

Publications

In Depth: Financial Regulators Issue Policies and Practices for Diversity

Related Professionals

Nelson D. Cary

Related Services

Corporate and Business Organizations

Labor and Employment

Related Industries

Financial Institutions

AUTHORED ARTICLE | Summer 2015

Published in the Summer 2015 issue of *The Bankers' Statement*

On June 9, 2015, the Federal Reserve, OCC and FDIC (as well as the SEC, CFPB and NCUA) issued a final interagency joint policy statement (JPS) establishing standards for assessing the diversity policies and practices of the entities they regulate.

Background

This JPS stems from Section 342 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act), which required each agency to establish an Office of Minority and Women Inclusion (OMWI) to take responsibility for issues relating to diversity in areas such as workforce management, employment and business activities. The final JPS closely resembles the October 25, 2013 proposed regulations, which received more than 200 comments. In sum, the JPS advises financial institutions to be committed to diversity in a number of areas, while detailing reporting standards and various ways for institutions to be transparent about their diversity-related policies.

Impact

Importantly, the JPS states that adherence to the JPS is voluntary and that the JPS will be used for “*assessing an entity's diversity policies and practices...*” in the referenced areas of interest. It also states that the agencies' approach to the assessments “*would not be part of the examination or supervisory process.*” It stresses that what it refers to as a “model assessment” involves a self-assessment by the institution of its diversity policies and practices using the proposed standards, voluntary disclosure of the self-assessment to the agencies, and “publication” of the institutions' diversity efforts in order to increase public awareness.

Also importantly, the JPS states that, while not part of the examination or supervisory process, the “*agencies may periodically review public information to monitor diversity and inclusion practices and reach out to regulated entities to discuss diversity and inclusion.*”

The JPS provides that (1) the policies and practices are not to be part of the examination process, (2) the agencies recognize the unique characteristics of institutions and their markets and communities, and (3) the JPS does not impose new legal requirements on regulated entities. But despite these assurances, the financial services industry should be aware that new agency policy initiatives can and often do result in issues that “creep” into the examination and oversight process in a de facto sense. And outsiders sometimes tend to use policy initiatives such as these to not only assess the dedication of institutions to the concepts of diversity and inclusion but to leverage these concepts as “best practices” and/or as de facto legal requirements in a manner not intended or formally provided by the policy initiatives.

As a result, irrespective of the caveats provided by the agencies, most institutions would be wise to treat the JPS seriously and as providing a requirement to undertake the referenced assessments in their organizations, and should be prepared to respond to regulatory as well as community inquiries.

Despite the agencies’ good intentions and the emphasis in the JPS that the process is not part of the examination process and does not provide new legal requirements for institutions, like many things in the financial services industry the law of unintended consequences may well apply. Therefore, any “policies” developed as a result of the JPS should be carefully crafted in order to anticipate the likelihood that they will, in fact, be sought for review by the agencies on an “informal” basis, and perhaps requested by community groups. They could also show up in various types of litigation against the institution, various aspects of CRA analysis, or become the basis for the award of governmental banking services. Local governments might also seek to leverage the “policies” in response to public pressure from community groups. Policy “standards” often take on a life of their own in the financial services industry, no matter how “voluntary” and well-intended they may be.

There is a long history of policy statements and voluntary regulatory suggestions morphing into de facto requirements for organizations in the financial services industry, and this particular policy statement may well provide significant fodder for further issues and challenges in an already-strained industry.

The JPS

Initially, the JPS defines several key terms, including “diversity,” “minority,” and “inclusion.” Specifically, “diversity” refers to women and minorities. “Minority” refers to African Americans, Native Americans, Hispanic Americans and Asian Americans. Importantly, financial institutions can incorporate broader definitions, though on its face, the JPS does not cover certain groups often protected under federal and state equal employment opportunity (EEO) laws, such as those with disabilities. “Inclusion” is defined as 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.”

The JPS also notes that the agencies formulated the standards recognizing that “each entity has unique characteristics, such as its governance structure, workforce size, total assets, contract volume, geographic location and community characteristics.” It also recognizes that the standards may be “tailored and used in a manner reflective of an individual entity’s size and other characteristics.” While helpful, the result is that there may be a wide variety of interpretations of those caveats by competing institutions serving the same markets which may result in comparative challenges for the institutions, the agencies, and for the communities and other third parties reviewing the individual diversity policies of each institution.

The JPS provides standards for agency assessment of diversity policies on five fundamental subjects:

1. Organizational Commitment to Diversity and Inclusion: The standards focus on leadership of the organization. Financial institutions should:

- a. include diversity and inclusion considerations in employment and contracting as important part of strategic plan for recruiting, hiring, retention and promotion;
- b. have a diversity and inclusion policy approved by senior leadership/board;
- c. provide regular progress reports to senior leadership/board;
- d. regularly conduct training on EEO and on diversity/inclusion;
- e. utilize senior level official to oversee/direct diversity and inclusion efforts; and
- f. take proactive steps to promote a diverse candidate pool.

2. Workforce Profile and Employment Practices: The standards focus on promoting inclusion of women and minorities in the workforce. Financial institutions should:

- a. implement diversity and inclusion policies and practices that comply with law;
- b. ensure equal employment opportunities for all employees, and do not engage in discrimination based on gender, race or ethnicity;
- c. implement policies and practices that create diverse applicant pools (for internal and external opportunities), such as outreach to women and minority organizations, participation in diversity workshops, etc.;
- d. assess diversion and inclusion efforts (track data in terms of applicants, hiring, promotions, separations, career development and retention); and
- e. hold management accountable for diversity and inclusion efforts.

For financial institutions required to have affirmative action plans, the standards do have a significant degree of overlap with OFCCP requirements.

3. Procurement and Business Practices-Supplier Diversity: The standards focus on increasing outreach to women-owned and minority-owned businesses. Financial institutions should:

- a. implement a supplier diversity policy providing fair chance for women-owned and minority-owned businesses to compete for procurement of goods and services;
- b. develop methods to evaluate supplier diversity (e.g., look at annual procurement spending as well as percentage of contract dollars awarded to women-owned and minority-owned business contractors by race, ethnicity and gender); and
- c. develop practices to promote diverse supplier pool, including, for example, outreach to women-owned and minority-owned organizations.

4. **Practices to Promote Transparency of Organizational Diversity and Inclusion:** The standards focus on providing transparency to permit public access to policies and practices. Financial institutions should make available through a website (or other form of communication):

- a. strategic plan for diversity and inclusion;
- b. policy on commitment to diversity and inclusion;
- c. progress towards achieving diversity and inclusion in workforce and procurement activities; and
- d. opportunities available that promote diversity (e.g., current (and potential) employment and procurement opportunities, availability of mentorship and developmental programs for employees and contractors).

5. **Entities' Self-Assessment:** The standards focus on encouraging entities to perform self-assessments on their diversity and inclusion policies and practices. Financial institutions should use standards to:

- a. conduct an annual self-assessment of diversity policies and practices;
- b. monitor and evaluate performance under diversity policies and practices on ongoing basis;
- c. provide information relating to the self-assessments to the OMWI Director of the relevant federal financial regulator; and
- d. publish information regarding efforts relating to the standards.

Conclusions

Again despite the limitations and caveats set forth in the JPS, the industry has seen a plethora of non-binding, well-intended policies become de facto requirements and opportunities for agency and third-party leverage over the years through “regulatory creep,” “best practices,” and the unique vulnerability of financial institutions to reputation risk and politics in general.

Through the law of unintended consequences, policies such as those in the JPS tend to create reputation risk for institutions as well as legal risk by parties attempting to use the well-intended policies to pursue political goals or financial gain irrespective of the stated intent and limitations. The concept of “publishing” the self-assessment by an entity may well lead to misunderstanding of the voluntary nature of the JPS and a number of abuses by third parties as well as generating inappropriate attempted intervention in the internal affairs of the institution.

Despite its intent and “voluntary” compliance, hopefully the JPS does not add to the already-significant burden facing financial institutions as they struggle to climb out of the recent financial crisis and deal with the existing regulatory burden and the after-effects of the crisis.