a Sustainable Economy*, AFL-CIO, ET AL (September, 2016) https://www.citizen.org/wp-content/uploads/sustainableeconomyreport.pdf

[20] Proxy Statement, *FedEx*, SECURITIES AND EXCHANGE COMMISSION (2019) https://www.sec.gov/Archives/edgar/data/1048911/000120677419002626/fdx3608061-def14a.htm#STOCKHOLDERPROPOSALS99

[21] https://www.sec.gov/comments/s7-06-16/s70616-259.pdf

It is especially telling that the one area that the SEC asks for additional disclosure relates to compliance costs. The SEC asks corporations to count up and disclose the total cost of all compliance, including compliance with environmental laws. We do not object to such disclosure, but find it revealing of a political agenda. The proposed SEC figure on total compliance costs (without a true calculus of benefits), will equip those who contest sensible safeguards with a convenient and potentially overstated figure.

The Chamber routinely laments the burden on the American economy of these sensible safeguards, ignoring benefits.[22] Other business-sponsored organizations that label themselves research organizations routinely criticize regulations, and this new SEC mandated disclosure will advance their cause.[23]

In fact, sensible safeguards promote the economy, with safe roads speeding commerce, safe food making for a healthy workforce, and more.

Conclusion

Pervading this proposed reduction in disclosure is the assumption that investors want less information, and that important information is overlooked when accompanied by extraneous material. This ignores the fact that the front line of information consumption are professional analysts at financial firms, as well as the fact that computers can easily search and sort information.

While the SEC ignores the many petitions we've cited, we are unable to ignore that this proposal turns its back on its mandate to promote investors. We ask the SEC to return to the drafting table and propose disclosures that respect these petitions.

For questions, please contact Rachel Curley at [redacted], or Bartlett Naylor at [redacted]

Sincerely

Public Citizen

---

[22] Bartlett Naylor, *Taking a Hard Look at a Campaign Critical of Fiduciary Rule,* NEW YORK TIMES (June 9, 2016) https://www.nytimes.com/2016/06/10/business/dealbook/taking-a-hard-look-at-a-campaign-critical-of-a-fiduciary-rule.html

[23] Taylor Lincoln, *A Key Cog in Charles Koch's Master Plan*, PUBLIC CITIZEN (2019) https://www.citizen.org/article/koch-cog-rsc/?eType=EmailBlastContent&eId=34f332f1-3022-46c6-a139-e757fdcb9ba1