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EMPLOYMENT ISSUES

Recent Diversity Requirements In Financial Services

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The calls for diversity to be a business priority and fundamental component of corporate governance are increasing. In the new year, financial services companies in the United States are responding to regulators' requests for information regarding the diversity of their workplaces. Virtually every major financial services regulatory agency has implemented in recent years guidelines and requirements for increased diversity in their operations, resulting, in many cases, in surveys and other requests for information regarding these issues.

In the United States, employment decisions based on protected characteristics and quotas requiring the hiring of women or minorities is generally unlawful. The move toward mandating the appointment of women and minorities on company boards and increasing the representation of underrepresented minorities in the workforce is nevertheless picking up pace.

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The most recent regulatory agency seeking disclosure of diversity-related information is the New York Department of Financial Services (DFS). Financial services and other employers have been scrambling to respond to these mandates and wondering how they interact with laws prohibiting employment discrimination.

Let's review the recent legal developments.

DE&I Disclosure: A Global Trend

The trend in recent years has been an emphasis on and investment in diversity, equity and inclusion (DE&I), resulting, in part, from the #MeToo movement and Black Lives Matter. This trend has every indication of continuing. The majority of the workforce is looking for employers to make measurable commitments in these areas. Regulators and legislators have responded by pursuing required mandatory disclosures of related information.

These events are not unique to the United States. An early example can be found in the United Kingdom, where, effective in April 2018, the Equality Act 2010 (Gender Pay Gap Information) Regulations 2017 required private sector employers with 250 or more employees to publish an annual "gender pay gap report" covering the mean and median average hourly pay by gender for relevant employees; the proportion of women and men in each of four pay quartiles; the gender bonus gap; and the proportion of male and female employees who received a bonus in the same 12-month period.

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Similarly, in Australia, the Workplace Gender Equality Act has required private sector employers with 100 or more employees to report statistics by gender on remuneration, workforce composition and the recruitment, promotions and resignations of their employees to the federal Workplace Gender Equality Agency.

And since 2019, all France-based employers with 50 or more employees are required to publish an annual report which must indicate the pay gap between men and women and the number of employees of the under-represented sex among the ten highest-paid employee.

In 2020, California adopted a Pay Data Reporting law requiring private employers with 100 or more U.S. employees and at least one employee in California to annually report on employees within designated pay bands based on gender and race/ethnicity.

Although some disclosure laws have been in place for several years, the impact on gender pay equity has been inconsistent at best. (In October 2021, Australia and the U.K. had the largest gender pay gap according to the Global Institute for Women's Leadership at King's College London, surveying frameworks in Australia, France, South Africa, Spain, Sweden and the United Kingdom. See Cowper-Coles et al., *Bridging the gap? An analysis of gender pay gap reporting in six countries* (October 2021). Spain and France had the smallest gender pay gaps, respectively.)

Recent U.S. Disclosure Laws and Rules

Following a trend of increasingly robust disclosure requirements, a number of U.S. laws mandate either the disclosure of the presence of women and minorities in certain discrete roles or their actual retention.

One of the earliest such laws is the 2018 California Board Gender Diversity Law, which requires corporations listed on the major U.S. stock exchanges with principal executive offices located in California, with at least five directors, to have at least two female directors; and three if the corporation has six or more directors. Violations may result in a $100,000 fine for the first violation, and $300,000 for each subsequent violation. California adopted a similar law related to board members from underrepresented communities in 2020.

New York state followed in July 2020 with its Women on Corporate Boards Study Act, requiring all public and private for-profit business corporations authorized to do business in the state to inform the Secretary of State of the number of directors on their Board and how many are women. The Department of State will publish its findings on its website on Feb. 1, 2022 and follow up every four years.

More recently, in August 2021, the U.S. Securities and Exchange Commission (SEC) approved a rule proposed by the Nasdaq stock exchange requiring most companies listed on the exchange to disclose annually aggregated statistical information about board members' gender, race, ethnicity, and LGBTQ+ status, in a format prescribed by Nasdaq.

The rule defines "diverse" for the purpose of compliance as a director who (1) self-identifies as female, without regard to his or her designated sex at birth; (2) who self-identifies as Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, or two or more races or ethnicities, or (3) who is lesbian, gay, bisexual, transgender or a member of the queer community (using the acronym LGBTQ+). Under the Nasdaq rule, companies are required to either meet certain thresholds or explain why they failed to do so.

The most recent laws follow this "comply or explain" requirement and suggest a larger trend that we can expect to continue.

Financial Services Directives

Specifically in the world of financial services, there have been several notable developments in diversity disclosure rules.

In 2015, pursuant to the Dodd Frank Wall Street Reform and Consumer Protection Act, a sea of federal bank regulatory agencies—the Office of the Comptroller of the Currency (OCC); Board of Governors of the Federal Reserve System (Board); Federal Deposit Insurance Corporation (FDIC); National Credit Union Administration (NCUA); Bureau of Consumer Financial Protection (CFPB); and Securities and Exchange Commission (SEC)—issued an interagency policy statement establishing joint standards for assessing the diversity policies and practices of the entities they regulate, as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

The Policy Statement encourages regulated employers to develop a "process to create and maintain a positive work environment that values individual similarities and differences, so that all can reach their potential and maximize their contributions to an organization." It defines "diversity" as Black Americans, Native Americans, Hispanic Americans, Asian Americans and women, but was meant to be flexible and can be broadened by companies. Specifically, the framework recommends publicly and

internally stating the organizational commitment; providing training; taking proactive steps to promote a diverse pool of candidates and selection of senior management; publicizing employment opportunities; creating relationships with minority organizations; creating a culture that values the contributions of all employees; and encouraging a focus on these objectives.

More recently, in July 2021, the New York Department of Financial Services (DFS), which regulates banks and trust companies, savings banks, savings and loans, credit unions, investment companies, foreign banking institutions, and many other financial services entities in New York state, issued an industry guidance entitled "Diversity, Equity and Inclusion and Corporate Governance."

Noting her "broad statutory authority" as set forth in the New York Banking Law to "require any banking organization to make special reports to her at such times as she may prescribe," the DFS superintendent stated that the guidance was intended to "outlin[e] DFS's expectation that New York-regulated financial institutions make the diversity of their leadership a *business priority* and a *fundamental component of their corporate governance*."

The DFS guidance applies to DFS-regulated banking institutions with over $100 million in assets, non-depository financial institutions with over $100 million in gross revenue, and all entities authorized to engage in virtual currency business activity. It requires, among other things, that employers respond to a survey which requests information concerning whether the entity has a written diversity policy; how often the entity's senior management reports on diversity related efforts to its board; the race and gender of each board member and each member of senior management; and "additional information you find relevant."

DFS plans to publish the results on an aggregate basis in the first quarter of 2022; "strongly encourages" companies to publicly disclose this information; and says that it will consider disclosing the information, perhaps on a disaggregated basis, in the future.

Demonstrating A Commitment to DE&I

As noted above, in the United States, quotas requiring the hiring of women or minorities are generally unlawful. Making individual employment decisions based on protected status generally remains unlawful, unless the decisions are part of a policy that is temporary in nature and that responds to a goal of remedying past discrimination. Choosing between two equally qualified employees based solely on their gender, for example, is never permissible.

Nevertheless, companies can take steps to demonstrate to regulators that they are serious about DE&I, not only on their boards but throughout their workforce. In recruiting and promoting, it may be advisable for employers to adopt diverse slates requirements. They should make sure that the standards and methods of the recruitment and promotion processes are clear, neutral, and unbiased.

Other appropriate initiatives include training on issues such as unconscious bias; establishing career advocacy programs which pairs high-performing employees with influential leaders to help them develop the skills and visibility needed to progress in their careers; and organizing affinity groups, which can provide diverse employees with a platform to expand and develop professionally.

Management Buy-In

Key to demonstrating a commitment to DE&I is demonstrating management buy-in, i.e., top-to-bottom, consistent messaging emphasizing inclusion and respect, showing the workforce that these are important goals, that participation is expected and evaluated, and equipping the entire employee population with tools to succeed.

This may include DE&I and unconscious bias training, workshops, forums and facilitated discussions, and incorporating these key concepts and messaging in other initiatives.

Workforce Assessment

A common obstacle to undertaking diversity initiatives is not knowing where to begin. Assessments can be undertaken based on quantitative or qualitative information.

An assessment of an organization's current composition and practices can begin with an analysis of demographic information. A threshold requirement for these types of analysis is the underlying data, which can generally include demographic information (collected through voluntary self-identification surveys), HRIS data, and performance management data. The analysis can focus the trends in hiring, workforce composition, promotion, in terms of gender, race/ethnicity, LGBTQ+, and perhaps other factors. However, to assure that the audit and results are privileged and

thus not discoverable in any litigation, these analyses should be carried out by counsel, or at counsel's direction.

In addition to the results-focused analysis of a quantitative assessment, employers are sometimes also interested in measuring belonging sentiment through employee surveys. However, such surveys can be quite risky because they may (unintentionally) seek information related to discrimination and harassment, be discoverable in litigation and may trigger an obligation to investigate. If an organization is considering these types of surveys, it should explore the related risks fully in order to make an informed decision and, if the surveys are undertaken, the format, questions, and messaging should be thoughtfully crafted.

Pairing Objectives With Initiatives

Many employers are tempted to take a results-focused approach to DE&I. However, an overemphasis on the results (i.e., changes to the demographic composition of the workforce), may tempt managers to make decisions based on protected characteristics and, therefore, increase the risk of discrimination claims. Instead, initiatives can be designed to address a component of DE&I, with the initiative itself being the point of emphasis.

For example, many employers have adopted aspirational goals for diverse hiring. Without corresponding policy or practice changes, however, it may be difficult to achieve the hiring objective and may even expose the organization to unnecessary risk of discrimination claims. Instead of emphasizing the results in recent hiring trends alone, employers should undertake initiatives targeted at the intended results through a review of the recruitment process. Specifically, such an initiative could seek to identify obstacles to equal employment opportunity, broaden the applicant pool, revise the content of job postings and descriptions, reconsider job qualifications, adopt requirements for diverse slates of candidates and/or assemble diverse hiring panels. These initiatives can also be adapted to address board of director composition, which has also been receiving increased attention.

Another area of focus has been retention, especially with the recent labor shortage. Employee resource groups (ERGs) can be an effective tool in increasing inclusion and belongingness and, therefore, retention, especially for underrepresented groups. ERGs generally relate to underrepresented communities, such as race, ethnicity, gender, LGBTQ+ and have a business purpose. (However, an employer can adopt a policy that categorically does not allow religious or political groups, as such groups tend to be more divisive then inclusive.)

In terms of advancement, instead of simply adopting an aspiration goal for the demographic composition of management or senior leaders, employers can develop initiatives intended to equip high performing employees with the skills, resources, and encouragement needed to advance. Mentoring programs focus on these considerations, can be tailored to specific organizations, and often have significant impact.

Employers can work with inclusion, equity, and diversity specialists on developing policies and initiatives aimed at improving diversity at all levels of the organization—including at the C-Suite and board levels, although the attorney-client privilege and work product doctrine would only apply when working with counsel with appropriate privilege protocols in place.

Conclusion

Diversity is undoubtedly a worthy goal for employers. Its importance is only increasing with respect to business priority and corporate governance. Notwithstanding the legal challenges in the United States to making employment decisions based on gender, minority status, and other protected characteristics, regulators continue to apply pressure to adopt practices designed to increase the diversity of boards, senior management, and the workforce at large.

Employers can and should take lawful steps to increase inclusion, equity and diversity and demonstrate, to regulators, investors, employees, customers, and other stakeholders, their commitment to these principles.

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