November 18, 2020

Chairman and CEO James Gorman
Morgan Stanley
Suite D, 1585 Broadway
New York, New York 10036

Dear Chairman and CEO Gorman:

In light of recent high profile police killings of Black people, the ensuing nationwide protests against racial injustice, and companies' responses to these events, we urge the board of Morgan Stanley to conduct and disclose the results of a racial equity audit that would identify, prioritize, and remedy the adverse impacts of the company's policies and practices on non-white stakeholders and communities of color. The board should engage a variety of key stakeholders in undergoing this audit and evaluating the specific topics to be addressed, including civil rights organizations, employees, and customers.

As outlined further below, we believe that this disclosure would demonstrate concrete steps that the company has taken to address racial injustice and unequal treatment not only in its own workplace, but also within the community that it serves. Morgan Stanley, like many other issuers, has made a public statement supporting Black Lives Matter and racial justice. While these statements are informative to investors, the meaning is lost without concrete action and introspection by company leadership.

The CtW Investment Group works with pension funds sponsored by unions affiliated with Change to Win, a federation of unions representing nearly 5.5 million members, to enhance long term shareholder value. These funds have over $250 billion in assets under management and are substantial Morgan Stanley shareholders.

The Banking Industry's Role in Reinforcing Racial Inequality Raises Concern

The current reckoning on racial injustice facing the financial industry is not new, with the industry playing a significant role in the economic inequality facing communities of color. White households on average hold 10 times the wealth of Black households, which is largely attributable to institutionalized racism within the U.S. financial system. The driving factor for this inequality in wealth distribution is lenders failing to issue mortgages to minorities. By way of example, for every $1 loaned out to finance residential properties in white neighborhoods in Chicago from 2012-2018, a mere 12 cents was invested in Black neighborhoods, despite anti-discrimination laws that were passed in the 1960's that bar such practices, known as "redlining."[1]

Mortgage issuances are just one concern, however. Black and Hispanic banking customers have also been reported to face higher monthly checking account fees than white customers. According to a recent survey, Black and Hispanic customers reported paying $12 and $16 per month, respectively, for

[1] Jennifer Tescher, *American Banker*, "Bankers need to walk the walk on equality," June 9, 2020, *available at* https://www.americanbanker.com/opinion/bankers-need-to-walk-the-walk-on-equality.

overdraft penalties and ATM surcharges, versus $5 per month for white customers.[2] A 2018 study by *New America* reinforced these findings, noting that Black and Hispanic communities face higher costs associated with opening accounts, higher maintenance fees, and larger minimum deposit requirements than their white counterparts.[3] Given that checking accounts effectively operate as a mechanism to participate more actively in the economy, these requirements redirect income and reduce the economic power of people of color, who also typically earn less than white customers. In light of the current pandemic and the significant spike in unemployment, these requirements threaten to reverse years of gains in the number of households having access to a bank account.

We have also seen the discriminatory practices of the financial industry when it comes to commercial banking for people of color. Minority-owned businesses continue to struggle with access to capital, much of which is restricted by the industry's low approval rates for funding small businesses within communities of color. The Federal Reserve has reported that more than half of Black-owned businesses that applied for a loan were rejected, twice the rate of a white owned business.[4] A study by *The Business Journals* of its 44 markets found that the four largest banks made 91% fewer Small Business Administration 7(a) loan guarantees to Black-owned businesses in 2019 than in 2007.[5]

Finally, not only have the financial industry's external practices adversely impacted communities of color, but its internal practices reflect little progress in achieving racial equity within the industry's workforce and leadership teams. The House Financial Services Committee recently held a hearing on workforce diversity within the banking industry, noting that at "megabanks," like Morgan Stanley, just under 10% of the workforce was Black. More alarming still was the fact that a mere 19% of executive senior level positions at all banks that reported back to the Committee were held by ethnic or racial minorities.[6] In order to better evaluate their full impact on communities of color, financial institutions must review their human capital management practices in relation to employees of color.

Morgan Stanley's External and Internal Practices Raise Concerns Regarding Racial Inequality

In response to the Black Lives Matter protests in June 2020, you announced a $5 million donation to the NAACP's Legal Defense Fund, creation of an "Institute of Inclusion" with initial funding of $25 million, and addition of a fifth value to the bank's core values related to Morgan Stanley's commitment to diversity and inclusion. Simply pledging funds and issuing commitments, however, are not enough to

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[2] Kristopher J. Brooks, *CBS News*, "Blacks and Latinos say they pay higher bank fees, research suggests, they're right," January 16, 2020, *available at* https://www.cbsnews.com/news/minorities-report-paying-higher-banking-fees-than-white-people-bankrate-survey-says/.

[3] Jacob Faber & Terri Friedline, New America, *The Racialized Costs of Banking*, June 2018, *available at* https://d1y8sb8igg2f8e.cloudfront.net/documents/The_Racialized_Costs_of_Banking_2018-06-20_205129.pdf, p. 4-5.

[4] Gene Marks, *The Guardian*, "Black owned firms are twice as likely to be rejected for loans. Is this Discrimination?" January 16, 2020, *available at* https://www.theguardian.com/business/2020/jan/16/black-owned-firms-are-twice-as-likely-to-be-rejected-for-loans-is-this-discrimination.

[5] Matthew Kish & Malia Spencer, *The Business Journals*, "One System Un)equal Access," October 15, 2020, *available at* https://www.bizjournals.com/portland/news/2020/10/15/unequal-access-how-the-us-financial-system-is.html?b=1602790745%5E21787983.

[6] House of Representatives, Financial Services Committee, *Diversity and Inclusion: Holding America's Large Banks Accountable*, February 2020, *available at* https://docs.house.gov/meetings/BA/BA13/20200212/110498/HHRG-116-BA13-20200212-SD003-U1.pdf (see Figures 5 and 6).

bridge the gap between decades of discrimination and the lack of wealth creation within Black and brown communities, nor does it address the shortcomings of the bank's own role in perpetuating inequality. For example, in 2012 a lawsuit was filed alleging that Morgan Stanley encouraged a subprime lender to push riskier loans onto Black borrowers in Detroit, from which Morgan Stanley profited off of once securitized. The case was resolved short of trial, so the extent of Morgan Stanley's actions was not adjudicated. While the claims stem from loans made prior to the 2008 financial crisis, we believe that the lawsuit highlights concerns about the impact of Morgan Stanley's practices and policies.

Further, though Morgan Stanley has committed to providing donations to organizations like the NAACP Legal Defense Fund, the bank has also provided support to the very same law enforcement institutions that are now being criticized for discrimination and excessive force against Black and brown communities. Two of Morgan Stanley executives together chaired the 2019 NYC Police Foundation Gala that honored you, CEO and Chairman Gorman. Morgan Stanley is also represented on the boards of the Atlanta Police Foundation and several other police foundation boards from Jupiter, Florida, to Long Beach, California. The company is also a Bronze Sponsor of the Charlotte Police Foundation. Critics see such foundations to operate as a subversive means of funding equipment outside the public eye, including surveillance tools that are used by police departments against communities of color. We hope that this proposed audit would address Morgan Stanley's relationships with police foundations.

Morgan Stanley is also known for its financial advisory services that focusses on high net worth individuals, but with its purchase of E-trade earlier this year, it's signaled a move towards online wealth management tools for customers of discount brokerage services. Among its 5 million retail customers, the purchase of E-Trade also brings 4,000 corporate customers who hold $580 billion in stock on behalf of their employees. One of the most critical elements of E-Trade's strategy is its zero commission fee policy on stocks, options and ETFs. While we recognize that Morgan Stanley's purchase of E-Trade was largely to move into money management for average Americans while adding additional fee-based revenues, given the financial industry's long standing pattern of discriminatory or overly burdensome fee structures for Black and brown customers, we hope that Morgan Stanley will carefully evaluate any changes to E-Trade's low cost trading structure and how these changes will impact customers of color.

Lastly, we note that Morgan Stanley, like many of its peers, appears to be lagging in its own development and retention of employees of color. According to Morgan Stanley's responses to an inquiry by the House Financial Services Committee, only 16.9% of the bank's senior executive level employees were racial or ethnic minorities. Yet, there were no Black or Hispanic executives within its C-suite until June 2020 amid the Black Lives Matters protests, when the company accelerated one Black executive's appointment up from December 2020 to the Operating Committee and appointed a second to the Management Committee.

The company also has a history of allegations of discrimination by Black and Hispanic employees. In 2007, the company paid a $16 million settlement related to a class action lawsuit that was filed alleging Morgan Stanley steered its client accounts towards white brokers, discriminating against Black and Hispanic brokers and preventing them from commissions and promotions. As part of that agreement, the company committed to make certain internal changes, including adjustments to their power ranking systems, which ranked brokers on performance to determine account allocations and consultation with psychologists to help with the hiring and retention of Black and Hispanic advisors and broker trainees.

This settlement, however, was not sufficient to address ongoing issues related to discrimination within Morgan Stanley's culture. In 2018, a former Black Morgan Stanley wealth manager claimed he was the subject of racial discrimination and subsequently fired for raising his concerns. This lawsuit moved into private arbitration due to a mandatory arbitration clause that was imposed by Morgan Stanley on its employees in 2015. Such clauses can have a chilling effect on whistleblowers, and keeps investors, directors, and the public at large in the dark of the full scope of any misconduct which may be taking place.

More recently, however, Morgan Stanley faces a pending lawsuit from its former global head of diversity, Marilyn Booker. In June 2020, Booker filed a suit against Morgan Stanley alleging systemic racism at the bank and retaliation for raising concerns over repeated instances of discrimination in the hiring, retention, and promotion of the bank's Black employees. This included her rebuffed attempts to raise with management a plan to restructure a training program for Black financial advisors. During her 16 year tenure at the firm, Booker alleged that Morgan Stanley reduced her budget for diversity initiatives, and soon after you became CEO in 2010, she was removed from her position as global head of diversity with no explanation. Given the bank's history and this most recent lawsuit, we question how, if it all, Morgan Stanley's new Institute of Inclusion will be involved in monitoring and addressing any equity gaps in compensation, promotion, and retention of employees of color. We also believe that the amount of funding that Morgan Stanley has pledged both in comparison to its peers, but also relative to its overall earnings, does not reflect the firm's commitment that diversity and inclusion is now considered a fifth core value akin to other priorities that include putting its shareholders first or innovating its financial products, which almost certainly have a larger budget allocation.

Conclusion:

Implementation of any next steps by Morgan Stanley to address racial injustice and economic inequality requires careful study of how its products and services have contributed to this imbalance. An audit that involves consultation by a variety of stakeholders, including employees and community groups, will provide a framework for this analysis. If you would like to discuss our concerns, please contact my colleague Tejal K. Patel, Corporate Governance Director, at tejal.patel@ctwinvestmentgroup.com.

Sincerely,

Dieter Waizenegger
Executive Director