Issue Paper: Employee Relations

It has been said many times that a company's workforce is its most valuable asset. In our opinion, there is a positive and a negative aspect to that statement. Employees do indeed provide tremendous value to their employers, making substantial investments of time and energy, and even their health and safety. But employees are not simply "assets" on a balance sheet. When Starbucks announced a pay raise for its employees, Chairman and CEO Howard Schultz used the word "partners," and said that "trust, after all, must be earned one human connection at a time." "Partner" is much closer to the mark.

Whether you are the CEO of a retailer with thousands of employees that meet your consumers face to face, or of a business with no consumer-facing employees at all, all successful companies must take the welfare of their employees seriously.

In this essay, we provide brief accounts of how some companies are responding to certain key challenges in the very broad area of "employee relations," including the gender pay gap, minimum wage reform and union relations.

Our Approach

Domini's Impact Investment Standards are organized around the key stakeholder groups that corporations depend upon to operate and generate profits, with a focus on the key themes that we believe best capture the strength of each of these relationships. Our standards help to identify companies run by managers capable enough to operate profitably while taking into consideration multiple stakeholders and the environment.

Among these stakeholder groups, employees are perhaps the most critical. We believe that corporations that treat their employees well should, in the long run, attain high levels of employee loyalty, high levels of productivity, and low levels of turnover – all potentially substantial contributors to profitability.

We are therefore looking for companies that invest in the health and development of their employees, focusing on the following key themes:

- Fair and Just Compensation and Benefit Programs
- Commitments to Diversity in the Workplace
- Empowerment and Investments in Training
- Solidarity with Unionized Workforce
- Continuous Improvement in Health and Safety

The companies discussed below currently meet our standards for investment, unless otherwise noted. This essay touches on a handful of key employee relations issues. We do not address health and safety or treatment of workers in corporate supply chains, for example, two areas that are consistently important to our investment decision-making, nor do we address corporate programs to meet the needs of the disabled, such as **Microsoft's** innovative efforts to employ individuals with autism, or companies like **Eiffage**, a French construction company, where employees own 28% of the firm's shares. In this area, every company has a story to tell. We hope you find these interesting and informative.

Equal Pay for Equal Work

The tech industry has faced persistent criticism over a lack of diversity and, in particular, a lack of opportunities for women. According to a recent study by Hired Inc. of 3,000 employers and 15,000 applicants, there is a 7% salary gap between male and female software engineers at major corporations.

In 2016, in response to shareholder proposals from our colleagues at Arjuna Capital, **Apple, Intel, Microsoft** and **Amazon** revealed that they pay their male and female employees equally. **Facebook** and Alphabet Inc. (**Google**) also announced they pay equally, but have yet to release data. What wasn't included in these disclosures was information on how often women are promoted or if there are biases that may prevent women from being hired or moved into senior roles.

Google began a study of its employee practices after it found that its male engineers were promoted at far higher rates than female employees. Although anyone was invited to apply for a promotion, the company found that women were less likely to do so. The company found two academic studies that indicated that 1) girls don't raise their hands as often as boys when answering math problems, even though they have a higher rate of accuracy when they do; and 2) women don't offer up their ideas as often as men in business meetings, even though observers say their thoughts are often better than the many offered by their male colleagues. When one of the heads of engineering sent an email to his staff describing the two studies and reminding them it was time to apply for promotions, the application rate for women soared. In 2013, the company started a series of diversity training workshops designed to help employees recognize unconscious bias and, as of September 2014, more than half of Google's employees had attended.

In 2013, **Salesforce** CEO Marc Benioff started a program called the Women's Surge. The goal was to achieve 100% equality for men and women in pay and promotion, and to make sure that at least a third of all participants at all meetings were women. Benioff asked managers across the company to identify their top executives, who would then receive additional leadership training. In divisions where mostly men were nominated, Benioff told the managers to come back with a more diverse list. When Benioff found that many women at Salesforce were paid less than their male counterparts, the company began raising the salaries of underpaid women. In 2015, Salesforce spent about $3 million to bring the salaries of female employees up to the level of their male counterparts.

Minimum Wage Reform

Until the early 1980s, an annual minimum wage income in the United States, after adjusting for inflation, was above the poverty line for a family of two. Today, the federal minimum wage of $7.25 per hour, working 40 hours per week, 52 weeks per year, yields an annual income of only $15,080, below the federal poverty line for a family of two. This reality has sparked the "Fight for 15" movement, which has mobilized tens of thousands of workers in hundreds of cities across the country attracting widespread attention from the public, the media, legislators and companies.

A sustainable minimum wage can support economic growth and reduce income inequality, a key risk to our economy. In 2014, more than 600 leading economists, including seven Nobel Prize winners and eight former presidents of the American Economic Association, said the United States should raise the minimum wage and index it. They argued that increases in the minimum wage have had little or no negative effect on the employment of minimum wage workers and that some research suggests that a minimum wage increase could have a stimulative effect on the economy as low wage workers spend their additional earnings, raising demand and job growth.

Costco, which employs approximately 205,000 individuals, is notable for its commitment to fair wages and benefits. It pays its retail employees approximately $20 per hour (not including overtime), compared to the national average of $11. Eighty-eight percent of employees reportedly have company-sponsored health insurance and pay premiums that amount to less than 10% of the overall cost of their plans. According to press reports, Costco has consistently resisted Wall Street pressure to conform its pay practices to lower industry standards.

Costco's CEO, Craig Jelinek, wrote a public letter to Congress in 2013, urging it to increase the minimum wage: "We know it's a lot more profitable in the long term to minimize employee turnover and maximize employee productivity, commitment and loyalty." In 2016, Costco announced that it would raise wages for new and current entry-level workers to $13 an hour, up from $11.50. Costco has annual worker turnover of approximately 10%, considerably better than the retail sector's 60% average. Other CEOs have been vocal about the need to increase the federal minimum wage, including James Gorman, CEO of **Morgan Stanley**, and Ron Shaich, the CEO of **Panera Bread Company**.

A number of companies, including **Gap, Bed Bath and Beyond** and **Starbucks** have responded to this debate by announcing wage increases.

We'd like to see more companies publicly state their views on this critical issue. Working with other investors, we developed a new proposal asking companies to adopt and publish principles for minimum wage reform. We submitted our proposal to **Best Buy** and **Staples**, and had constructive conversations with management at both companies. Our discussions with Best Buy led to a withdrawal of the proposal when we were informed that the company's board of directors was overseeing a process already underway to further develop the company's position on wage levels within the company to ensure its employees have sustainable careers and the company continues to attract the best talent.

Operating Globally, Thinking Locally

As global investors, we must ground our evaluation of employee relations in local realities. It makes little sense, for example, to reward a company for offering a benefit that is legally required in its local market. It is also important for American companies that operate globally to be flexible and adapt their programs to local needs.

Starbucks, which employs more than 191,000 people in 68 countries, has used regional surveys and focus groups designed to identify its workers' greatest challenges. In the United States, this process identified health coverage, which the company has offered to full and part-time employees since 1988.

Starbucks also identified college tuition as a key challenge in the United States, and responded with a unique benefit -- it would pay for employees to get a four-year college degree online at Arizona State University. Any employee that works twenty hours or more a week and has the grades and test scores to gain admission to Arizona State is eligible for the program. The program was announced in 2014 and, to date, more than 6,000 employees have enrolled. The company hopes to have at least 25,000 employees graduate by 2025.

In Britain and China, housing costs were identified as the greatest challenges. In 2015, Starbucks began providing monthly housing allowances to full-time employees in China and interest-free loans to help its employees in the United Kingdom afford a rental deposit, a program it developed with Shelter, a housing charity. Starbucks will lend a maximum of one month's wages to employees who have been with the company for over a year, which the employee pays off over 12 months.

We are particularly interested in employee benefits that exceed local requirements. **Fujifilm**, of Japan, is notable for benefits that help its employees establish a healthier work-life balance, particularly parents. The company prohibits overtime working hours until a child starts elementary school at the age of six, exceeding legal standards by three years, and allows a six hour working day until a child starts third grade at the age of nine, exceeding the legal standard by six years. Fujifilm also offers three years of parental leave, exceeding the legal requirement of one year. The company also provides specialized benefits for elder care. The company began these programs in 2014 for a core business reason – they believed they needed a diverse workforce to create products that would appeal to consumers in a changing world.

In South Africa, we are particularly interested in companies' efforts to promote people of color, and to address the HIV/AIDS epidemic. **Tiger Brands**, a packaged goods company, was founded in 1920 and is headquartered in Bryanston, South Africa. Four people of color and two women serve on the company's ten-member board of directors, and three women, including one woman of color and two men of color, serve on the company's eleven-member executive management team.

In 2014, Tiger Brands invested almost R8 million ($592,000) in on-site clinic services. These include occupational health support, as well as limited primary healthcare, and is free to all permanent and temporary employees on site. One of the company's clinics is also open to the community. The company also offers HIV/AIDS support for employees. In 2015, 331 employees were voluntarily counseled and tested and 95% of employees who tested positive enrolled in the program.

A Brave New World

The modern workplace is changing. Although the fear that machines would replace workers has been present since the early days of the Industrial Revolution, those 19th century workers could not have anticipated the use of computers to manage the human work week.

A 2014 New York Times article highlighted a growing practice among retailers to utilize automated scheduling software, which can produce erratic schedules for employees. Such companies might provide notice of hours only a day or two in advance, dismiss employees mid-shift because the computer says sales are slow, or schedule employees for very late nights followed by very early mornings. After the story was published, **Starbucks**, the focus of the article, announced that it would change its scheduling practices and New York's Attorney General sent letters to thirteen retailers asking for information regarding their scheduling policies.

Some employers, like **Target**, post employee schedules ten days before the start of a work week, and don't use the on-call approach. **Costco** gives part-time workers at least a week's notice about their schedules, and **JCPenney** also has a policy against on-call scheduling. **Gap** phased out on-call scheduling in September 2015 and **L Brands**, the parent company of Victoria's Secret, also recently ended the practice.

We live in an interconnected world, where simple management decisions can have significant effects. Corporate policies regarding something as simple as scheduling worker shifts can become public controversies that can damage trust in a brand. Other employee policies can have direct impacts on public health.

In July 2015, **Chipotle** announced that it would offer hourly workers paid sick leave, paid vacation and tuition reimbursement, benefits that were previously only available to salaried workers. These policies are both admirable and uncommon among restaurant chains. They also make good sense for Chipotle's consumers, who are put at risk when sick people come to work because they cannot afford to stay home. Only five months after announcing these new benefits, however, more than 140 Boston College students picked up norovirus from a sick worker who wasn't sent home. In 2015, almost 500 people fell ill after eating at Chipotle restaurants due to E. coli and norovirus outbreaks. In the wake of this crisis, which battered the company's stock price, the company took action to enforce its sick leave policy and to add new programs to extend sick leave when circumstances warrant.

Union Representation

The right to form or join a union of one's choice and to bargain collectively for the terms of one's employment are among the core conventions of the International Labor Organization and are recognized as fundamental human rights. Healthy and vital unions play a crucial role in addressing the imbalances in power that often arise between corporate management and workers in their struggle for fair working conditions.

Union relations can be contentious, but strikes can be a sign of a healthy union. These issues can therefore be difficult to evaluate, and rarely lead us to exclude a company from our portfolios, unless we see a pattern of unethical or illegal behavior.

In some cases, however, a lack of unionization can be a decisive factor for us. Take, for example, two similarly situated companies – **United Parcel Service** and **FedEx**. Historically, we have approved UPS for our portfolios, and excluded FedEx. At UPS, approximately 60% of employees are represented by the Teamsters. With the exception of its pilots, however, the vast majority of FedEx employees are not affiliated with a union, and FedEx has lobbied aggressively to stave off unionization. FedEx drivers are independent contractors and can start at $30,000-35,000 a year with no overtime, no retirement plan, no health-care benefits and only one week of vacation per year. By contrast, a full-time unionized UPS driver starts at a base of $39,000 a year, with regular raises up to $52,000. Overtime pay brings the total to more than $80,000 a year for the majority of drivers, along with a full benefits package.

In many ways, the FedEx approach is the precursor for many “sharing economy” companies like **Uber** and **AirBnB**. FedEx’s model has been challenged in a number of court cases over the years, and the company has responded by reorganizing aspects of its business to avoid unionization by its drivers.

Whole Foods has long resisted any attempts at unionization, despite the fact that employees of grocery chains, like **Kroger**, are generally represented by the United Food and Commercial Workers Union. John Mackey, the company’s co-CEO and co-founder, says the company isn’t “so much anti-union as beyond unions.” While Mackey’s sometimes aggressive anti-union rhetoric is a concern, we take comfort in the fact that Whole Foods takes employee benefits seriously and has, in some cases, responded to unionization efforts by increasing benefits. Whole Foods employees pay between $0 and $20 per paycheck for health insurance, depending on company tenure. Employees are also allocated up to $1,800 a year for personal wellness accounts to be spent at their discretion. The company rewards teams for coming in under budget and distributes a monthly surplus that averages about 6% of total wages. As a further commitment to solidarity with its workforce, the company caps its executive salaries at no more than nineteen times the average worker’s pay.

In the United States, with a few exceptions, like **Macy’s**, it is uncommon to see unionized employees at retail chains. American retail workers are more likely to belong to a union if they work for companies based in Europe. In August 2016, for example, employees at eight Zara locations in New York chose to join the Retail, Wholesale and Department Store Union. Zara is owned by **Inditex** of Spain, one of the world’s largest retailers. The company offered no resistance and agreed to recognize the union, stating that “this is a normal consequence of our commitment regarding the rights of freedom of association worldwide.” Similarly, there have been unionized employees at **H&M** (Hennes & Mauritz, Sweden) locations in the U.S. since the 2000s.

Of course, unions are not always respected at the American workplaces of European companies. In 2007, we co-filed a shareholder proposal with **FirstGroup**, a transportation company based in Scotland, to address allegations of anti-union activity at First Student, the company’s U.S. school bus subsidiary. The proposal was submitted along with the International Brotherhood of Teamsters, the Service Employees International Union, and more than 140 FirstGroup employees. Domini’s participation was critical in allowing the unions to meet the onerous British filing requirements. We then attended a meeting in London with FirstGroup’s CEO and chairman to discuss our concerns. FirstGroup hired a independent monitor to oversee its U.S. operations and ensure it was meeting its obligations to respect its workers’ rights, a program that is being held out as a potential model for other companies. Although we cannot claim sole credit for this important development, we have been told that investor involvement (including a large group of European pension funds) was a turning point in the engagement.

Domini

Domini asks SEC for Better Employee Relations Disclosure

The Securities and Exchange Commission requires publicly traded corporations to disclose the number of people they employ, but that is only the bare beginning of what we'd like to know. In 2016, the SEC requested public comments on its disclosure rules and asked whether companies should be required to disclose more information about their employee base. We submitted a lengthy letter, including the following requests for employee information:

- Employee turnover rate, including significant layoffs
- Breakdown between domestic and foreign employees
- Breakdown of full-time, part-time, seasonal and sub-contracted employees
- Diversity information, including gender pay ratio data
- Percentage of employees represented by a union. For companies with significant union representation, provide a narrative discussion of its process for engagement with the union, noting any significant disputes.
- Benefits and incentive structures available to all full-time employees
- Company goals regarding diversity, employee training and retention, and efforts to implement these goals
- Significant pending legal proceedings, or regulatory investigations, including fines or judgments awarded, relating to employee management.

Investors are well-advised to pay attention to how the companies they invest in treat their employees. By doing so, they can gain fresh insights into the quality of corporate management teams and identify those companies that are best positioned to compete in a rapidly changing marketplace. More importantly, however, by raising these questions with corporate managers, investors send the message that employees matter. When large companies take this seriously, and invest in their employees, they can create lasting value with ripple effects throughout our globally connected economies.

About Domini Impact Investments

Domini Impact Investments manages mutual funds for individual and institutional investors who wish to create positive change in society by integrating social and environmental standards into their investment decisions. **Visit www.domini.com or call 1-800-582-6757 to learn more.**

As of 3/31/17, these companies represented the following percentages of each Fund's portfolio: Domini Impact Equity Fund: Amazon (3.45%), Apple (2.53%), Best Buy Co Inc (<0.01%), Chipotle (0.28%), Costco (<0.01%), Gap (<0.01%), Alphabet Inc (Google) (2.93%), Intel (2.48%), J. C. Penney (<0.01%), Kroger (<0.01%), L Brands (<0.01%), Microsoft (1.02%), Morgan Stanley (<0.01%), Staples (<0.01%), Starbucks (<0.01%), Target (<0.01%), United Parcel Service (<0.01%), Whole Foods (<0.01%). Domini Impact International Equity Fund: Fujifilm Holdings Corp (0.10%), Tiger Brands (0.34%). Domini Impact Bond Fund: Microsoft (0.24%), Morgan Stanley (0.61%) (general obligation corporate bonds). FedEx and AirBnB are not approved for investment by any of the Domini Funds. Uber is privately held. The following companies were not held as of 3/31/17: Bed Bath and Beyond, Eiffage, Facebook, FirstGroup, H&M, Inditex, Macy's, Panera Bread Company, Salesforce.

The composition of each Fund's portfolio is subject to change. Visit www.domini.com for a complete description of each Fund's portfolio.

The Domini Funds are not insured and are subject to market risks, such as sector concentration and style risk. Investing internationally involves special risks, such as currency fluctuations, social and economic instability, differing securities regulations and accounting standards, limited public information, possible changes in taxation, and periods of illiquidity. Investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. You may lose money.

The Domini Impact Bond Fund is not insured and is subject to market risks, including interest rate and credit risks. During periods of rising interest rates, bond funds can lose value. The Domini Impact Bond Fund currently holds a large percentage of its portfolio in mortgage-backed securities. During periods of falling interest rates, mortgage-backed securities may prepay the principal due, which may lower the Fund's return by causing it to reinvest at lower interest rates. Some of the Domini Impact Bond Fund's community development investments may be unrated and carry greater credit risks than its other investments.

The Domini Funds maintain portfolio holdings disclosure policies that govern the timing and circumstances of disclosure to shareholders and third parties of information regarding the portfolio investments held by the Funds.

This commentary should not be deemed an offer to sell or a solicitation of an offer to buy the stock or bonds of any of the companies noted, or a recommendation concerning the merits of any of these companies as an investment.

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Before investing, consider the Funds' investment objectives, risks, charges, and expenses. Visit www.domini.com or call 1-800-762-6814 for a prospectus containing this information. Read it carefully.

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