

October 22, 2019

**Via Electronic Delivery**

Ms. Vanessa A. Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

**RE: File Number S7-11-19 – Comments on Proposed Amendments to Modernize Select Disclosures under Regulation S-K**

Dear Ms. Countryman:

The Center on Executive Compensation (“Center”) and HR Policy Association are pleased to jointly submit their comments and perspectives (“Commission”) on the Commission’s proposed amendments to modernize disclosures under Regulation S-K (Regulation S-K).

HR Policy Association’s (the “Association”) membership comprises the most senior human resource executives for more than 390 of the largest companies in the United States and globally. Collectively, our membership employs more than 20 million employees worldwide (which is nearly nine percent of the private sector workforce). The Center On Executive Compensation is a division of the Association. It is a research and advocacy organization dedicated to principles-based research, education and advocacy on executive compensation and related governance matters.

While the Commission has proposed several substantive amendments to Regulation S-K that touch on various other important disclosure topics/areas, our comment letter is focused on addressing the Commission’s proposed changes that impact disclosure of Human Capital Resources and/or Human Capital Metrics (HCM). The Commenters share the Commission’s stated (and laudable) goal that any amendments to Regulation S-K should “improve [the] disclosure regime for both investors and registrants”<sup>1</sup>. Bearing these principles in mind, the Commenters respectfully submit the following comments.

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<sup>1</sup> "Securities and Exchange Commission, Modernization of Regulation S-K Items, 101, 103 and 105 (Proposed Rules)." Federal Register 84:164 (August 23, 2019) p. 44358. Available at: <https://www.federalregister.gov/d/2019-17410>; Accessed: Sept. 14, 2019..

## I. **Executive Summary**

The Commenters are two organizations comprised of the highest-level human resources officers for many of world's largest companies, and our comments reflect their views and comments.

As stated, the Commenters' comments are largely confined to the Commission's proposed amendments to Item 101(c) that requires registrants (on a principles-basis) to:

Include, as a disclosure topic, human capital resources, including any human capital measures or objectives that management focuses on in managing the business, to the extent such disclosures would be material to an understanding of the registrant's business;<sup>2</sup>

In articulating its proposed changes to Regulation S-K, the Commission specifically rejected "'prescriptive' disclosure requirements"<sup>3</sup> that stand separate from management's judgment. Rather, the Commission determined that a registrant's disclosure should be guided by the principle of materiality while appropriately leaving the task of making that determination to "a registrant's management [who would need to] evaluate the significance of information in the context of the registrant's overall business and financial circumstances and to determine whether disclosure is necessary."<sup>4</sup>

The Commenters strongly agree that if a principles-based approach to disclosure of material human capital metrics or measures is far preferable to a prescriptive approach, if necessary at all, and should be framed as merely reiterating a company's already existing obligation to disclose material risk factors, including human capital risk. Boards are responsible for managing this risk on behalf of shareholders, and disclosure should serve to facilitate engagement on human capital matters, for which there is no standardization at present.

While companies operate their business using numerous metrics (financial, operational, and qualitative, including HCM), the Association and the Center believe that it would be extremely difficult for registrants to distill the essence of their complex organizations (especially in the area of Human Capital Management) into a set of standardized human capital metrics that are meaningful to them. Additionally, if the Commission were to amend Regulation S-K to require inclusion of specific human capital metrics, the Commenters believe that a significant additional regulatory effort would be required to define in detail the specific definitions and construction for each required metric.

Absent such additional definitive guidance (and likely even with such guidance), the Commission would effectively assert that two different registrant's HCM disclosures can be easily compared to each other. This is not currently the case, and the Commenters believe it is neither effective nor efficient to pursue such standardization.

While virtually all registrants use metrics (including HCM) to manage their organizations, the Commission was correct in recognizing that the principles undergirding the requirement for material investor disclosure articulated in Regulation S-K serve a very different purpose.

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<sup>2</sup> *Id.* at 44,360

<sup>3</sup> *Id.* at 44,359

<sup>4</sup> *Id.*

Investors expect management to use a robust set of systems, processes and metrics to run their organizations and for Boards to monitor these processes. With respect to human capital issues, the Commenters believe the information and commentary accompanying a registrant's business performance is the most effective context for disclosure of human capital management.

The Commenters agree the Commission may assist investors by encouraging registrations to consider how their human capital resources could be articulated to investors in a manner that is rooted in materiality and placed in context relative to the company's particular industry and business strategy.

However, we strongly believe the Commission should resist the desire to enumerate in the text of the regulation examples of that it considers appropriate human capital metrics in the text of the regulation. This happened with respect to the non-binding "examples" the Commission included to illustrate issues companies may wish to address in the CD&A. Rather than use the list to help develop a principles-based disclosure, the list was taken by many registrants as disclosures to be included in the CD&A.

## **II. Principles-Based Disclosure of Human Capital Metrics Is Preferable to Mandated Approach**

If the Commission decides to pursue greater disclosure of human capital metrics, the Commenters strongly prefer a principles-based disclosure to a mandated disclosure. Previously, the Association is on record opposing mandated human capital metrics disclosure.<sup>5</sup> It is the Commenters' view that specifically mandated disclosures add little to investor insight because of the significant differences in use and measurement designed to capture the different markets for human capital that exist across different businesses.

It is important to state affirmatively that in objecting to 'prescriptive requirements,' the Commenters and their members are not saying that human capital resources and managing the value of this 'resource' are not important. To be sure, the Commenters' members routinely use many types of HCM to manage their business operations daily. The Association's previously expressed concerns pertain not only to the cost of complying with a prescribed set of disclosures, but more importantly, to the lack of value such a disclosure delivers to investors.

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<sup>5</sup> See HR Policy Association Comments to the HR Standards Secretariat of the Society for Human Resource Management (SHRM) in Response to Investor Metrics Draft American National Standard (ANSI-SHRM-02001.201X dated April 9, 2012) *available at* [http://www.hrpolicy.org/downloads/2012/12-40\\_SHRM\\_Comments.pdf](http://www.hrpolicy.org/downloads/2012/12-40_SHRM_Comments.pdf).

Since the interest in publishing HR metrics has taken hold, the proponents of a more prescriptive disclosure regime have based their position that such mandates are workable (and in fact preferred) on several specific rationales. In reviewing the Commission's preface to the proposed amendments, the proponents of a prescriptive approach used these same justifications. These can be articulated as follows:

1. The use of human capital metrics (as a practice and discipline) is broadly accepted, clearly defined, and well-understood. Metrics can, therefore, be determined by all parties with great precision using identical definitions and methodologies. This yields human capital metrics that are wholly consistent and can be easily compared between companies both within and across industries;
2. Given the wide acceptance of HCM, virtually all registrants are using identical metrics universally in the same respects to run their businesses. As such, registrants would not face any additional burden or cost in providing this readily available HCM information to the investing public;
3. Concerns registrants may have with the proprietary nature of this information is significantly outweighed by the investing public's need to better understand the registrant's human capital resources;
4. Armed with this critical information, investors can self-assess the registrant's human capital resources management leading to beneficially deeper insight into not only the registrant's management of its human capital resources, but more importantly its underlying business. In addition, investors would have the ability to cross-compare a registrant's human capital resources with those of other issuers to better understand the registrant's business; and
5. Absent the SEC requirement disclosure of a set of pre-defined metrics, registrants would "game the system" and/or simply "talk around" the issue of their human capital resources depriving investors of important and necessary information on the registrant's business operations.

The Commenters disagree with these rationales. We urge the Commission to adopt a principles-based approach to a mandated approach. Each of the rationales for a more prescriptive approach detailed above misses the mark of beneficial investor disclosure. The Commenters response to the arguments above are as follows:

1. Common HCM Definitions or Reporting Approaches Do Not Exist. There is not a set of generally accepted, standardized Human Capital Metrics that companies use, even though certain companies or certain industries may use similar *categories* of human capital metrics.
  - a. Tailored to Individual Companies. Human capital metrics by their nature have been designed to be internal measures, and thus tend to be tailored to individual companies. Often human capital metrics vary depending on the company's industry and the needs of their business (or even the registrant's IT systems available to collect required inputs). There are significant variations in what

information is relevant to a company and thus what is measured, how it is collected and how frequently it is collected or even what is relevant to any particular industry or organization.

- b. Investor Interest and Use of HCM Varies Widely. Likewise, different investors have different levels of interest in human capital and focus on different aspects of human capital depending on their investment strategies. This reinforces the need for a principles-based disclosure of material information.
- c. A Prescriptive Approach Would Require Significant Additional Definition and Disclosure. If the SEC were to prescribe disclosure of certain HCM, the Commission would be responsible for determining which metrics should be disclosed, precisely defining each term, the applicable measurement periods, data collection required, disclosure formatting requirements and the required footnotes. It would also need to determine how changes in the business may be incorporated into HCM results to not mislead investors, among other issues. This would lead to an additional burden on the Commission vis-a-vis the need to provide regulations, significant guidance on registrants and the investing public. Although such an approach may lead to comparability, the disclosed metric may not reflect how a company looks at a particular human capital issue, requiring yet more disclosure.

Take for example the calculation of employee turnover. The Commission would need to address several key questions in its regulations (after all, this information would be part of a 'filed' disclosure) including:

- Which individuals are employees?
- What is the definition of turnover – does it include involuntary as well as voluntary turnover?
- What is the measurement date?
- What is the impact of seasonal and/or temporary workers on the calculation?
- For multinational employers, how can the same metrics be made relevant across multiple jurisdictions with highly varied employment markets, customs, and regulations?
- How would the impact of business combinations (acquisitions and divestitures) impact turnover?
- What amount of turnover data (monthly, quarterly, semi-annually or annually) would be useful to investors?

To simply say all registrants measure turnover (which they universally do) masks the shortcomings of requiring and developing a uniform definition. Not only do companies measure this ‘simple metric’ differently, very often organization within a single registrant will calculate turnover differently because it reflects the differences in their operations.

A principles-based approach would allow the Commission to lay an impactful framework that then could be used to foster engagement between the issuer and investors.

2. A Prescriptive Approach Would Lead to Greater Burdens Without Additional Insight Similar to the Pay Ratio Mandate. As stated above, no ‘standard’ set of HCM metrics exists by which all registrants measure themselves. Beyond the regulatory burdens discussed above, a prescriptive approach would require many registrants to calculate metrics in a way that they do not use, imposing significant additional costs on registrants for little value to investors. That is, the mandated disclosure of HCM without broad agreement among registrants, investors and the Commission is likely to look like the pay ratio disclosure.

For example, the pay ratio number may be disclosed by all companies and thus purport to be comparable. However, the pay ratio provides little insight due to the extreme variance in the corporate structures and strategies which serve as the underlying inputs for the pay ratio calculation. Thus, without *significant* additional context on why a ratio is high or low or why a comparison to another company is valid, the metric fails in its stated purpose – to provide useful information about a company.

Similar to pay ratio, if companies were required to disclose specific human capital metrics, many would be required to calculate data for disclosure that otherwise serves no business or strategic purpose with respect to that particular company. Further, such a disclosure would likely result in substantial additional narrative disclosures in order explain the number and give further context to avoid having investors draw the incorrect conclusions.

Returning to the example of employee turnover above, the disclosure of a standardized turnover number gives little insight without management provided context on whether the company can retain critical talent.

Thus, a principles-based approach allows registrants to put their HCM in the context of their business strategy when such information is material to an understanding of the company. Unlike the mandated pay ratio rules, the Commission has a choice how it structures HCM rules to avoid past pitfalls for registrants and investors alike.

3. Mandated Disclosure Risks Disclosing Proprietary Information and/or Personal Information. With respect proprietary information, the Commenters’ concerns fall into two areas: (1) proprietary business practices, and (2) disclosing personal information.

With respect to proprietary business practices, the Commenters are concerned that the metrics may provide a competitive advantage in the way the issuer has developed and used the information in running its business. Such a company would not be interested in sharing that information with its competitors.

The concern with respect to divulging personal information is based on earlier attempts to develop a mandated human capital disclosure that included, *e.g.*, a requirement to disclose leadership depth. The concern we expressed at that time was that at senior levels, disclosing leadership depth could be tantamount to identifying the individuals involved by name.

This information has considerable competitive value and tells competitors exactly how the company is staffed and organized. Of equal or even greater concern, the disclosure of leadership depth provides a clear target for executive recruiters and competitors looking for talent, or potentially puts the company at undue risk of attracting latent if a “lack of leadership depth” is identified.

Most large companies depend on the unique talents of a limited number of ‘key’ individuals who do not possess policy-making influence (*e.g.*, a key product designer or key salesperson). How a company might go about addressing the needs of limited set of key individuals below the policy-making level realistically delves into how the registrant is managing its day-to-day operations, which is outside the scope of SEC disclosure requirements.

Rather than focusing on specific metrics, under a principles-based disclosure, companies can explain the categories of information that are relevant to the company, thus providing a basis for engagement with investors without divulging sensitive competitive information. This is very similar to the way that companies now disclose their CEO succession processes. Individual successors are not identified, but the succession review process is disclosed and discussed.

4. A Principles-Based Approach Is the Most Effective Approach for HCM Issues. With respect to the assertion that disclosure of Human Resources Metrics would provide investors with deeper insight into a company’s operations, the principles-based approach the Commission has proposed allows registrants the flexibility to continue to use Human Capital Metrics tailored to their individual needs while appropriately requiring registrants to disclose HCM that are ‘material’ to the registrant’s organization.

The goal of the disclosure should be providing investors with *material* information that leads to true insight, especially with respect to management of human capital risk. This is akin to the requirement that Compensation Committees assess and disclose in the proxy statement any material risks created by the company’s compensation structure by employees and executives.

5. Many Companies Already Report HCM Through Sustainability Reports. Most registrants already disclose considerable information in their sustainability reports that encompass human capital, which reaffirms that a heavy regulatory approach to human capital is not needed. According to a 2019 Shearman & Sterling report, 96 of the top 100 companies publish a CSR report and 83 include disclosures related to human capital and

talent.<sup>6</sup> In addition, registrants frequently re-examine the appropriateness of the metrics they capture and either tweak them or make wholesale changes. Thus, there is a question as to whether additional disclosure is necessary.

If the Commission decides to move forward, the proposed amendments (as clearly stated by the Commission) require a registrant to disclose metrics as well as such changes if any such change was deemed ‘material’ (as defined by longstanding Commission and court precedents). Such a standard is more appropriate and will serve to mitigate the potential of disclosure overload the issuer community as an important guidepost in the preparation of its disclosures. The principles-based approach will also allow companies to explain to investors how the Board and management use HCM to monitor operations and mitigate risk.

In sum, the Commenters support the Commission’s principles-based approach regarding HCM disclosures compared to a mandated disclosure. The Commenters strongly encourage the Commission to resist further efforts or petitions to impose either blended principles-based and prescriptive regime or solely prescriptive regime with respect to HCM disclosures.

### **III. Addressing Specific Requests for Comment**

The Commission, in its draft amendments specifically asked for comments on specific issues. The Commenters are pleased to provide its thoughts and suggestions as those comments and recommendations pertain to human capital resources. Specifically, the Commenters address the Commission’s Request for Comment with respect to items 12, 15 and 21 through 24.

**Comment Request 12.** Should we shift to a more principles-based approach for Item 101(c), as proposed? Would registrants find it difficult to apply the principles-based requirements?

**Commentary:** The Commenters support the Commission’s principles-based approach. This approach is rooted in the Commissions principles as articulated by the SEC Chairman of: “(1) materiality; (2) comparability; (3) flexibility; (4) efficiency; and (5) responsibility.”<sup>7</sup> The Commenters do not believe that the effort of implementing a principles-based approach would outweigh the benefits to the investing public and as discussed above, believes that comparability should not be the touchstone for HCM disclosure.

**Recommendation(s):** The Commenters recommend that all final amendments concerning the disclosure of Human Capital Metrics clearly state that disclosure of such discussion (including the disclosure of any metrics) is to be supplied consistent with the

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<sup>6</sup> Shearman and Sterling, Corporate Governance and Executive Compensation Survey 2019, at 13-14, last accessed at [http://digital.shearman.com/i/1162884-2019-corporate-governance-executive-compensation-survey/0?\\_ga=2.171521381.47734696.1571760385-997498302.1568461070](http://digital.shearman.com/i/1162884-2019-corporate-governance-executive-compensation-survey/0?_ga=2.171521381.47734696.1571760385-997498302.1568461070).

<sup>7</sup> Clayton, Jay. “Remarks to the SEC Investor Advisory Committee.” Public Statements, Securities & Exchange Commission, Securities & Exchange Commission, 28 Mar. 2019, <http://www.sec.gov/news/public-statement/clayton-remarks-investor-advisory-committee-032819#>, Remarks to the SEC Investor Advisory Committee; Lasted Accessed: September 15, 2019.

Commission's focus on 'materiality.' At this point, the focus is to create comparability of the format of disclosure but not specific metrics, given the wide differences in the how companies use and defined such metrics and the impact of having the SEC define the metrics at this point.

**Comment Request 15.** Should we retain Item 101(c)'s distinction between disclosure topics for which segment disclosure should be the primary focus, and those for which the focus should be on the registrant's business taken as a whole, as proposed? If so, is our allocation of the listed disclosure topics into the two categories appropriate?

**Commentary:** As it impacts Human Capital Resource reporting, the Commenters support the Commission's position with the proviso that "materiality" remains the standard whether it is the business as a whole or segment and "comparability" for investors is maintained.

**Recommendation(s):** Any final amendments impacting disclosure of Human Capital Metrics should clearly state that such metrics are subject to both 'materiality' and the need to enhance investor 'comparability.' The final amendments should state that to the extent that a registrant believes that a business segment is otherwise material to its business taken as a whole, the registrant may have a reporting obligation with respect to its human capital resource as to that segment. On the other hand, a registrant that manages HCM in a comparable manner across different business segments should not be mandated to provide segment-level disclosure where such disclosure would not provide material additional information.

**Comment Request 21.** Should disclosure regarding human capital resources, including any material human capital measures or objectives that management focuses on when managing the business, be included under Item 101(c) as a listed disclosure topic, as proposed? Should we define human capital? If so, how?

**Commentary:** The Commission's approach should be to remind (not require) registrants of the importance of reporting to investors material information that may impact the investor's decision to buy or sell the registrant's securities. The Commenters believe that by listing examples and other criteria in Regulation S-K, there is a substantial risk that registrants will view the examples as a 'soft requirement' thereby encouraging them to move away from a principles-based analysis to human capital resources the Commission so carefully laid out.

**Recommendation(s):** The Commission should be commended for its principles-based approach with respect to human capital resources and put the onus on registrants to articulate for investors material information with respect to Human Capital Resources. The Commission should clearly state the omission of discussion of a registrant's human capital resource shall not be construed as a failure by the registrant to meet its obligations under the Commission's disclosure regime.

**Comment Request 22.** With respect to human capital resource disclosure, should we provide non-exclusive examples of the types of measures or objectives that management may focus 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, as proposed? Would providing specific examples potentially result in disclosure that is immaterial and not tailored to a registrant’s specific business? Would not including such examples result in a failure to elicit information that is material and in some cases comparable across different issuers?

**Commentary:** The Commenters believe that given the established requirement that each registrant’s disclosure contain material information with respect to the registrant’s Human Capital Resources is a clear and unambiguous standard. The Commenters believe that trying to provide what would be well-intended as helpful examples in the text of the regulation would give the false impression that the Commission’s real intention was to impose a set of ‘soft’ prescriptive requirements. This could have the effect of undermining the Commission’s clear intent to establish a principles-based disclosure based on materiality. This happened with respect to the non-binding “examples” the Commission included to illustrate issues companies may wish to address in the CD&A. Rather than use the list to help develop a principles-based disclosure, the list was taken by many registrants as disclosures to be included in the CD&A.

**Recommendation(s):** The Commission should resist the desire to enumerate examples of what it would consider to be appropriate human capital resource metrics in the text of the regulation. The Commenters share the Commission’s concerns as articulated in the request for comment.

**Comment Request 23.** With respect to human capital resource disclosure, should we include other non-exclusive examples of measures or objectives that may be material, such as the number and types of employees, including the number of full-time, part-time, seasonal and temporary workers, to the extent disclosure of such information would be material to an understanding of the registrant’s business? Could other examples include, depending on the nature of the registrant’s business and workforce: Measures with respect to the stability of the workforce, such as voluntary and involuntary turnover rates; measures regarding average hours of training per employee per year; information regarding human capital trends, such as competitive conditions and internal rates of hiring and promotion; measures regarding worker productivity; and the progress that management has made with respect to any objectives it has set regarding its human capital resources? Would providing specific examples potentially result in disclosure that is immaterial and not tailored to a registrant’s specific business? Would not including such examples result in a failure to elicit information that is material and, in some cases, comparable across different issuers?

**Commentary:** The Commenters incorporate their comments above articulating its concerns with metrics and their comparability. The Commenters believe that the Commission’s articulated principles-based approach is far preferable to a prescriptive approach. The Commission’s approach serves as an important reminder to issuers of the importance of providing investors with material information, including that pertaining to Human Capital Resources.

Each issuer manages its business differently. By providing examples, the Commission may inadvertently cause issuers to believe that their disclosure obligation ends after they have supplied whatever metrics are enumerated. As the Commission has made clear, determining whether something is or is not “material” is the determining factor for disclosures. Providing a list of examples in the text of the regulation may only serve to undermine the seriousness of that analysis by creating an impression that the Commission considers the examples to be material. The Commenters believe that if the Commission articulates examples it could result in immaterial disclosure that is not tailored to the registrant’s business.

**Recommendation(s):** The Commission should resist articulating in its regulations what might otherwise be regarded as helpful examples of human capital metrics a registrant should consider. To the extent that the Commission believes such illustrative information would be helpful it should be limited to the preamble to the amendments.

**Comment Request 24.** Should we retain an explicit requirement for registrants to disclose the number of their employees? Alternatively, should we permit registrants to disclose a range of the number of its employees and/or a range for certain types of employees?

**Commentary:** Given the fact that registrants are required to provide comparative data on executive compensation (i.e., pay ratio), which essentially draws upon the registrant’s total employees, the Commission should look for consistency between what registrant’s supply investors in their annual reports.

**Recommendation(s):** Any statement as to the number of employees (as defined by local law) should be materially accurate. It goes without saying that organizations are in constant flux as to the number of employees they have on-roll at any one point in time. Some investors use the total headcount as a proxy for a registrant’s productivity. In that case, the investor is using registrant supplied information to analyze the registrant’s performance – something that the Association and Center clearly support.

Ms. Vanessa A. Countryman

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## **Conclusion**

The Commenters appreciate the opportunity to provide its comments on the Commission's proposed amendments Regulation S-K. The Commenters believe the Commission's principles-based approach is far preferable to a prescriptive approach. To that end, the Commission should resist prescribing what Human Capital metrics are important either explicitly or implicitly (through articulated examples).

If you have any questions about the Center's comments, please do not hesitate to contact me at 202-789-8670

Sincerely,



Timothy J. Bartl

President, HR Policy Association

Chief Executive Officer

Center On Executive Compensation

cc:     Securities and Exchange Commission:  
          Hon. Jay Clayton, Chair  
          Hon. Robert J. Jackson, Jr. Commissioner  
          Hon. Hester M. Peirce, Commissioner  
          Hon. Lead L. Roisman, Commissioner  
          Hon. Allison Herren Lee, Commissioner