Wal-Mart’s Labor Problem:
Limits to the Low-Road Business Model

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Introduction

Two thousand and twelve, the year of Wal-Mart’s 50th anniversary, has proven to be a momentous year for the world’s largest retailer, though not in the way company officials anticipated. This year, in the wake of a major scandal involving the apparent violation of the Foreign Corrupt Practices Act, the company, faced an unprecedented revolt of shareholders, with roughly a third of outside shareholders voting against current CEO Mike Duke, former CEO Lee Scott, Chairman Rob Walton, and Audit Committee Chair Chris Williams.

During the 2012 fiscal year, Wal-Mart’s same-store sales turned positive, a welcome development after nine consecutive negative quarters, and in the second half of the calendar year the company’s stock price experienced one of the strongest runs in years. But this apparent success may not be an indicator of any fundamental turnaround: the company’s same store sales are still negative on a 3-year basis, and the company’s stock returns year-to-date are merely on par with those of the S&P 500 Retail Index.

And with signs that the company is facing increased unhappiness among Wal-Mart associates, there may be major challenges in the company’s future. As the national political debate has, over the past year, turned to questions of income inequality and corporate influence in politics, Wal-Mart’s low wages and its impact on US manufacturing brought unwelcome attention to the company’s business model. Meanwhile, the extreme wealth of the Walton family heirs, and their own right wing political activism, has seemed to underscore the company’s role in generating inequality of both wealth and power. Whatever the outcome of this national political debate, it would appear that as a consumer company with one of the most recognized brands in the world, Wal-Mart currently faces a significant level of risk. So do its investors.
Wal-Mart workers on strike

On Thursday October 4th, 2012, 70 Wal-Mart associates walked off the job at nine stores in the Los Angeles area. After a period of relative quiet in the preceding several months, and a series of attempts to reach out to company executives, workers throughout Wal-Mart’s distribution chain have begun to respond more forcefully to the company’s increasing retaliation against worker efforts to raise standards at the company. Meanwhile the risk of continued labor conflict, and the potential impact it may have on the company’s reputation, casts a shadow over the Wal-Mart’s plans to ramp up a new phase of small-format growth in US urban markets.

“Workers like myself have been calling on the company to address issues with scheduling, benefits, wages and above all, respect in the workplace. But instead of being responsive, Wal-Mart has lashed out at us for speaking up. The company is trying to silence and intimidate us through unfair disciplinary actions, cutbacks in hours and even firings. We’re on strike to protest these illegal attempts to silence us,” said Venanzi Luna, a striking Wal-Mart associate from Los Angeles.

The retail store worker’s strike in Los Angeles follows two separate strikes by workers in Wal-Mart-controlled warehouses in Southern California and Illinois, where workers had long complained of systematic wage theft, health and safety dangers, and abusive conditions on the job. In both cases, and in the retail store strikes as well, the precipitating event appears to have been the company’s retaliation against workers who tried to speak out.
Retaliation against associates
Wal-Mart recently fired several workers active in the Organization United for Respect at Walmart (OUR Walmart), despite a promise from Wal-Mart’s Senior Vice President of Global Labor Relations that the company would not retaliate against workers who join the organization. Other workers have been intimidated by store managers.

Over the past few months, in response to these reprisals, dozens of Unfair Labor Practice (ULP) charges have been filed by OUR Walmart on behalf of OUR Walmart members who have experienced retaliation for their activities with the organization. These ULPs fall into three general categories:

- **Terminations**: workers have been terminated by Wal-Mart in retaliation for their participation in OUR Walmart
- **Threats**: workers have been threatened with loss of job or store closings in retaliation for their activities with OUR Walmart
- **Reduction in hours**: retaliatory reduction of hours for workers who have been involved with OUR Walmart

These abuses have come in a larger context where managers have been waging an anti-OUR Walmart propaganda campaign in stores around the country, complete with a corporate-produced slide show playing in an endless loop in break rooms, and which depicts OUR Walmart as a front group trying to steal associates’ money.

Low staffing continues to impact operations
Many of the concerns raised by OUR Walmart members boil down to hours and staffing levels, and appear to be directly related to the significant cost cutting Wal-Mart executives have been pursuing. Over the past several years Wal-Mart management has emphasized the apparent success of what it calls the “productivity loop” whereby expense reductions are used to fund investments in price, which are intended to increase traffic and sales, which then presumably provide the basis for further investments in price. While a large portion of these expense reductions have come from removing labor from the stores, management has consistently asserted these cuts have not impacted operations or customer service. Indeed, in August Wal-Mart touted new labor saving technologies which they say will allow the company to reduce headcount.
Wal-Mart claimed the out-of-stock problem had been addressed through a “new” inventory and stocking system, but few associates appear to have been informed of this new system.


without impacting customer service. But frontline Wal-Mart associates from across the country have disputed this contention by company executives. The stores are, they believe, struggling to manage day to day operations without adequate staffing.

A year ago, after Wal-Mart associates and industry analysts first began to argue that the company was suffering a significant number of out of stocks, the company acknowledged it had been experiencing a problem, changed the metric it used for measuring in-stock levels and claimed the problem had been addressed through a “new” inventory and stocking system, but few associates appear to have been informed of this new system. Wal-Mart associates continue to observe significant problems related to understaffing. Over the past month many associates have documented these problems with photos (printed throughout this report).

“Wal-Mart has cut employees’ hours and cut the labor costs to a point where it actually is harming not the just the workers, but it affects the operations day to day of the store and it also affects the customers,” Lori Amos, a 16 year Wal-Mart associate, told Reuters.

With the planned ramp-up of the Neighborhood Market format, Wal-Mart executives are doubling down on their bare-bones-staffing strategy.

Despite these challenges, Wal-Mart executives appear to be extending the low-staff model even further with the planned re-launch of the company’s Neighborhood Market format, which, according to management statements and press reports, is able to achieve higher returns on investment through significant reductions in staffing as well as minimized construction costs in the initial building phase. Whether or not this will work remains to be seen, but what is clear is that Wal-Mart executives, rather than investing in more associates and higher levels of customer service, are doubling down on their bare-bones-staffing strategy.
Workforce investment is profitable

Despite Wal-Mart executives’ insistence on cost cutting, the members of OUR Walmart’s demand for improved staffing is not inconsistent with a desire for profitable business. Contrary to popular managerial belief, which holds that payroll at low-cost retailers should be kept as low as possible, recent research shows that spending more on staffing, in terms of wages, hours and training, can help rather than hurt a retailer’s bottom line. In a study of four low-cost retailers, Costco, Trader Joe’s, Quiktrip, and Spanish supermarket chain Mercadona, Professor Zeynep Ton of MIT’s Sloan School of Management found that these four chains, which invest substantially more in training and payroll than their peers, also have substantially higher asset and labor productivity than similar companies with leaner payrolls. These companies, which operate using what Ton calls a “virtuous circle,” generally provide full-time jobs with room for advancement, above-industry wages, and predictable schedules, and they experience lower turnover and higher sales per labor hour than peers. Customer service at these stores also receives notably higher ratings than the industry as a whole.4

According to Wharton School researchers, every additional dollar of payroll added to a store, on average, increased revenue by $10, and for some stores that were particularly understaffed, the revenue lift was as high as $28.

Deteriorating customer service

If the national surveys are accurate, consumers generally do not like shopping at Wal-Mart, and the issues cited by customers who dislike their experience in Wal-Mart stores appear to be directly related to staffing problems.

University of Michigan’s American Consumer Satisfaction Index (ACSI) ranked Wal-Mart last among Discount and Department Stores in 2011, with a score that had decreased 4.1% since the previous year and 12.5% since 1994.4 (ACSI uses data from customer interviews in an econometric model to score customer satisfaction on a 1-100 scale.) Notably, Wal-Mart’s score declined from the low 80s 15 years ago, to the high 60s in 2011; and from consistently above the average for Department & Discount stores to consistently below during that time period. This deterioration in relative performance is consistent with Wal-Mart associates’ perception of declining job security and increasing stress.

Similarly, researchers Marshall Fisher, Serguei Nettesine and Jayanth Krishnan at the Wharton School found in an analysis of 17 months of data for a large retailer that the impact on revenue of increased store staffing is “incredibly high.” According to Marshall, “on average, revenue increased by $10 for every additional dollar of payroll added to a store, and for some stores that were particularly understaffed, the revenue lift was as high as $28.”5

Wal-Mart Veteran 'Loves the Company,' Wants Change

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GOEBEL: "OUR WAL-MART" HAS THOUSANDS OF MEMBERS IN 600 U.S. WAL-MART STORES

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that there has been a significant change in the company’s approach regarding customer service.

Similarly, Wal-Mart performs badly in its grocery business compared with other supermarkets.

Meanwhile, Consumer Reports ranked Wal-Mart second-to-worst among supermarket chains in its most recent survey of the industry, in which 24,203 people participated. Consumer Reports found that Wal-Mart received the lowest marks for service. 7 Similarly, in a separate Consumer Reports survey of shoppers at general retailers, a category including Wal-Mart, Sam’s Club, and eight other clothing and general merchandise retailers, Wal-Mart received the lowest score and Sam’s Club was ranked 8th, while Costco took the top spot. Consumer Reports noted that “Wal-Mart shoppers were especially likely to complain about long checkout lines and inadequate customer service.” 8
Health and safety risks

Many Wal-Mart associates believe the low staffing levels contribute to safety risks at the company, and clearly Wal-Mart management has struggled with safety violations in its stores, at times resulting in an unsafe working environment for employees and an unsafe shopping environment for customers. The company has had particular trouble managing safety risks on Black Friday.

In November 2008, a 34-year-old temporary Wal-Mart employee was trampled to death early in the morning on Black Friday at a Supercenter in Valley Stream, New York. OSHA cited the company in 2009 for inadequate crowd management, issuing a meager $7,000 fine for the incident. The citation was upheld in March 2011, after the company spent more than $2 million on legal fees contesting the fine, arguing that crowd trampling should not be considered an occupational hazard that retailers have a responsibility to try to prevent.

Though there have been no reported deaths at Wal-Mart during Black Friday since the fatal accident in 2008, Black Friday violence and trampling continue to occur at Wal-Mart stores around the country. The Associated Press reported that in 2011, there were violent incidents in at least nine Wal-Marts around the country in which 24 people were injured. In one case, an off-duty police officer used force that made a 54-year-old man fall to the ground and lose consciousness. The man had put a video game in his pants to free his hands to help his young grandson, who had been trampled, when police approached the man, accused him of shoplifting, and knocked him to the ground.

In 2012, Wal-Mart was charged sizable penalties by OSHA for repeat safety violations in two separate instances, totaling $418,000. Given that the maximum civil penalty from OSHA for a non-repeat “serious violation” is a mere $7,000, the fines issued to Wal-Mart stand out as especially sizeable. The larger of the penalties (related to blocked emergency exits, lack of safety procedures for control of power hazards and other problems), issued in February for $365,500, would have been only $77,500 if Wal-Mart had not already been recently cited for similar violations at other locations in 9 states. In a survey of notable cases resulting in similar penalties for repeat violations issued by OSHA between April 2011 and February 2012, SafetySmart Compliance, an OSHA compliance guide website, the $365,000 February fine stands out as the second-largest on the list. In an analysis of the case, law firm Markhoff & Mittman, P.C. states that “Wal-Mart has been cited for similar violations over the years and safety risks do not seem to be improving in some locations.”

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Wage and hour violations

While Wal-Mart executives proudly boast of the company’s relentless pursuit of labor expense reductions, the company’s history of systematic wage and hour law violations in the United States has been extensively documented. The company took the visible and costly step of settling 63 pending wage and hour class-action lawsuits for a maximum of $640 million in December of 2008. Since then, it has settled at least seven more class-action wage-and-hour cases for an additional $345 million. The company also paid $5.3 million in back wages and civil penalties to 4,500 Vision Center employees in a case settled with the Department of Labor in May 2012. The DOL found that Wal-Mart had misclassified the workers as exempt from the Federal Labor Standards Act’s overtime requirements, illegally denying them overtime pay.

In its most recent Form 10-K filed with the Securities and Exchange Commission, Wal-Mart disclosed that it remains a defendant in “numerous” wage and hour class actions, and has continued to appeal a ruling in one such suit. The case in question, Braun/Hummel v. Wal-Mart, went to trial in 2007, at which point the plaintiffs were awarded $187.6 million in compensation and lawyers’ fees – the largest class action verdict in the state’s history. In June 2011, an appeals court found that the $45.8 million awarded in lawyers’ fees as part of the verdict may be too high and needs to be recalculated. Wal-Mart plans to take the case to the Pennsylvania Supreme Court, but if the 2007 award is upheld, this would bring Wal-Mart’s total costs for wage and hour class-action settlements and verdicts up to $1.18 billion since December 2008.

Gender, race, disability and religion

Wal-Mart continues to face formidable challenges in court related to gender discrimination in pay and promotions. Although class certification in the Dukes v. Wal-Mart national class action was blocked by the Supreme Court in summer 2011 for technical reasons, two regional class-action complaints have been filed, in California and Texas. In June 2012, the plaintiffs’ counsel and co-counsel also announced that nearly 2,000 individual charges in 48 states and in every Wal-Mart region have been filed with the Equal Employment Opportunity Commission alleging gender discrimination in pay and promotions.

Wal-Mart’s reputation has also taken a hit for other recent discrimination and harassment lawsuits. Between June 2006 and August 2012, Wal-Mart has settled at least 9 EEOC cases for $13.4 million related to disability discrimination, gender discrimination, racial discrimination, religious discrimination and sexual harassment. The most notable of these settlement occurred in March 2010, when the company paid $11.7 million to settle an EEOC class-action case alleging that a Wal-Mart distribution center in Kentucky systematically denied jobs to female applicants and used gender stereotypes to fill entry-level positions. Non-EEOC lawsuits related to discrimination have also resulted in formidable costs for the company, including a $17.5 million settlement in 2009 for a class-action lawsuit in which plaintiffs claimed that Wal-Mart discriminated against African-American truck driver applicants. Also in 2009, the Massachusetts Supreme Judicial Court unanimously upheld $2 million in compensatory and punitive damages against Wal-Mart in a gender discrimination suit.
Violations in Wal-Mart’s supply chain

Public scandals and legal violations continue to occur at Wal-Mart contractors and sub-contractors throughout the company’s supply chain, both in supplier factories and in warehouses that store and move goods sold at Wal-Mart.

According to a recent report by the National Employment Law Project, in the Inland Empire, labor violations in the warehousing industry are widespread, including lack of overtime pay, piece rate pay schemes that only lead to compensation for select portions of work performed, illegal and falsified pay records, and hazardous workplace conditions.

The logistics industry

In the case of the logistics industry, a recent wave of regulatory citations and worker unrest at multiple of Wal-Mart’s national warehousing hubs has created uncertainty for the smooth distribution of goods in the United States.

In Southern California’s Inland Empire and in the Chicago area, warehouse worker advocates have found conditions in the industry to be deplorable and in many cases illegal. Southern California and Elwood, Illinois, are central hubs of Wal-Mart’s vast national distribution system, making it one of the largest clients of the warehousing and logistics industry in these regions.

Wal-Mart’s distribution system relies upon the use of third-party contractors in shipping and storing, and these companies in turn rely largely on the labor of temporary workers dispatched through staffing agencies. According to a recent report by the National Employment Law Project, in the Inland Empire, labor violations in the warehousing industry are widespread. Violations found include lack of overtime pay, piece rate pay schemes that only lead to compensation for select portions of work performed, illegal and falsified pay records, and hazardous workplace conditions. NELP goes on to argue that despite Wal-Mart’s high degree of involvement in setting the parameters for working conditions at its warehousing and logistics contractors’ facilities, “outsourced workers laboring on Wal-Mart’s behalf toil at the bottom of a complex hierarchy of intermediaries and in alternative employment schemes that leave them vulnerable to significant worker rights abuses and unsure where to seek redress,” while Wal-Mart “skirts responsibility” for the impacts of its business model on these workers because they are not direct company employees.

In response to these conditions, Warehouse Workers United (WWU), a group of warehouse workers in the Inland Empire, and Warehouse Workers for Justice (WWJ), a similar organization in the Chicago area, have united hundreds of workers in Wal-Mart warehouses in an effort to raise standards in the industry. Recent actions taken
by WWU have exposed the poor labor practices utilized by Wal-Mart’s contractors and subcontractors in the Inland Empire, putting these companies in significant financial and legal risk. WWU has reported health, safety and labor violations at Wal-Mart-controlled warehouses to Cal/OSHA and the California Labor Commissioner, which has led to inspections at multiple facilities resulting in over $1.3 million in citations. Penalties so far include:

- $499,000 to a subcontractor for failure to provide itemized wage stubs
- $616,250 to a subcontractor for failure to provide proper wage statements
- $256,445 to two subcontractors for multiple safety violations

The two larger penalties are connected to violations at Wal-Mart’s largest distribution center in the region, run by Schneider Logistics.

The organization filed another complaint over unsafe conditions at a separate Wal-Mart-controlled facility in the region in July 2012. WWU and WWJ have also assisted workers in filing multiple class-action lawsuits against staffing agencies and warehouse operators in California and Illinois over the past several years.

In addition to these lawsuits, workplace unrest in Wal-Mart’s logistics and warehousing supply chain in Southern California, Illinois and New Jersey is growing significantly, as these contracted and sub-contracted workers have started to identify ways to hold Wal-Mart responsible. Warehouse workers and ally organizations have explicitly identified Wal-Mart as a major client in these warehouses, and national and international publications, including the New York Times and the Guardian, have published features about the warehouse workers’ struggles. In addition, the workers have argued in court, with preliminary success, that staffing agencies and warehouse operators are jointly liable for labor and safety violations in warehouses. Given Wal-Mart’s level of involvement in the day-to-day operations of the facilities, it seems likely that the worker organizations might eventually demonstrate that Wal-Mart also has liability for legal and regulatory violations at the warehouses, since it acts as a joint employer in many cases. Lastly, the extensive problems at Wal-Mart-controlled facilities are explicit violations of Wal-Mart’s own Standards for Suppliers. WWU filed a formal ethics complaint with the company over this issue in August 2012.

More significantly, in September warehouse workers in both Southern California and Illinois engaged in separate work stoppages in protest against retaliatory actions taken against workers’ attempts to stand up for their rights and address the problems in the Wal-Mart-controlled warehouses. On October 1st, 600 community supporters converged on one of the striking warehouses in Elwood, Illinois and were met by riot police. Seventeen people were...
arrested for civil disobedience and the warehouse was forced to shut down for the day. Striking warehouse workers in Southern California returned to work on September 28th; striking warehouse workers in Illinois.

**Wal-Mart’s suppliers of goods**

Recent reports by whistleblowers and outside observers reveal that many Wal-Mart suppliers of goods around the world also continue to violate local laws and Wal-Mart’s Standards for Suppliers. Scott Nova, corporate social responsibility expert and Executive Director of the Worker Rights Consortium, calls Wal-Mart “the leading corporate contributor to the persistence and pervasiveness of abusive and exploitative labor conditions in global export manufacturing.”

Workers’ rights organizations from around the world continue to uncover new labor violations in Wal-Mart’s supply chain, suggesting systemic, widespread failures in Wal-Mart’s prevention and handling of these issues. Recent notable cases:

In April 2012, the National Guestworker Alliance uncovered pay violations, excessive overtime and forced work at **C.J.’s Seafood**, a crawfish supplier in Louisiana employing Mexican guestworkers that sold 85% of its product to Wal-Mart. In July, the Department of Labor levied $248,000 in fines, back wages and damages against the company because of serious safety violations, willful violation of laws regarding the use of temporary foreign workers, lack of overtime pay, illegal wage deductions and pay below the minimum wage. The New York Times published multiple stories about the C.J.’s case, including an editorial on July 8, 2012, “Forced Labor on American Shores.” The piece pinpointed the nexus between Wal-Mart’s ruthless cost-cutting efforts and rights abuses at suppliers: “When companies force suppliers to slash costs, corners will be cut and workers will be abused.”

The National Guestworker Alliance also reported in June 2012 that in a survey of 18 other U.S. Wal-Mart suppliers utilizing H2-B guestworkers, 12 of them had accrued 622 federal citations for safety, health, and wage and hour violations since the 1980s as well as “dozens of federal lawsuits alleging significant violations of civil and labor rights law.” Eight of the 12 companies had accrued one or more of these violations since 2005.

In April 2012, workers at **Phatthana Seafood**, a shrimp processing plant in Songkhla, Thailand, went on strike to protest human trafficking and poor working conditions. Phatthana is part of **PTN Group**, and PTN Group’s shrimp is distributed by **Rubicon Resources LLC**, a large Wal-Mart supplier. Most of the workers at Phatthana are migrants from Cambodia and Myanmar, and the factory allegedly confiscated the workers’ passports, held the workers in debt bondage, and paid them so little that they could not afford to eat. Similar reports also came to light around the same time regarding a Wal-Mart pineapple supplier in Kanchanaburi, Thailand, **Vita Foods**. When Human Rights Watch confronted Wal-Mart about these issues, the retailer simply denied that Phatthana has ever supplied shrimp to Wal-Mart, despite documented evidence that shrimp from the company was sold on Wal-Mart’s shelves in the United States as well as Wal-Mart’s own past advertisement of its relationship with Rubicon as a “sustainable” supplier.

Other reports of serious labor violations at Wal-Mart suppliers all over the world continue to surface, including recent reports of serious pay, labor rights, and safety violations in China and Jordan.
Wal-Mart continues to struggle with reputation problems

Bad news about worker treatment, discrimination and legal compliance issues has a material impact on Wal-Mart’s ability to appeal to customers. A confidential report prepared for Wal-Mart by McKinsey in 2004, at a time when the company was being barraged by complaints from labor and environmental organizations about its irresponsible practices, found that up to 8% of Wal-Mart customers surveyed had stopped shopping at the store because of “negative press they had heard.”57

A sampling of other brand rankings reveals continued challenges to Wal-Mart’s stature:

Harris Interactive annually asks a sample of Americans to identify the 60 most visible companies and then surveys to rate those companies’ reputations. In 2012, Wal-Mart ranked 41 out of 60, trailing many of its competitors like Amazon (#4), Kohl’s (#16), Costco (#19) and Target (#27). Not only did it lag behind this group of competitors, but Wal-Mart’s ranking dropped while the others’ rose.58

On Fortune’s list of the most admired companies in the world, Wal-Mart dropped 13 places in 2012, falling to #24.59

Amplicate, a social media analytics firm, declared Wal-Mart “the least loved department store on social media.” Complaints made about the company focused on working conditions, “low salaries, low quality products and poor customer service.”60

Wal-Mart’s response to its reputational blunders in recent years has cost the company hundreds of millions of dollars and has taken up executives’ valuable time, even though the root cause of its poor reputation – an internal culture of non-compliance – has yet to be addressed. Untold hours have been spent by top-level Wal-Mart personnel in an attempt to soften the company’s image, however in the wake of the widely publicized Mexico bribery scandal61 Wal-Mart’s most recent 10-Q notes that the bribery allegations and resultant investigations “may require the involvement of certain members of the Company’s senior management that could impinge on the time they have available to devote to other matters relating to the business.”62
Spending related to reputation and branding has also increased significantly. Wal-Mart’s annual advertising budget has steadily increased in recent years, excluding a small dip in FY2012. Even including the slight recent decline, the company’s advertising budget in FY2012 was 44% larger than it was in FY2006 and 138% larger than it was in FY2004. Q1 and Q2 2013 reports noted that the advertising budget also increased in these two quarters. The company’s charitable giving, an issue that the company’s public relations materials heavily emphasize, has skyrocketed in recent years. The total dollar value of cash and in-kind giving from Wal-Mart and the Wal-Mart Foundation globally in FY2012 was $958.9 million, up 564% from FY2004 (the earliest year data is available on the company’s website).

Abusive conduct hinders growth efforts

Regenerating strong sales growth at Wal-Mart US will depend to a great degree on successful new store openings. However, at the start of this century, the major greenfields for Wal-Mart’s future growth were urban America – the Northeast, West Coast, and Chicago. Wal-Mart has saturated much of rural and suburban America to such a degree that it is cannibalizing its own stores in many of those areas. In 2009 Wal-Mart’s then-Vice Chairman, Eduardo Castro-Wright, proclaimed that Wal-Mart could increase its sales by $80-$100 billion via expansion into America’s urban markets. He went on to say that Wal-Mart had in place a robust real estate program to go after that opportunity.

Castro-Wright’s observation wasn’t the first time that Wal-Mart had identified this opportunity. Earlier in the last decade the company had made a push to build stores in Chicago, New York City and Los Angeles – among the largest retail markets in America—only to be greeted with stiff opposition from residents and leaders of those communities who were uninterested in welcoming Wal-Mart and its poor labor practices.

In 2006 USA Today described Chicago as “…the epicenter of a debate around wages at large retailers ever since the city rejected a proposal by Wal-Mart Stores Inc. to open a store on the South Side…” The Chicago City Council went as far as passing an ordinance, later vetoed by the Mayor, requiring big box stores like Wal-Mart to pay a minimum wage of $10 along with at least $3/hour worth of benefits.

In 2004, in Inglewood, a city in the LA metro area, after opposition from elected officials to the opening of a new store, the company put forth a ballot initiative in an effort to exempt itself from zoning and environmental restrictions. However, residents rejected the proposal with 60% saying no to Wal-Mart.

In 2005 after a failed effort to open its first store in New York City, then-CEO Lee Scott told New York Magazine: “I think New York will be good for us and we’ll be good for New York.” And make no mistake, he added emphatically, “We will be in New York.” After that first failure in Queens the company turned its eye to Staten Island. Yet once again, it found itself facing significant opposition. This quote from a Staten Island resident encapsulates the challenge Wal-Mart faced “we need this Wal-Mart like a hole in the head … this is a corporation that has a lot of baggage about how it treats its employees.” Two years later with still no stores in the city, Scott told reporters and editors from the New York Times that “I don’t care if we are ever here [New York City].”

After succumbing to this string of defeats the company began an offensive to remake its image, spending millions of dollars on advertising, increasing charitable giving, and undertaking a number of public initiatives on the environment, food deserts, healthy food and women’s empowerment to name a few. In FY2012 Wal-Mart and the

Wal-Mart’s former-Vice Chairman, Eduardo Castro-Wright, proclaimed the company could increase its sales by $80-$100 billion via expansion into America’s urban markets.
Wal-Mart Foundation gave $872.7 million in cash and in-kind gifts in the United States. Often these initiatives were undertaken in the same cities in which its earlier efforts to open stores had failed, all with an eye toward reducing opposition to future store openings.

As expected the company again refocused on urban America with a hope that its rebranding effort would stick. But it didn’t. Even while it was handing out millions of dollars in grants in cities around America residents raised concerns about who Wal-Mart really was and what it would mean for their communities.

In New York City, after rumors began that Wal-Mart was negotiating with developers in Brooklyn, residents quickly mobilized and formed Wal-Mart Free NYC. To date the coalition has successfully blocked the company’s entry into this site even though it requires no political approval. Crain’s New York Business opined in early 2012 that Wal-Mart’s “window of opportunity is closing” in New York City and cited the opposition of labor unions as a contributing factor. And when rumors began to circulate about Wal-Mart’s interest in Queens, the developers of that property quickly issued a press release asserting that “We have not had any talks with Wal-Mart…and we have no intention of discussing this site with them.” The New York Observer reporting on the issue titled its story “Just How Desperate Is Wal-Mart to Open in New York – And Have They Lost All Their Allies?” A major setback for the company occurred in September when it lost its bid to open a supercenter at the Gateway II site in Brooklyn; the location will instead be occupied by a unionized grocery store.

Another city the company has long courted is Washington DC. In 2010, Wal-Mart announced that it had selected four sites to open stores in the city – that number later grew to six – with a plan to open stores in late 2012. Like New York, a coalition opposed to Wal-Mart, Respect DC, rallied to confront the company. In April of 2012 Wal-Mart reset the opening of the stores to the end of 2013 “… after facing some resistance from activists and opponents…” And in an August report from this year a reporter updated Wal-Mart’s status this way: “Now with the clock ticking down on 2012, just one of those six sites has begun construction, another has been reduced to a gaping hole in the middle of a retail corridor, and the remaining four are only in the permitting process.” The article went on to note that some residents opposed Wal-Mart because of the wages and working conditions of its employees.

In the Boston metro area the company recently abandoned plans for two stores saying that the projects no longer made financial sense. The council president of one of the towns “…said he believes residents’ strong negative reaction to a Wal-Mart store in their town influenced the retailer’s decision to put aside its plans.”

The company’s current plans to open its Neighborhood Market format in major metropolitan centers may cause further community relations problems as its business model is based on reducing the number of employees staffing the stores as well as spending less on initial construction costs. These elements of the Neighborhood Market strategy appear to undermine one of the primary selling points company officials have used in appealing to community groups and elected officials in urban markets across the US—that Wal-Mart will bring needed jobs.
A failure of governance

Wal-Mart’s apparent failure to institute rigorous internal controls that would prevent the kind of legal and regulatory violations the company has become known for has significant implications for investors. The company’s reputation continues to suffer from reports of wage and hour violations, race and gender discrimination, retaliation against worker organizing efforts, as well as the recent Mexico bribery scandal. This lack of effective internal controls is not a new issue, and investors identified it almost ten years ago, and the company’s long-standing failure to address it has only increased the negative consequences for investors. Those negative consequences include increased costs from judgments, settlements and fines and the accompanying legal fees and also harm to Wal-Mart’s reputation. The negative reputation garnered from the compliance failures limits the company’s ability to expand both domestically and internationally, while the operational effects of lax internal controls are reflected in worker and customer dissatisfaction.

A history of shareholder engagement

In 2005 and 2006, a group of Wal-Mart shareholders made a concerted attempt to engage with the Board of Directors about the company’s pattern of flagrant law-breaking, the Board’s lack of oversight of these issues, and their potential risks to investors. The group of large institutional investors involved was led by New York City’s then-Comptroller William C. Thompson, Jr. and included the New York City Pension Funds, the Illinois State Board of Investment, the California State Controller, F&C Asset Management, Hermes and Universities Superannuation Scheme. At the time, the four groups collectively owned 11.5 million shares of Wal-Mart stock worth $545.8M.

Concerned about “recent reports of legal and regulatory non-compliance,” the funds’ primary request was that the Wal-Mart Audit Committee establish a sub-committee of independent directors with the assistance of outside counsel to review Wal-Mart’s internal controls designed to ensure compliance with laws, regulations, and company policies, reporting directly to shareholders. The Committee refused this request, calling the shareholders’ concerns “neither necessary nor appropriate.” The investor group then sent a detailed disclosure request to the Committee – covering Wal-Mart’s internal controls, whistleblowing policies, workforce management systems, supplier code of conduct compliance, and compensation systems – which the Committee never meaningfully addressed.

The investor group found Wal-Mart’s response to the engagement to be overly general and insufficient, resulting in no changes to Wal-Mart’s policies related to legal and regulatory compliance or the oversight and disclosure of these issues. The list of questions that the investor group sent to the Audit Committee, in November 2005, suggests that many of the public and legal scandals the company has faced in the intervening years might have been prevented if the Committee had given the issues meaningful deliberation when confronted then.

The negative reputation garnered from compliance failures limits the company’s ability to expand both domestically and internationally, while the operational effects of lax internal controls are reflected in worker and customer dissatisfaction.

After the failed dialogue, the investor group filed a resolution for consideration at the 2007 shareholder meeting. The resolution called upon the Board of Directors to “issue a report on the social and reputational impacts of reported and known cases of management non-compliance...” A representative of one of the institutional investors stated that “weaknesses in internal controls have eroded the company’s reputation ...[and] We fear that its failure to deliver on these policy commitments is inhibiting Wal-Mart’s ability to expand into new domestic markets.”

Wal-Mart’s Labor Problem

Limits to the Low-Road Business Model
After the Mexican bribery scandal, the current New York City Comptroller reminded investors that “Wal-Mart's board has repeatedly rebuffed our office and the New York City Pension Funds when we have raised concerns over the company's failure to comply with legal and ethical standards.” It is important to note that the Mexico bribery scandal, only made public in a New York Times exposé in April 2012 and described below in more detail, took place between September 2005 and early 2006, concurrent with the investor group's attempts at engagement over compliance issues with the Audit Committee. An internal Wal-Mart memo released by the New York Times suggests that then-chair of the Audit Committee, Roland Hernandez, was notified of the bribery scandal by November 16, 2005. Since the unsuccessful attempt to engage with the Audit Committee, shareholders have taken other types of action to signal to the Board that Wal-Mart's lack of internal controls pose serious long-term risks to investors. These actions include shareholder proposals, no votes on candidates for the Board of Director voting, divestiture, and shareholder lawsuits.

Internal compliance controls continue to fail

In the seven years since New York City Comptroller and others pursued dialogue with Wal-Mart's Audit Committee about its insufficient internal controls, numerous public reports of internal scandals and legal and regulatory violations have occurred. The potential costs of these violations are likely a weight on the company's stock price. The list of recent violations bears a striking resemblance to the list of legal and regulatory issues facing the company when the Comptroller approached the Audit Committee in 2005 – it includes allegations of legal violations by high-level executives, violations of U.S. retail workers' legal rights, and gross discrepancies between Wal-Mart's Supplier Code of Conduct and the realities of working conditions at Wal-Mart's suppliers.

Mexican bribery scandal

Most prominent of the many public scandals Wal-Mart is currently embroiled in is related to allegations of bribery at its Mexican subsidiary, Walmex. In a New York Times exposé in April 2012, it was revealed that top Wal-Mart executives allegedly covered up whistleblower reports of the widespread use of bribes of Mexican officials totaling $24 million to facilitate new store openings between 2002 and 2005. As a result of these allegations, Wal-Mart is under investigation by the Department of Justice, the Securities and Exchange Commission, and multiple Mexican agencies. The company has also retained outside counsel to conduct an expanded internal investigation into FCPA compliance in countries believed to be “higher-risk” for corruption: Mexico, China, Brazil, India and South Africa. These countries represent large operations for Wal-Mart (Mexico, China, Brazil, South Africa) as well as countries with immense growth potential (China, Brazil, sub-Saharan Africa, India). Curiously, the scope of the investigation, which is overseen by the company's Audit Committee (itself implicated in the cover-up), does not include Argentina.

U.S. Representatives Elijah E. Cummings, Ranking Member of the House Oversight and Government Reform Committee, and Henry A. Waxman, Ranking Member of the House Energy and Commerce Committee, launched a Congressional investigation into the allegations on April 23, 2012.

Wal-Mart spent $34 million and $51 million in expenses related to FCPA investigations in the three and six months ending July 31, 2012, respectively, with the expectation that it will spend and additional $70-$80 million in the following two quarters. The federal investigations, related subpoenas and requests for testimony and information, and shareholders lawsuits also pose the risk of a variety of negative consequences, as outlined in
Walmex’s Q2 2012 Financial Statement Notes.\textsuperscript{102} Past FCPA fines in other cases have amounted in some cases to around 1\% of a company’s sales – in Wal-Mart’s case equal to $4.5 billion.\textsuperscript{103}

The bribery allegations have also resulted in close to a dozen shareholder lawsuits against Wal-Mart, its executives and its Directors, including one securities class action and multiple derivative lawsuits. In the company’s latest quarterly filing, it was noted that the bribery allegations may result in “ongoing media and governmental interest in these matters that could impact the perception among certain audiences of its role as a corporate citizen.”\textsuperscript{104}
1 “Notes from the WMT Back-to-School Tour: Basics 101,” Stifel Nicholas, August 1, 2012.
3 http://www.chicagotribune.com/business/sns-rt-us-Wal-Mart-employeesbre8901b1-20121001,0,1608484.story
19 Seven settled wage-and-hour class action cases since December 2008 include: Smith/Ballard v. WM, USDC, Northern Dist. of CA, 3/16/06; Salvas v. WM, Superior Ct., Middlesex County, MA, 8/21/01; Braun v. WM, 1st Judicial Dist. Ct. Dakota County MN, 9/12/01; Savaglio v. WM, Superior Ct. of CA, Alameda County, 2/6/01; Savaglio v. WM, Superior Ct. of CA, Alameda County, 2/6/01; Moore v. WM, USDC, Dist. of OR, 12/7/05, and a $3 million settlement paid directly to the Commonwealth of


23 Wal-Mart Stores Inc. form 10-Q, filed September 6, 2012.


30 http://www.workforce.com/article/20091007/NEWS01/310079999


33 Ibid.


46 http://www.salon.com/2012/10/03/wal_mart_warehouse_strike_heats_up singleton/

47 Scott Nova, Testimony to the Competition Tribunal of South Africa in the case of the large merger between WAL-MART STORES and MASSMARKET HOLDINGS LIMITED, November 2010.


62 Wal-Mart Stores Inc. form 10-Q, filed September 6, 2012.

63 Wal-Mart Stores, Inc. Forms 10-k, filed March 26, 2006 and March 27, 2012.

64 Wal-Mart Stores Inc. forms 10-Q, filed June 1, 2012 and September 6, 2012.


84 Ibid.
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