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January 18, 2022

Acting Superintendent Adrienne A. Harris
New York Department of Financial Services
1 State Street
New York, NY 10004-1511

Re: ***Diversity, Equity and Inclusion and Corporate Governance***

Dear Acting Superintendent Harris:

I write on behalf of the Alliance for Fair Board Recruitment, a not-for-profit legal defense foundation that believes racial, sex, and ethnic classifications are unconstitutional, unfair, and harmful. This letter is to warn the Department of Financial Services (DFS) about serious legal and factual issues that plague ex-Superintendent Lacewell's proposed racially discriminatory disclosure program.

The policy requires regulated banking and financial institutions to report the gender, racial, and ethnic makeup of their boards and management with the intent of making "progress" towards diversity goals. This blatantly discriminatory policy violates the Fourteenth Amendment, federal anti-discrimination laws, and New York State law. Further, it will not even achieve the goals it claims to seek. The evidence Ms. Lacewell relies on is deeply flawed and does not show that discrimination will improve firm performance or workplace safety.

This is not the first time that Ms. Lacewell has apparently manipulated statistics to achieve illegal ends—she has also been accused of editing a nursing home report to hide a high COVID-19 death toll—but it should be the last.[1] This plan is unwise and unlawful and should not be pursued in its current form.

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According to the July 29th Industry Letter, written by then-Superintendent Lacewell, DFS has ordered reporting of the gender, racial, and ethnic makeup of New York Regulated Banking Institutions and Regulated Non-Depository Financial Institutions' boards and management so that DFS may collect and publish this data.[2] These efforts, Ms. Lacewell explained, are needed to address the "safety and soundness" of the industry. Further, Ms. Lacewell emphasized that this reporting is just "to start" and that firms must make "progress"

[1] J. David Goodman & Danny Hakim, *Cuomo Aides Rewrote Nursing Home Report to Hide Higher Death Toll*, NEW YORK TIMES (Mar. 4, 2021) https://www.nytimes.com/2021/03/04/nyregion/cuomo-nursing-home-deaths.html.

[2] *See* Industry Letter Re: Diversity, Equity and Inclusion and Corporate Governance, New York Department of Financial Services (July 29, 2021), https://www.dfs.ny.gov/industry_guidance/industry_letters/il20210729_diversity_equity_incl_corpgov.

towards diversity goals or else even more onerous discrimination will be required. Specifically, the letter goes on to explain that Ms. Lacewell has considered "quotas," a method that DFS has endorsed as "effective tools to ensure some diversity on corporate boards."[3]

Curiously, DFS does not ask banks to disclose information the American Association of Bank Directors (AABD) thinks is relevant to director performance, "such as experience, knowledge, banking backgrounds, educational levels, financial statement literacy, age, and record of integrity and independence."[4] Instead, in support of this program, the letter makes a number of claims about why diversity—and only diversity—is "good for the bottom line." She opines that, among other things, diversity results in increased profitability, that women on boards are likely to be more risk averse, and that diverse work environments are associated with "reduced instances of interpersonal aggression." But the evidence just isn't there.

Take, for example, the claim that diversity reduces instances of "interpersonal aggression." For this proposition, Ms. Lacewell cites a report by Catalyst, a non-profit activist group devoted to supporting women in the workplace.[5] The Catalyst article in turn cites a meta-study on "diversity climate" in the workplace,[6] which—in favor of its own interpersonal aggression claim—itself cites a single observational study correlating data from questionnaires distributed to nurses in 30 hospitals in Israel.[7] That study, examining perceptions of workplace hostility between Jews and Arabs, found that ethnic diversity **increased** perceptions of interpersonal aggression, but that the effect was mitigated if nurses also perceived a positive "diversity climate." What this means for New York firms is—to put it mildly—not at all obvious. "Diversity climate" is not a measure of diversity at all. It instead quantifies the nurses' subjective perceptions of how fairly their team and the head nurse treated staff, assessed by asking the nurses to score from 1 to 5 items like, "I trust my unit to treat me fairly." There is no way to meaningfully extrapolate from the findings of this single study on workplace treatment in Israeli hospitals to any kind of conclusion about racial diversity on New York bank boards. To the extent that it suggests anything, the Israeli study indicates that what matters most is good management practices that treat people fairly regardless of their ethnicity, a point on which the proposal is conspicuously silent.

Another example is Ms. Lacewell's claim that studies show that gender and racial diversity leads to increased financial performance. But as the SEC has admitted in its recent

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[3] My Chi To, Insurance Commissioner's Agenda: NY On Industry Diversity, LAW360 (Nov. 2, 2021) https://www.law360.com/publicpolicy/articles/1436223.
[4] David Baris, President of the American Association of Bank Directors to Adrienne A. Harris, Acting Superintendent of the NY Department of Financial Services (Dec. 3, 2021) http://aabd.wpengine.com/wp-content/uploads/2021/12/AABD_NYDFS-Letter_12-3-21-2.pdf
[5] Catalyst, Why Diversity and Inclusion Matter: Quick Take (June 24, 2020), https://www.catalyst.org/research/why-diversity-and-inclusion-matter/.
[6] Elissa L. Perry & Aitong Li, Diversity Climate in Organizations, Oxford Research Encyclopedia of Business and Management (Oct. 30, 2020) https://doi.org/10.1093/acrefore/9780190224851.013.45.
[7] Anat Drach-Zahavy & Revital Trogan, Opposites Attract or Attack? The Moderating Role of Diversity Climate in Team Diversity-Interpersonal Aggression Relationship. 18 J. Occupational Health Psychology (2013) https://ssl.haifa.ac.il/10.1037.

examination of the same studies, the results are "mixed."[8] The SEC is too generous. The extensive body of actual, rigorous studies show that sex diversity has little or no discernible effect on firm performance. And for racial diversity there is no reliable evidence at all. The lone study Ms. Lacewell musters with statistically significant findings in support of the financial benefits of racial diversity is a report by the consulting firm McKinsey. While the 2020 McKinsey Report finds "a positive, statistically significant correlation between company financial outperformance and diversity on the dimensions of both gender and ethnicity" it qualifies its results—"Correlation is not causation. There are real limitations, and we are not asserting a causal link."[9] But even if these claims were true, racial discrimination for the sake of profit is evil. If the McKinsey study had found that having more women on boards decreased corporate performance, that would not justify sex discrimination against them. Our country once justified widespread race and sex discrimination on the basis of economic necessity. That disgraced mode of thinking should remain where it was left: in the historical dustbin.

Ms. Lacewell also points to the fact that some companies are already seeking to diversify their boards through racial discrimination. But that other private parties are already doing something illegal is no evidence that encouraging others to do it is wise or legal. And discrimination on the basis of race is illegal.

First, government policies that perpetuate racial classifications are incompatible with Equal Protection Clause of the Fourteenth Amendment of the Constitution, which protects "any person" against denial of "the equal protection of the laws."[10] Ms. Lacewell's proposed "diversity" scheme violates this text by subjecting firms and their directors and management to classification based on race. As the Supreme Court has held, "[r]acial classifications are antithetical to the Fourteenth Amendment, whose 'central purpose' was 'to eliminate racial discrimination emanating from official sources in the States.'"[11] What DFS proposes is not narrowly tailored or serving a compelling state interest but is no more than blunt racial balancing. "Allowing racial balancing as a compelling end in itself would effectively assure that race will always be relevant in American life, and that the ultimate goal of eliminating entirely from governmental decision making such irrelevant factors as a human being's race will never be achieved."[12]

Second, Ms. Lacewell's encouragement of member companies to recruit directors and management based on gender and race also increases the risk these firms will run afoul of federal anti-discrimination law, namely Title VII of the Civil Rights Act of 1964 and the Civil Rights Act of 1866, as codified in 42 U.S.C. § 1981. Title VII prohibits employment discrimination on the basis of "race, color, religion, sex, or national origin" by employers. If, in hiring board members

[8] SEC, Order Approving Proposed Rule Changes to Adopt Listing Rules Related to Board Diversity (Aug. 6, 2021).
[9] Vivian Hunt et al., *Diversity Wins: How Inclusion Matters*, McKinsey & Company (May 2020).
[10] U.S. Const. Art. XIV, § 1.
[11] *Shaw v. Hunt*, 517 U.S. 899, 907 (1996) (quoting *McLaughlin v. Florida*, 379 U.S. 184, 192 (1964)).

[12] *Parents Involved in Cmty. Sch. v. Seattle Sch. Dist. No. 1*, 551 U.S. 701, 730 (2007) (plurality opinion) (cleaned up).

to meet diversity goals, a company declines to hire someone because of their race or sex, they violate Title VII. This applies even in the event of so-called "reverse discrimination."[13] Section 1981 works similarly. As the late Justice Ginsburg once explained, § 1981 was designed to"break down all discrimination between black men and white men regarding basic civil rights."[14] It is, in other words, a statutory extension of the Fourteenth Amendment's equal protection guarantee to all contracting, regardless of whether it is public or private in nature.[15]

Ms. Lacewell's letter goes far beyond recommending permissible, race-neutral efforts to recruit from a broader and more diverse talent pool. Rather, it explicitly directs banks to make race conscious decisions about hiring and retention.[16] There is thus no way for banks to actively make "progress" in their efforts to "improve diversity" in the way the letter directs without taking race into account when they hire and fire board members. This is blatantly illegal under § 1981.

In fact, you yourself could be liable as an government officer for causing this discrimination under 42 U.S. Code § 1983, which provides that "[e]very person who, under color of any statute, ordinance, [or] regulation, . . . subjects, or causes to be subjected, any citizen . . . to the deprivation of any rights . . . shall be liable to the party injured." Under § 1983, you could face monetary damages—for example to compensate a replaced bank director's lost compensation—as well as punitive damages, even if you did not know you were violating the victim's constitutional rights.[17] Qualified immunity is no shield when officials are suitably warned and "have time to make calculated choices about enacting or enforcing unconstitutional policies."[18] You clearly have both, especially upon receipt of this letter. By demanding that firms reserve board and management positions for individuals of a particular race, Ms. Lacewell's letter encourages and directs companies—no matter how well intentioned—to illegally discriminate on this very basis.

Finally, firm discrimination in board hiring violates New York State law. The New York Bill of Rights states that, "No person shall, because of race, color, creed or religion, be subjected to any discrimination in his or her civil rights by any other person or by any firm, corporation, or institution, or by the state or any agency or subdivision of the state."[19] Discrimination on the basis of race is subject to severe penalties. New York State Human Rights Law, states that "The opportunity to obtain employment without discrimination because of . . . race . . . [or] sex . . . [is] a civil right."[20] Discrimination in violation of this right in hiring subjects the firm to compensatory damages, punitive damages, and being compelled to hire or reinstate the

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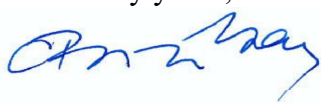
[13] *See Ricci v. DeStefano*, 557 U.S. 557, (2009).
[14] *Comcast Corp. v. Nat'l Ass'n of Afr. Am.-Owned Media,* 140 S. Ct. 1009, 1020 (2020) (Ginsburg, J., concurring) (cleaned up).
[15] *See* Gratz v. Bollinger, 539 U.S. 244, 276 n.23 (2003) ("purposeful discrimination that violates the Equal Protection Clause of the Fourteenth Amendment will also violate § 1981").
[16] For example, where it instructs, "Firms should aim to have a board and management team that benefit from a wide diversity of skills, experiences, and perspectives, including those based on gender, race or ethnicity."
[17] *See* Owen v. City of Independence, 445 U.S. 622 (1980).
[18] *Hoggard v. Rhodes*, 141 S. Ct. 2421, 2422 (2021).
[19] NY Const art I § 11
[20] N.Y. Exec. Law 15 §291.1

discriminated against employee.

There are many honest people in New York working hard to end racial discrimination and increase opportunities for all Americans. Linda Lacewell unfortunately was not one of them. Removing the enduring disadvantages caused by racist policies of our nation's past is a noble goal, and one all should share. But the pursuit of this goal through perpetual racial balancing—"a process of continual improvement, not a destination"—is not only illegal, it is self-defeating. As Chief Justice Roberts has explained, the "way to stop discrimination on the basis of race is to stop discriminating on the basis of race."[21] DFS's plans would not discourage but encourage firms to engage in racial classification and discrimination. This must stop. What Justice Thomas said almost three decades ago bears repeating now: "there is a moral and constitutional equivalence between laws designed to subjugate a race and those that distribute benefits on the basis of race in order to foster some current notion of equality."[22] True equality is equality of opportunity, where one's race or sex is not used as some kind of proxy for other characteristics. As the AABD has explained, "meeting the fiduciary duties of a director . . . is not dependent on being a member of any group."[23] Rather it depends on character, intelligence, business acumen, and leadership skill—traits that can be found in men and women of all races and backgrounds.

The Lacewell policy is indefensible, Superintendent Harris, and you should act swiftly to unmake it.

Sincerely yours,



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[21] *Parents Involved in Cmty. Sch. v. Seattle Sch. Dist. No. 1*, 551 U.S. 701, 748 (2007) (opinion of Roberts, C.J.).
[22] *Adarand Constructors, Inc. v. Peña*, 515 U.S. 200, 240 (1995) (Thomas, J., concurring) (cleaned up).
[23] Baris, *supra* note 4.