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Federal Financial Regulatory Agencies Poised to Implement Diversity Standards

By George Barbatsuly and Joshua Rinschler

Acting under a little-analyzed provision of the Dodd-Frank Act, six federal financial regulatory agencies recently published joint-proposed standards for assessing the diversity policies and practices of the institutions they regulate. In their current form, the standards would impose significant new reporting obligations on the more than 70,000 entities regulated by these agencies, including financial institutions, investment banking firms, mortgage banking firms, asset management firms, brokers, dealers, financial services entities, underwriters, accountants, and investment consultants. While the standards are broad, their purpose remains unclear, and the agencies have not explained how they plan to use the information submitted under them. The comment period for these proposed standards has been extended to February 7, 2014, and regulated entities that have not yet provided comments may wish to do so to ensure that their views are heard before the standards take effect.

The Proposed Diversity Standards

Section 342 of the Dodd-Frank Act, 12 U.S.C. § 5452, requires each of six federal financial regulatory agencies – the Consumer Financial Protection Bureau, Office of the Comptroller of the Currency, Federal Reserve Board of Governors, Federal Deposit Insurance Corporation, National Credit Union Administration, and Securities and Exchange Commission (“Agencies”) – to establish an Office of Minority and Women Inclusion (“OMWI”). Under the statute, each OMWI is responsible for all matters of the agency relating to diversity in management, employment, and business activities, and is required to develop standards for assessing the diversity policies and practices of entities regulated by the agency.

On October 25, 2013, the Agencies jointly published proposed standards for assessing the diversity policies and practices of the institutions they regulate (“Proposed Standards”). A stated goal of the Proposed Standards is to “promote transparency and awareness of diversity policies and practices within the entities regulated by the agencies.” Under the standards, the Agencies would evaluate the diversity policies of regulated entities across four broad categories: (1) organizational commitment to diversity and inclusion; (2) workforce profile and employment practices; (3) procurement and business practices and supplier diversity; and (4) practices to promote transparency of organizational diversity and inclusion.

- **Organizational commitment to diversity and inclusion.** Relevant considerations in this category would include whether a regulated entity makes diversity and inclusion considerations in employment and contracting an important component of its strategic plan; whether the entity has a diversity and inclusion policy that is approved and supported by senior management and the board of directors; whether the entity provides regular progress reports on diversity initiatives to the board and/or senior management; and whether equal employment and diversity education and training are conducted on a regular and periodic basis.

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- **Workforce profile and employment practices.** Relevant considerations here would include whether a regulated entity is using data (such as required filings with the Equal Employment Opportunity Commission (“EEOC”)) to evaluate and assess workforce diversity and inclusion efforts; whether it holds management accountable for such efforts; and whether it has policies and practices, such as outreach to minority and women organizations, that create diverse applicant pools for internal and external opportunities.
- **Procurement and business practices and supplier diversity.** In this category, the Agencies would consider whether a regulated entity has a supplier diversity policy that provides a fair opportunity for minority- and women-owned businesses to compete in procurements of business goods and services; methods to evaluate and assess its supplier diversity; and practices to promote a diverse supplier pool such as outreach to minority- and women-owned contractors.
- **Practices to promote transparency of organizational diversity and inclusion.** Relevant considerations in this category would include whether a regulated entity makes information about its diversity and inclusion activities publicly available on an annual basis through its website, in promotional materials, and in annual reports to shareholders.

The Proposed Standards would apply to all entities that these six Agencies regulate – some 70,000 financial institutions, investment banking firms, mortgage banking firms, asset management firms, brokers, dealers, financial services entities, underwriters, accountants, and investment consultants. Although the Agencies state that the Proposed Standards may be tailored to take into consideration an institution’s size and other characteristics (such as total assets, number of employees, governance structure, revenues, number of members or customers, contract volume, geographic location, and community characteristics), the Agencies do not specify how these characteristics will be considered.

The Agencies envision an assessment process that includes: (1) a self-assessment in which a regulated entity uses the Agencies’ standards to conduct an evaluation of its diversity and inclusion policies and practices; (2) the entity’s voluntary disclosure of the self-assessment results to the appropriate Agency; and (3) the entity’s voluntary disclosure of information about its efforts to comply with the standards on its website and in annual reports and other materials.

The Proposed Standards do not address what actions the Agencies plan to take if an entity’s diversity and inclusion policies and practices are found to be deficient. Section 342 of the Dodd-Frank Act expressly provides that any diversity standards under the statute are not to be construed “to mandate any requirement on or otherwise affect the lending policies and practices of any regulated entity, or to require any specific action based on the findings of the assessment.” 12 U.S.C. § 5452(b)(4). However, despite this statutory language, the Proposed Standards state that the Agencies may use the information disclosed by regulated entities as a “resource in carrying out their diversity and inclusion responsibilities.”

Concerns with the Proposed Standards

The Agencies have requested comments on all aspects of the Proposed Standards, and more than 50 comments have been submitted to date. While the commenters have largely praised the goal of workplace diversity that Section 342 embodies, a number of regulated entities and other organizations have identified some serious concerns with how the

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Agencies are proposing to implement these goals through the Proposed Standards. Among the more prevalent concerns are the following:

- Lack of a clearly defined goal. The proposed standards set forth “transparency and awareness of diversity policies and practices within the entities regulated by the agencies,” but they do not define the term “diversity,” nor do they provide guidance on how regulated entities are expected to measure their progress in this area.
- Lack of clarity in how the Agencies will use the information disclosed. As noted above, Section 342(b)(4) of the Dodd-Frank Act expressly provides that any diversity standards are not to be construed to mandate any requirement on or otherwise affect the lending policies and practices of any regulated entity, or require the Agencies to take any specific action based on the findings of the assessments. However, under the Proposed Standards, the Agencies may use any information disclosed “as a resource in carrying out their diversity and inclusion responsibilities,” although no detail is provided regarding the nature of these responsibilities. Exactly how the Agencies will use this information as a resource, and what other agencies or organizations may be privy to the information, are questions that the Proposed Standards do not answer.
- Unclear consequences of non-participation. While Section 342(b)(4) states that the diversity standards contemplated by the statute are not intended to mandate any requirement on any regulated entity, the Proposed Standards are drafted prescriptively and do not clearly state that they are intended to be voluntary. They likewise fail to make clear what, if any, adverse consequences will flow to a regulated entity that chooses not to participate in the Proposed Standards or provide information pursuant to them.
- Duplication and potential conflicts with other laws. Some commenters have noted that existing law already advances the goals embodied in the Proposed Standards. For example, government contractors are already required to file Employer Information Reports (i.e., the “EEO-1” reports) that contain data on the employment diversity at regulated entities. Employers are also subject to a number of federal and state mandates prohibiting workplace discrimination against protected classes. Indeed, Section 342 explicitly requires that diversity efforts be undertaken in a manner “consistent with applicable law.” 12 U.S.C. § 5452(c)(2). However, some commenters have expressed concern that the Proposed Standards could be viewed as mandating diversity outcomes that the Dodd-Frank Act does not require and encouraging discrimination against members of groups that diversity policies are not intended to benefit.
- Practical compliance challenges. Some commenters have also focused on the practical difficulties in implementing and complying with the Proposed Standards. For example, whereas the Proposed Standards state that one of the evaluation categories is whether the regulated entity “has methods to evaluate and assess its supplier diversity,” including various metrics and analytics, many regulated entities simply lack the authority or practical ability to obtain the data needed to evaluate the diversity of suppliers and other service providers. Even where pertinent data is available to a regulated entity, the costs of data management and analysis can be substantial.
- Public access to the information disclosed. Commenters have also highlighted the fact that information disclosed under the Proposed Standards will be publicly available. Indeed, the Proposed Standards expressly state that they are aimed at “facilitating greater awareness and transparency of the diversity policies and practices of regulated

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entities” and are intended to “provide the public a greater ability to assess diversity policies and practices of regulated entities.” For example, the self-assessment model outlined in the Proposed Standards envisions that regulated entities will publicly disclose their own internal self-assessments, implicating privilege issues. Regulated entities will also be expected to make detailed metrics and demographic information available to the public, which could raise privacy concerns and put sensitive and confidential business information at risk.

- Increased litigation risk. Public disclosure also presents the risk of increased litigation against regulated entities. Under the Proposed Standards, the plaintiff’s bar would have ready access to detailed self-assessments and employment metrics that can be used to shape discrimination lawsuits against employers. Other federal government agencies, such as the EEOC and Office of Federal Contract Compliance Programs, will be able to more closely scrutinize regulated entities and perform disparate impact studies with the demographic information that regulated entities would need to make publicly available. In particular, the public availability of such information appears to fit neatly within the EEOC’s ongoing “Systemic Initiative,” in which that agency has made the identification, investigation, and litigation of cases alleging class or company-wide discrimination as a top enforcement priority.

Comment Period Extended

The comment period for the Proposed Standards has been extended until February 7, 2014. In addition to seeking comments on the proposal generally, the Proposed Standards highlight several specific questions commenters are encouraged to address, including: whether the Proposed Standards are effective and appropriate to promote diversity and inclusion; whether the Proposed Standards are sufficiently flexible to allow meaningful assessments of a wide range of entities; and whether there are other factors that would be useful in assessing the diversity policies and practices of regulated entities. The Proposed Standards can be accessed at the link at the bottom of this alert, and detailed instructions on how to submit comments to each agency can be found at pages 2-8 of the Proposed Standards. Regulated entities that have not yet commented on the Proposed Standards may wish to do so at this time to ensure that their views are heard before these potentially significant reporting obligations take effect.

The attorneys in the Labor, Employment and Workplace Safety group at K&L Gates are available to assist clients in the formulation of their comments. We are also available to assist clients in formulating appropriate compliance and risk-avoidance strategies if the Proposed Standards take effect in their current or substantially similar form.

[Click here to view the proposed standards.](#)

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