



California Public Employees' Retirement System

Executive Office

400 Q Street, Sacramento, CA 95811 | Phone: (916) 795-3829 | Fax: (916) 795-3410

888 CalPERS (or 888-225-7377) | TTY: (877) 249-7442 | www.calpers.ca.gov

Sustainability Accounting Standards Board

1045 Sansome Street, Suite 450

San Francisco, CA 94111

Via email: kelli.okuji-wilson@sasb.org

February 21, 2021

Subject: "Public Consultation" on the Preliminary Framework on Human Capital and the Sustainability Accounting Standards Board (SASB) Standards

Dear Recipient,

On behalf of the California Public Employees' Retirement System (CalPERS), I write to express our support for the SASB Preliminary Framework on Human Capital.

As the largest public defined benefit pension fund in the United States, CalPERS manages approximately \$450 billion in global assets on behalf of more than two million members. CalPERS' Investment Belief #4 recognizes that "Long term value creation requires effective management of three forms of capital: financial, physical and human." As fiduciaries, we aim to provide long-term sustainable, risk-adjusted returns by efficiently allocating capital and voting in line with our long-term objectives.

Corporate reporting plays a critical role in the integrity and efficiency of financial markets as effective disclosures facilitate informed decision-making by providing transparent and relevant data on the economic performance and condition of a business. So, as a global institutional investor, we expect companies to provide integrated representations of operational, financial, human capital management, environmental, social, and governance performance in terms of both financial statement and non-financial statement results. However, the current disclosure regime for corporate reporting falls short of our expectations, and we believe that companies should disclose better information so that shareowners can more easily identify, assess, and manage risk and opportunity.

As a long-time proponent and member, we applaud SASB in taking the steps to account for human capital across its standards. The convergence of the current economic, climate, and public health crises, as well as the mounting call to advance racial equity have accelerated investor focus on effectively managing all forms of capital, especially human capital. As

emphasized by the rise of a new class of worker (i.e., Frontline Essential Worker),¹ it is clear that businesses depend on the workforce as a source of value creation which, if mismanaged, could harm long-term performance. The size, scale and viability of a company's operations has a direct impact on the scope of potential human capital risks which underscores why these disclosures are being sought as shareowners push for greater transparency and society demands for all of its people to be valued.

As outlined in the CalPERS Governance and Sustainability Principles² (Principles), "we expect, fair, accurate, timely, and assured reporting on how companies employ financial, physical, and human capital to generate sustainable returns, as well as how they identify, monitor, and mitigate risks to those three forms of capital." However, current financial reporting rules require companies to disclose very little information about how human capital is measured or managed. In addition, reporting varies by company and too often what is reported fails to reflect reality. Furthermore, global reporting standards around the "S" of Environmental, Social, Governance (ESG) have historically been weak. At a regulatory level, the recent SEC rulemaking³ on human capital disclosures was non-prescriptive and did not go far enough to address the information gap between what company managers know about a company and what is revealed to investors. We have long-advocated for more line-item disclosures as opposed to the purely principles-based approach more common globally. So, we are delighted to support SASB's work to modernize corporate reporting and thereby move the market forward with respect to human capital disclosures, hopefully, including a substantially greater focus on diversity and the addition of certain identified metrics.

This project is also timely given SASB and the International Integrated Reporting Council's (IIRC) plans to address global sustainability standards. It is CalPERS' view that comprehensive global standards for corporate reporting must include sustainability factors that drive long-term risk and return. In past comment letters,⁴ CalPERS has made clear our desire for more detail around human capital management disclosures. Additionally, through our work with the Human Capital Management Coalition we have advocated for stronger disclosure requirements for human capital reporting that provide quantitative context and qualitative explanation for a company's strategy to create long-term value and mitigate risks through its management of human capital. Similarly, through our participation on the SEC's Investor Advisory Committee, we urged the SEC to undertake a robust examination of the role human capital management plays in value

¹ According to the [U.S. Department of Homeland Security](https://www.ncsl.org/research/labor-and-employment/covid-19-essential-workers-in-the-states.aspx#%3A%7E%3Atext%3DAccording%20to%20the%20U.S%20Energy%20to%20defense%20to%20agriculture), essential workers are those who conduct a range of operations and services that are typically essential to continue critical infrastructure operations.

² <https://www.calpers.ca.gov/docs/forms-publications/governance-and-sustainability-principles.pdf> (dated September 2019).

³ <https://www.sec.gov/rules/final/2020/33-10825.pdf>.

⁴ See the following:

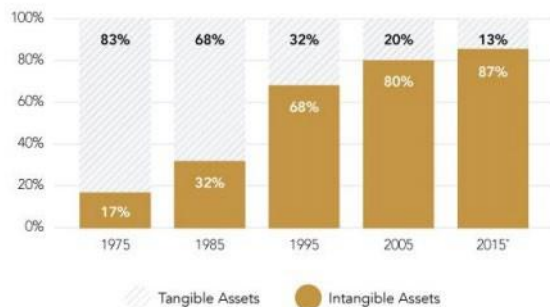
- <https://www.sec.gov/comments/s7-20-15/s72015-38.pdf> Letter from CalPERS to Brian J. Fields, Secretary, U.S. Securities and Exchange Commission (Nov. 30, 2015).
- <https://www.sec.gov/comments/s7-06-16/s70616-267.pdf> Letter from CalPERS to Brian J. Fields, Secretary, U.S. Securities and Exchange Commission (July 21, 2016).
- <https://www.calpers.ca.gov/docs/legislative-regulatory-letters/sec-10-22-19-letter-modern-s-k-items-101-103-105.pdf> Letter from CalPERS to Vanessa Countryman, Secretary, U.S. Securities and Exchange Commission (dated October 22, 2019).

creation and provided recommendations⁵ on improving the corporate disclosure system to include specific disclosures regarding intangible assets, such as human capital.

The critical need for better human capital management disclosures, particularly around the health and well-being of a company's workforce, was reaffirmed in a statement⁶ made by former United States Securities and Exchange Commission (SEC) Chairman Jay Clayton. Although Clayton's position on human capital disclosures was only adopted in principal, one cannot ignore the evidence that 85 percent of the S&P 500 balance sheet is intangible assets. Therefore, current financial reporting is insufficient as it only covers 15 percent of the balance sheet.

Figure 1

COMPONENTS of S&P 500 MARKET VALUE



SOURCE: OCEAN TOMO, LLC

Recognition of the positive correlation of human capital to value creation continues to build amidst growing research⁷ driving the mounting call for human capital management disclosures. The Office of the Illinois State Treasurer published a white paper⁸ titled "The Investment Case for Board Diversity" which provides an extensive and comprehensive review of academic and practitioner research on the value of gender and racial/ethnic board diversity for investors. The examination finds that "the gender and racial/ethnic composition of corporate boards does indeed have a material and relevant impact on company performance and investors." Likewise, a research study⁹ on "The financial case for human capital disclosure by firms" by Dr. Anthony Hesketh, Lancaster University Management School, found a positive correlation between performance and disclosure of human capital data. While the value-relevance of human capital disclosures is without question, we have yet to reach consensus on the right reporting standards.

⁵ <https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac032819-investor-as-owner-subcommittee-recommendation.pdf> (dated March 19, 2019).

⁶ <https://www.sec.gov/news/public-statement/statement-clayton-hinman> (dated April 8, 2020).

⁷ Research has found that high quality HCM practices correlate with lower employee turnover, higher productivity, and better corporate financial performance, producing a considerable and sustained alpha over time. See: Mark Huselid, The Impact of Human Resource Management Practices on Turnover, Productivity, and Corporate Financial Performance, 18 Academy of Management J. 635 (1995). See: Alex Edmans, Does the Stock Market Fully Value Intangibles? Employee Satisfaction and Equity Prices, 101 J. of Financial Economics 621 (2011).

⁸ [https://illinoistreasurergovprod.blob.core.usgovcloudapi.net/twocms/media/doc/il%20treasurer%20white%20paper%20-%20the%20investment%20case%20for%20board%20diversity%20\(oct%202020\).pdf](https://illinoistreasurergovprod.blob.core.usgovcloudapi.net/twocms/media/doc/il%20treasurer%20white%20paper%20-%20the%20investment%20case%20for%20board%20diversity%20(oct%202020).pdf) (October 2020).

⁹ Intangible or Invisible? https://www.calpers.ca.gov/docs/board-agendas/202007/full/day1/03-pp-hcm_a.pdf.

To enhance consistency and comparability, a framework for human capital disclosures should include certain line items. We are delighted to see that the six key themes under evaluation in SASB's Preliminary Human Capital Framework are consistent with the universal line-item disclosure metrics that we petitioned¹⁰ the SEC to mandate. We do hope that SASB places a significantly larger emphasis on the impact and importance of diversity on boards and in the work force. We acknowledge that some human capital metrics may be unique or universal depending on the industry, sector, or business strategy; however, there are a number of specific cross-cutting issues that apply to all companies.

At a minimum¹¹, universal human capital reporting by companies should include:

- 1 Workforce demographics (number of full-time and part-time workers, number of contingent workers, policies on and use of subcontracting and outsourcing)
Overlap with SASB theme(s): Workforce composition and workforce costs, Workplace culture, Workforce investment, Alternative workforce, and Labor conditions in the supply chain
- 2 Workforce stability (turnover (voluntary and involuntary), internal hire rate)
Overlap with SASB theme(s): Workplace culture and Mental health, wellbeing, and health-related
- 3 Workforce composition (diversity, pay equity policies/audits/ratios)
Overlap with SASB theme(s): Workforce composition and workforce costs, Workplace culture and Workforce investment
- 4 Workforce skills and capabilities (training, alignment with business strategy, skills gaps)
Overlap with SASB theme: Workforce investment
- 5 Workforce culture and empowerment (employee engagement, union representation, work-life initiatives)
Overlap with SASB theme: Workplace culture
- 6 Workforce health and safety (attendance policies, work-related injuries and fatalities, lost day rate)
Overlap with SASB theme: Mental health, wellbeing, and health-related
- 7 Workforce productivity (return on cost of workforce, profit/revenue per full-time employee)
Overlap with SASB theme(s): Workforce composition and workforce costs, Workplace Culture, Workforce investment, and Mental health, wellbeing, and health-related
- 8 Human rights commitments and their implementation (principles used to evaluate risk, constituency consultation processes, supplier due diligence)
Overlap with SASB theme(s): Alternative workforce and Labor conditions in the supply chain
- 9 Workforce compensation and incentives (bonus metrics used for employees below the named executive officer level, measures to counterbalance risks created by incentives)
Overlap with SASB theme(s): Workforce composition and workforce costs, Workplace culture, and Alternative workforce

¹⁰ <https://www.sec.gov/rules/petitions/2017/petn4-711.pdf>, Human Capital Management Coalition petition to the U.S. Securities and Exchange Commission (dated July 6, 2017).

¹¹ <https://uawtrust.org/AdminCenter/Library.Files/Media/501/About%20Us/HCMCoalition/hcmc-commentsubmission-oct2019.pdf> (dated October 22, 2019).

We believe that SASB should expand the general issue categories under its human capital dimension to include these disclosure metrics across all industries. These themes are material to investors across many companies and should inform SASB's future standard-setting work. Addressing these specific themes will produce a system of meaningful, uniform, and comparable disclosures that will provide investors with a more comprehensive accounting of its workforce. This is significant because the most valuable part of many companies is its people, the human capital.

Research is a core pillar of CalPERS' sustainable investment strategy, which reflects CalPERS Investment Belief #4, so we have a Request for Information out at this time which seeks to identify providers that can assist CalPERS in sourcing and evaluating a new round of analysis and research related to climate change risk and human capital management in what will be the third phase of the Sustainable Investment Research Initiative. This curated and peer-reviewed research will inform our strategy on sustainable investment and help ensure CalPERS' investment decisions are grounded on cutting-edge, evidence-based economic insights.

We appreciate the opportunity to provide our comments and look forward to supporting SASB in its future standard-setting work. Please do not hesitate to contact Anne Simpson, Managing Investment Director, at Anne.Simpson@Calpers.ca.gov, if you have any questions regarding our responses. Thank you for considering our comments.

Sincerely,

Marcie Frost
Chief Executive Officer

cc: Anne Simpson