How much is the 'great resignation' costing companies?
22 June 2022, by JK Bahr

For many investors, the SEC's November 2020 human capital disclosure requirement didn't require enough. The rule allows companies to choose what workforce costs, wellness, diversity and retention details—among other human capital data—to share, providing substantial managerial discretion. Human capital has become a major financial performance predictor, especially amidst a tight labor market. On average, labor expenses make up 57% of operating costs at S&P 500 companies, according to MyLogIQ. High turnover rates can also indicate poor management or a lack of business agility. In competitive markets shareholders worry that companies might subvert workforce risks without stricter SEC regulations. But a new study by three Vanderbilt professors may allay these fears. It examines human capital disclosures over 20 years, finding most companies reveal risk in good faith and that prior SEC rule changes made a significant impact.

Which human capital topics do companies discuss?

Peter Haslag, Berk A. Sensoy, and Joshua T. White, finance professors at Vanderbilt's Owen Graduate School of Management, used natural language processing to analyze what type of employee-related information managers from 3,000 companies provided to investors from 2001 to 2021.

They identified 11 key human capital disclosure topics: attract and retain (A&R), integration, workforce reductions, unions, data security, health and safety, trade secrets, competition, bribery, morale and diversity. The authors measured each topic's frequency and compared it with shareholder priorities and relevance within each company's industry.

"If managers are providing timely disclosures, we expect them to provide more intense discussions of topics that are material to their investors," Sensoy said. "We might not find that if investor concerns about inadequate disclosure are valid."

For example, companies in unionized industries should devote more discussion to collective bargaining agreements. A&R should be a heavily covered topic, particularly in competitive industries where turnover risk is greater. These trends are exactly what the researchers found in the data.

"Firms seem mostly forthcoming in the factors relevant to their human capital," White said. "A&R disclosure is generally increasing over time, and firms with more high-skilled workers, greater turnover, and shorter employee tenure provide more A&R disclosures. Also, firms facing greater competition still disclose more A&R statements, on average, rather than strategically withholding information."

Are human capital disclosures accurate?

Since attract and retain was one of the most common topics in human capital disclosures,
researchers used it as a proxy to determine reporting accuracy. They compared the reported A&R data to a proprietary database of 45 million job histories. They calculated separation rates for each company and identified predictable causes like industry mobility and high labor competition. The remaining turnover with no predictable causes might indicate employee dissatisfaction.

"The data showed a strong positive relation between employee turnover and A&R disclosure increases in the following year," Haslag said. "And there are even more disclosures when unpredicted employee turnover increases. Overall, it supports the idea that managers are largely forthcoming and accurate about A&R risk."

**How have SEC regulations affected human capital disclosures?**

The study also tracked changes in human capital disclosure through two SEC regulation changes: the expanded mandatory risk disclosures in 2005 and the explicit requirement for human capital information in 2020. They found a 20% increase in A&R-based human capital disclosures after 2005 and a 40% increase in A&R information since the 2020 rule change. In both instances, the largest gains were at companies that previously reported abnormally low information about their workforce turnover.

"The results suggest that SEC mandates have made a meaningful impact on companies that might not have otherwise provided the information," Sensoy said.

The study demonstrates that, on average, human capital disclosures reveal substantial information and reflect current underlying workforce dynamics. The result has major implications for regulators considering requiring more granular and timely workforce disclosures. Although many investors may call for specific human capital mandates, such requirements across all companies could create costs that outweigh the benefits.

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