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Reflections on the Diversity-Performance Nexus at Elite American Law Firms: Toward a Theory of a Diversity Norm

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REFLECTIONS ON THE DIVERSITY-PERFORMANCE  
NEXUS AMONG ELITE AMERICAN LAW FIRMS:  
Toward a Theory of a Diversity Norm

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*Abstract*

This exploratory article considers the diversity-performance nexus among elite American law firms. I present a taxonomy of existing theories – the neoclassical economic theory of discrimination, the “new markets” hypothesis, and the organizational efficiency/managerial theory of diversity – that explain this nexus with greater or lesser success. I argue that these theories do not seem fully to explain certain institutional and behavioral realities among elite American law firms with respect to workplace diversity. The article thus supplements the existing theories with a (deliberately) parsimonious social norms (signaling) model of diversity that (at least at first blush) seems more consistent with some of the observed institutional and behavioral regularities among these firms. However, the social norms model that I describe is deficient in that it treats diversity as an exogenous norm. I therefore propose to embark upon future research involving a deeper exploration of the question whether (and why) elite American law firms have internalized a diversity norm and the potential obstacles to such internalization, as well as an empirical analysis.

*This paper should be read as a “thought” piece that lays the groundwork for a future study.*

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## I. INTRODUCTION

The legal profession is one of the least diverse professions in the United States.<sup>1</sup> Notwithstanding progress in recent years, the elite American corporate bar is even less diverse than the rest of the legal profession.<sup>2</sup> Furthermore, it has been that way for a long time. The homogeneity of the elite corporate bar persisted, even after many other private companies began to integrate their workforces in response to changes in such factors as market demographics and globalization.

In the recent University of Michigan affirmative action decision, *Grutter v. Bollinger*, influential representatives of corporate America submitted amicus briefs

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<sup>1</sup> The following statistics on the relative representation of African-Americans in various professions substantiate this claim in stark terms:

<i>Profession</i>	<i>Percentage African American</i>
Lawyer	3.9% (2001) 2.6% (1983)
Accountant/Auditor	9.5% (2001) 5.5% (1983)
College Professor	6.1% (2001) 4.4% (1983)
Physician/Psychologist	7% (2001) 5.9% (1983)

Amon (2004) (reporting U.S. Census Bureau statistics).

<sup>2</sup> The U.S. Equal Employment Opportunity Commission reports the following statistics for larger U.S. law firms (i.e., firms with 100 or more employees):

	<i>1975</i>	<i>2002</i>
<b>Associates</b>		
Women	14.4%	40.3%
African American	2.3%	4.4%
Hispanic	0.7%	2.9%
Asian American	0.5%	5.3%
<b>JD Degrees</b>		
Women	33%	48.3%
African American	4.2%	7.2%
Hispanic	2.3%	5.7%
Asian American	1.3%	6.5%

U.S. Equal Employment Opportunity Commission (EEOC) (2003). Employers are required to file an EEO-1 report with the EEOC if it has at least 100 employees. There is a substantial overlap between the universe of elite law firms and the universe of large law firms.

supporting the University of Michigan's affirmative action policies based on the "diversity is good for business" rationale. This raises the interesting question whether the "diversity is good for business" rationale extends to elite corporate law firms.<sup>3</sup> This exploratory article thus considers the diversity-performance<sup>4</sup> nexus among elite law firms.

I present a taxonomy of existing theories that address the relationship between diversity and performance, with greater or lesser success: the neoclassical economic theory of discrimination, the "new markets" hypothesis, and the organizational efficiency/managerial theory of diversity. In addition, I introduce a novel social norms approach to diversity in elite law firms. The various theories are not mutually exclusive and I do not purport to delineate a pecking order of theories to explain the relationship between elite law firm diversity and performance. Indeed, some of the theories might be complementary. An important long-term goal is to understand the ways in which the different theories might be aggregated into a larger, more complete explanation.

Of the various theories I shall examine, the neoclassical economic theory of discrimination probably provides the least insight into the diversity-performance link, in part because it is the least institutionally refined approach. The social norms approach is an especially promising approach because, unlike the other theories, it can explain some apparent empirical puzzles in the evidence. In addition, a social norms approach might ultimately accommodate both the instrumental and the non-instrumental significance of diversity among elite American law firms.

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<sup>3</sup> Wilkins (2004) was among the first to raise the question whether the "diversity is good for business" rationale extends to elite law firms.

<sup>4</sup> By performance, I am referring to common law firm performance measures, such as measures of profits or revenue per partner.

The article is organized as follows. Part II presents a taxonomy of existing theories that address the relationship between diversity and performance. In this part, I describe and critique the following theories: the neoclassical economic theory of discrimination, the “new markets” hypothesis, and the organizational efficiency/managerial theory of diversity. In Part III, I sketch and critique a social norms (signaling) theory of the diversity-performance nexus. Finally, Part IV summarizes and concludes the article and suggests promising avenues for future research, in particular a deeper exploration of the question whether (and why) elite American law firms are committed to a non-instrumental diversity norm and an empirical analysis.

## **II. A TAXONOMY OF EXISTING THEORIES**

### **A. Neoclassical Economic Theory of Discrimination or “Bigots are Weak Competitors”**

Although (for reasons I articulate below) I think that this is the least promising framework within which to assess the diversity-performance nexus among elite law firms, the neoclassical economic theory of discrimination (Becker, 1957; Epstein 1992) is a useful starting point before considering several more institutionally nuanced theories.<sup>5</sup> The basic implication of the neoclassical economic approach is that diversity has no value independent of the “intrinsic” value of human capital.<sup>6</sup> In other words, the neoclassical economic framework is at best agnostic about the role of diversity in

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<sup>5</sup> For an interesting examination of the historical evolution of neoclassical labor economics and its dominance over the institutional approach to labor economics, see Boyer and Smith (2001).

<sup>6</sup> John Donahue contrasts the “intrinsic” value of human capital with the “contingent” value of human capital: “at best labor markets can only be expected to equate price with the value of labor as determined not simply by the intrinsic value of the assets as in capital markets but by the contingent assessment that will be influenced by an array of discriminatory participants. Put differently, labor markets can only hope to achieve contingent equality, while capital markets can deliver the higher ideal of intrinsic equality” (Donahue 1994, 2594-2595).

enterprise performance (ignoring for now the role of third party effects, which I discuss in the next section) and it can be read to suggest that law firms should not pursue diversity any more than they should engage in irrational discrimination (again, abstracting for the time being from third party effects). At the same time, the neoclassical theory would lead one to expect diversity in law firms to the extent that the lack of diversity reflects race or gender discrimination.

The basic premise of the neoclassical economic theory of discrimination is that the labor market is perfectly competitive. That is, the going (market clearing) wage exactly equals the marginal product of labor. In turn, the marginal product of labor represents the “intrinsic” value of human capital. Given this set of premises, the “market does not like bigots” hypothesis holds that in equilibrium firms that discriminate are eliminated by competitors, who can hire equally or more qualified minority employees at lower wages and thus operate at lower cost. In short, employers’ irrational “tastes” for discrimination are inconsistent with their economic self-interest and the market acts as a disciplinary device against such irrational preferences (Becker 1957, Sunstein 1991).

What does the neoclassical framework imply for diversity among elite law firms? First, it produces the rather unrealistic positive claim that law firms do not in fact discriminate because if they did they would go out of business in the highly competitive law services market. Second, it yields the normative claim that law firms should simply hire entering associates whose marginal product (“intrinsic” value) of labor equals the going market wage, irrespective of whether such a hiring decision fosters or discourages a diverse workplace. In fact, a strong normative implication seems to be that elite law firms should *not* pursue diversity as an independent goal because doing so would be as

irrational as exercising a “taste” for discrimination. I consider each of these implications in turn.

The first implication of the neoclassical framework is the positive claim that law firms do not discriminate, since those that do will not be viable in the long-run competitive equilibrium. Non-discriminating firms will be able to hire equally productive minority attorneys at lower wages, translating into lower client fees. Alternatively, non-discriminating firms will be able to hire “superstar” minority associates at the same (or lower) wages than those at which discriminating firms hire “average” white associates. Thus, to the extent that a low level of diversity signifies discrimination, elite law firms that are more diverse should eliminate elite law firms that are less diverse. Happily, in the long run, no firms discriminate and the current observed demographics are not the result of discrimination but rather of meritocratic and objective hiring processes.

The real world is neither as simple nor as happy as this account suggests, unfortunately. Past and lingering intentional and institutional discrimination undoubtedly explain in part the empirical reality of a persistent lack of diversity at elite American law firms (see, e.g, Gulati and Wilkins 1996, Johnson 1997, Roithmayr 2000, Roithmayr 2004, Wilkins 2004). There is no evidence that market forces ever eliminated discriminatory elite law firms. On the contrary, some of the oldest, most successful and most elite American firms have been the least diverse historically and continue to be so today.<sup>7</sup> There is no evidence that their performance has suffered because minorities have

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<sup>7</sup> As David Wilkins notes, “Given the absence of pressure on all sides, it should not be surprising that as late as 1980 large law firms remained almost as white as they were when John W. Davis stood up to defend de jure segregation almost thirty years before” (Wilkins, 2004, 1568).

been grossly underrepresented in these firms. In fact, historically many of these firms thrived in spite of their discriminatory hiring practices. Thus until social norms changed, Jews and women were excluded from most large firms; very few firms rushed in to fill the gap and there is no evidence that those that did ever drove any competitors out of business. There is no reason to think the situation of blacks or Hispanics would be different.

The possibility of elite American law firms' historical success despite discrimination is due precisely to the failure of the normative claim of the neoclassical framework, which is that competition requires that law firms should equate the going wage with the marginal product of labor (and thus cannot discriminate). This prescription overlooks at least two considerations. First, there is the fact that labor markets are not perfectly competitive, and, as a result, labor market discrimination is bound to be more resistant to market pressure than the neoclassical model predicts. Without perfect competition, labor markets can sustain deviations between the price of labor/wages (or "contingent" value) and true value (or "intrinsic" value) indefinitely (see, e.g., Baron and Newman 1990, Darity 1989). Such deviations may be driven by employers' "irrational biases or prejudices" (Donahue 1994, 2592). The potential for a sustained divergence between contingent and true value is likely to be strongest in industries, like legal services, where product quality is opaque and thus hard to observe both internally and outside of the firm (Bartholet 1982, Gulati and Wilkins 1996, Levin and Tadelis 2004). In addition, deviations between "contingent" value and "intrinsic" value can be perfectly rational, in settings that reward "statistical discrimination" (Charny



and Gulati 1998, Phelps 1972, Sunstein 1991).<sup>8</sup> For example, suppose on average lawyers over six feet tall are much better rainmakers than lawyers under 5'6", and although some lawyers under 5'6" may be great at bringing in clients and some over 6' may be terrible, it is very expensive to determine who the exceptions are. In these circumstances always preferring those over 6' to those under 5'6" makes economic sense.

Second, the institutional structure of elite law firms explains why discrimination could have persisted among them without giving rise to market penalties. Elite law firms' internal labor markets dampen competitive pressures among such firms and thus render them less able than other business organizations to detect and to sanction discrimination in their ranks (Gulati and Wilkins 1996). This is because these internal labor markets are characterized by efficiency wages (Gulati and Wilkins 1996) and promotion tournaments (Galanter and Palay 1991, Gilson and Mnookin 1990, Gulati and Wilkins 1996). Efficiency wages and promotion tournaments in elite law firms are partial solutions to the monitoring problems caused by the difficulty of assessing the quality of legal work.

One mechanism that partners use to induce effort by associates is efficiency wages. An efficiency wage is a wage set at a premium over the competitive market clearing wage. The premium embedded in an efficiency wage should induce greater employee effort and lower monitoring costs:

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<sup>8</sup> Indeed, Charny and Gultai (1998) and Sunstein (1991) suggest that firms that do not engage in statistical discrimination might not survive in a competitive market. According to Sunstein, "Efforts to view people through more finely-tuned (and, hence, more expensive) devices than stereotypes will be punished....Markets will not drive out discrimination to precisely the extent that discrimination consists of economically rational stereotyping" (Sunstein 1991, 27-29).

“This wage premium has two effects that collectively tend to lower monitoring costs. First, by offering a higher than market-clearing wage, firms generate a large pool of qualified applicants from which to hire. This reduces search costs and places the burden on applicants to differentiate between themselves and the rest of the pool. Second, once a worker is hired, she has an incentive to work hard since she knows that if she is fired for shirking, she cannot obtain a similar salary elsewhere and that there are many ‘unemployed’ workers who would gladly take her place” (Gulati and Wilkins 1996, 518-519).

In effect, the efficiency wage reduces employers’ screening and monitoring costs. Most elite law firms appear to pay efficiency wages for these reasons. What this means is that associate wages are sticky and unresponsive to downward pressures (Gulati and Wilkins 1996). Law firms that attempt to reduce their costs by lowering or eliminating the wage premium are likely to lose “good” workers to other firms and to attract “bad” workers. “Firms that seek to cut costs by refusing to pay the wage premium run the risk of losing ‘good’ workers to firms that do while simultaneously attracting ‘bad’ workers who cannot currently get jobs at the higher wage (Gulati and Wilkins 1996).<sup>9</sup>

Efficiency wages are only part of the story, however. Promotion tournaments (so-called “up-or-out” systems) are another important feature of elite law firms’ internal labor markets that reduce monitoring costs in these firms:

“In [tournament models,] firms solve [monitoring problems] with a carrot rather than a stick. Instead of threatening to fire workers who shirk, thereby causing

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<sup>9</sup> Note also the signaling effect to clients of high wages – high wages signal to clients (who also have trouble assessing quality) that their work is being entrusted to the very best lawyers. Thus an attempt to “brand” their services will lead elite law firms to pay higher wages (i.e., efficiency wages).

them to sacrifice supra-market wages, the firm offers a reward for consummate efforts—commonly a cash bonus or promotion to a high-compensation position. Workers in effect participate in a tournament to win, competing against each other in the efforts they make for the firm. Tournament models have particular appeal in our context because they help to explain the structural features of promotion to partnership...that are common in law firms...: careful evaluation over a period of years and sharp changes in status and compensation for successful firm members, even when the transition seems to mean little change in actual productivity” (Charny and Gulati 1998, 71-72).

Efficiency wages and up-or-out promotion schemes, both of which are prevalent in elite law firms, sever the link between associate wages and productivity. The implication is that discrimination in the market for elite law firm jobs will not be manifest in racial wage differentials, as predicted by the neoclassical model of discrimination, but rather in differential career development opportunities and therefore differential promotion opportunities between white and minority associates. The latter types of labor market disparities are even less likely to be penalized in the market than wage differentials, since they less directly affect a law firm's cost structure (Charney and Gulati 1998, 75).<sup>10</sup> Indeed, such disparities might even be rational profit-maximizing strategies for elite law firms (Gulati and Wilkins 1996).

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<sup>10</sup> The neoclassical model assumes only antitrust laws. However, if a firm paid new black attorneys less, it would be unlikely to win a discrimination claim by saying either that black attorneys demanded less income than white attorneys or that the black attorneys they hired were less able and so worth less than their white counterparts. Even if one or the other were true, it would be hard to prove and bad publicity costs would be huge. Some firms got burned by women hires in the 70s; but remarkably few given similar incentives to treat women less well.

The neoclassical model is also unable to explain why many elite law firms seem to be pursuing greater diversity, or at least why they are increasingly paying lip service to the virtues of diversity. According to the model, the intrinsic value of human capital is a function of objective factors, such as years of education, years of experience, skills, age, etc. The intrinsic value of human capital is not a function of such subjective, job irrelevant factors as race and ethnicity (although such markers might be highly correlated with objective measures of human capital, as recognized by models of statistical discrimination). The neoclassical model is at best agnostic (i.e., colorblind) about diversity and there is thus no optimal degree of diversity in this framework, save for the degree of diversity demanded by clients (I address this point in the next subsection). In fact, in the neoclassical framework diversity hiring might be discriminatory and, as such, may be equally irrational as a refusal to hire minorities for prejudicial reasons.<sup>11</sup>

The neoclassical economic theory of discrimination is the least institutionally nuanced among the theories that I consider in this article and for that reason it is unable to address the diversity-performance nexus.

#### B. Client Demand for Diversity: the “New Markets” Hypothesis<sup>12</sup>

In a break with their past exclusionary history, many titans of corporate America are publicly declaring their commitment to diversity, both in their own organizations and

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<sup>11</sup> White diversity hiring is a form of discriminatory hiring within the neoclassical framework (one is indulging a taste for job irrelevant characteristics) it is not necessarily irrational in a world where minorities are willing to work for less than similarly are less skilled whites but, for reasons noted above, cannot be paid less. Searching out diversity may in this case impose no additional labor cuts and may in fact bring a greater skill return than hiring the marginal white.

<sup>12</sup> I borrow the phrase “new markets” from Wilkins (2004), who borrows the term from the managerial literature.

in the law firms that service them.<sup>13</sup> Many corporations are increasingly realizing the value of diversity to their own bottom lines, particularly as their customers and workplaces are becoming increasingly diverse (see Brief for Amici Curiae 65 Leading American Businesses in Support of Respondents 2003, Brief of General Motors Corporation as Amicus Curiae in Support of Respondents, 2003)

At the same time, owing in part to their own increasing diversity, many corporate legal departments are also encouraging their external counsel to diversify their workplaces. For example, Shell requires its external counsel to report the number of women and minority hours that it bills on Shell projects. Shell then annually presents the statistics to its law firms and shows how they did relative one another. Apparently, Shell has “provided critical feedback to those firms it considered to have underperformed in this regard compared to other firms” (Lister 2003). Moreover, Shell is not the only corporation that is encouraging its external counsel to diversity. Additional examples include Sara Lee, Duke Energy, ConocoPhillips, and J.P. Morgan Chase and Co., among others. J.P. Morgan, for example, requires the law firms that service it to report the hours and amounts billed by minority and female lawyers. It places these statistics in a spreadsheet that is then distributed among J.P. Morgan managers. Lister (2003).

In theory at least, client demand for diversity should give more diverse law firms a competitive edge over their peers, other things equal. However, as David Wilkins cogently argues, there are several reasons to doubt whether such client initiatives are likely to have a significant effect on elite law firms. First, the true stimuli of general

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<sup>13</sup> This corporate commitment to diversity is evidenced by the corporate amicus briefs filed in *Grutter v. Bollinger* (Brief for Amici Curiae 65 Leading American Businesses in Support of Respondents 2003, Brief of General Motors Corporation as Amicus Curiae in Support of Respondents, 2003).

counsel initiatives, like the “Morgan Letter”<sup>14</sup>, are unclear (Wilkins 2004). Such initiatives have often been initiated by minority bar associations or minority corporate counsel, thus calling into question corporate clients’ independent commitment to such initiatives (Wilkins 2004). Second, and related, minority corporate counsel face certain pressures and obstacles within their own organizations that might make them unable to direct much legal work to minority associates and partners (Wilkins 1999). Moreover, even if minority corporate counsel do send work to law firms, it may not be the most valuable legal work from the law firm’s perspective (Wilkins 1999, Wilkins 2004). Third, even if client-driven diversity initiatives are truly sincere, most available evidence suggests that they function as carrots rather than as sticks (Wilkins 2004). Indeed, Conley’s (2005) field interviews with lawyers on the question of diversity suggest that law partners are not fearful of losing clients for being insufficiently diverse.

Several institutional features of today’s legal services marketplace also call into question the role of client demand in systematically fostering diversity at elite law firms. First, due to the declining importance of firm-specific capital, many corporate clients no longer hire a single elite law firm to do all of their external legal work (one-stop

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<sup>14</sup> In the late 1990s, Charles Morgan, the general counsel of Bell South corporation, authored “Diversity in the Workplace: A Statement of Principle” (the so-called “Morgan Letter”). The Morgan Letter reads in part, “we believe that promoting diversity is essential to the success of our respective businesses. It is also the right thing to do. We expect the law firms which represent our companies to work actively to promote diversity within their workplace. *In making our respective decisions concerning selection of outside counsel, we will give significant weight to a firm's commitment and progress in this area.*” <http://www.acca.com/gcadvocate/calltoaction/diversitystmt.html> The letter was signed by more than 350 general counsel. More recently, there is the “Call to Action: Diversity in the Legal Profession”, authored in spring 2004 by Roderick Palmore, General Counsel of Sara Lee. The “Call to Action” reaffirms general counsel’s commitment to diversity in legal practice. The signatories “*intend to end or limit our relationships with firms whose performance consistently evidences a lack of meaningful interest in being diverse.*” Palmore was disappointed by the slow progress since the Morgan Letter. Thus, while the “Call to Action” builds upon the former initiative, it adds stronger language suggesting that corporations might terminate their relationships with law firms whose diversity continues to lag. <http://www.mcca.com/site/data/magazine/2005-01/saralee0105.shtml>. By November 2004, more than 60 firms had signed the “Call to Action”.

shopping), but rather patronize several elite law firms for different types of legal problems, depending on individual partners' reputation and expertise (Gilson and Mnookin 1989, Schneyer 1998).<sup>15</sup> At first blush, this would seem to make a law firm more sensitive to a given client's demand for diversity by increasing competitive pressure among elite law firms (Hillman 2001). However, this potential effect is mitigated by the fact that a corporate client that is being serviced by many different law firms might actually be less sensitive to the lack of diversity of any single law firm that advises it, provided that the law firms that do advise it on "diversity-sensitive" matters (e.g., employment discrimination litigation or government work) are sufficiently diverse. In addition, collective action problems among corporate clients may prevent any single client from making serious demands for greater law firm diversity.

Factors internal to elite law firms might also mitigate the impact of client demand for diversity. First, the larger the law firm and the more diversified is its client base, the more willing the firm might be to lose a particular client (Smigel 1964, [ ]) <sup>16</sup> in the highly unlikely event that such a client withdraws patronage in protest of such law firm's lack of diversity. Second, firm-client agency costs might yield insufficient diversity. In the past, firm-client agency costs were mitigated by the twin characteristics of firm-specific reputation and lock-step compensation, which gave law firm partners incentives to monitor each other. However, the gradual move away from lock-step compensation toward productivity-based partner compensation systems (so-called "eat what you kill" systems) and partner-specific reputation has placed upward pressure on client-firm

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<sup>15</sup> Schneyer (1998) notes that, "[I]n choosing firms for discrete tasks, general counsel emphasize the individual reputations and track records of the lawyers who will do the work, not the reputations of their firms" (Schneyer 1998, 1787).

<sup>16</sup> Double check this citation.

agency costs, since law firm partners now have fewer incentives to engage in mutual monitoring than they once did (Berstein 2003, Ribstein 1998). Increased firm-client agency costs might adversely affect firm diversity in the following manner. While some partners' clients might value diversity, other partners' clients might either be indifferent toward or even dislike diversity. The latter partners have no economic incentive to promote diversity. This effect is exacerbated to the extent that the partners whose clients value diversity are not the rainmakers or power brokers in the firm (Wilkins 2004) and/or to the extent that law firms maximize the interests of their clients as a class and not those of individual clients (Schneyer 1998).

A plausible outcome is a segmented market for legal services in which some types of legal services are performed by firms with diverse lawyers and other types of legal services are performed by relatively homogenous firms. There is some empirical support for this hypothesis. Many black attorneys have left partnerships at majority-white law firms in order to more effectively service their clients (Wilkins 2004). Another corroborating piece of evidence is that there seems to be a systematic correlation between a firm's client base and the degree minority and female representation among its associates (Chambliss 1997). Finally, Conley's (2005) field research suggests that just such a pattern (of segmented markets) has emerged among smaller law firms.<sup>17</sup>

All of this is not to say that client demand is wholly irrelevant. Rather, it is to suggest that certain economic and institutional realities of both law firms and their corporate clients might dampen the effect of client demand for diversity. Ultimately, the

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<sup>17</sup> Describe Conley's study.



role played by client demand is an empirical question which to this point has not been well answered.

### C. Internal Organizational Efficiency

One pillar of the business argument for diversity is the claim that having a more racially and culturally diverse workforce has a beneficial impact on organizational performance. This claim has been studied theoretically and empirically in the management literature. There are at least two channels through which diversity might enhance organizational efficiency: (1) more creative and flexible decision-making and business strategy and (2) better ability to manage an increasingly diverse workplace (Wilkins 2004).

#### 1. Decision-Making and Business Strategy

There are several purported benefits to having a more diverse workforce. First, a more diverse workforce might be better able to understand diverse customer preferences: “knowledge-based resources such as cultural diversity allow firms to succeed by giving them the skills needed to adapt products or services to market needs and meet competitive challenges” (Richard 2000). Second, more diverse work teams might make better decisions, in terms of both the quality of the decisions and the range of viewpoints represented and alternatives considered:

“Minority views stimulate consideration of nonobvious alternatives in work settings and appear useful for making valuable judgments in novel situations. Heterogeneity in decision-making and problem-solving styles produces better decisions through the operation of a wider range of

perspectives and a more thorough critical analysis of issues” (Richard 2000, 165).

Third, more diverse workforces might be better equipped to manage change: “[i]f an organization overcomes resistance to change in the area of accepting diversity, it may be positioned well to handle other types of change” (Richard 2000, 165). The idea here is that an organization that is more open to demographic change is probably also more tolerant and flexible regarding other changes that necessitate novel strategic approaches.

However, there are competing arguments why diversity might not improve, and indeed might even harm, organizational performance. First, there’s the definitional issue concerning what precisely is meant by diversity and what type of diversity is beneficial to problem-solving within organizations. As David Wilkins argues, “the tendency has been to expand the definition of diversity to include everything from geography to organizational position to personal habits and taste in food or sports [and hence] the extent to which companies value the link between racial diversity [in particular] and problem solving remains an open question” (Wilkins 2004, 1587).

Second, even assuming that social scientists can agree upon a consistent and salient definition of diversity, not all of the potential alternative perspectives that accompany diversity are valued in the corporate setting. In particular, managers might not receive minority perspectives which are too divergent from status quo views or practices too well (Carbado and Gulati 2003, Wilkins 2004), especially if management is focused on the short-term (Carbado and Gulati 2003). If that is the case, then minorities might be reluctant to present alternative perspectives or choose to remain silent, “thereby reinforcing the view that their diversity makes no positive contribution to group problem

solving” (Wilkins 2004, 1588). In fact, minorities often feel that they must make themselves appear to have similar viewpoints to those of their colleagues so that they do not stand out as different in the workplace.<sup>18</sup>

Third, whether diversity improves corporate performance is contingent upon the business environment within which the firm operates. For example, it appears that firms pursuing a growth strategy benefit from greater diversity (Richard 2000). In contrast, diversity appears to be costly in firms that are downsizing or pursuing a no-growth strategy (Richard 2000). Finally, whether or not an organization benefits from greater diversity probably also depends importantly upon the firm's ability and resources dedicated to manage its diversity (Thomas 1993, 192). Managing diversity can be costly and may offset the purported benefits of greater workplace heterogeneity if a firm is either unwilling or unable to harness diversity to its advantage.

The empirical evidence on the diversity-performance relationship is mixed. Some empirical studies suggest that diversity improves productivity. Other empirical studies suggest that diversity has either no effect or a negative effect on performance. A significant limitation of the existing empirical literature is that it focuses on business corporations. Other than that of Pearce, Hickey and Burke (1998), very few empirical studies examine the link between diversity and law firm performance.

## 2. Better Management of Diverse Workplace

One potential benefit of having a diverse workforce is a better ability to manage an increasingly diverse workforce (“managerialism”) (Wilkins 2004, 1583). According

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<sup>18</sup> Carbado and Gulati (2003) describe the “but for” minority as the minority employee who is in all respects, except in her racial phenotype, identical to her white colleagues. See also Wilkins (2004).

to David Wilkins, “[d]eveloping a managerial elite capable of overseeing this increasingly diverse workforce is one of the major business imperatives cited by diversity advocates” (Wilkins 2004, 1583). This is particularly true in the military and in corporate America, both of which are becoming sufficiently diverse that having managers who are capable of “interact[ing] with and...understand[ing] the experiences of, and multiplicity of perspectives held by, persons of difference races, ethnicities, and cultural histories’ is indeed a business necessity” (Wilkins 2004, 1583, quoting the General Motors Brief in *Grutter v. Bollinger*).

Be that as it may for the military and corporate America, David Wilkins correctly points out that elite corporate law firms are not sufficiently diverse for the same managerial argument to apply to them. Moreover, “large law firms have demonstrated by their past conduct that substantially greater changes in the demographics of incoming associates will not necessarily produce corresponding changes among firm managers” (Wilkins 2004, 1584). As a cogent example, David Wilkins notes the persistently slow increase in the proportion of female partners, notwithstanding the fact that women have “comprised more than forty percent of the incoming associates in the nation’s largest law firms,” for nearly twenty years (Wilkins 2004, 1584). Women comprise barely more than fifteen percent of the partnership ranks, although they are approaching half of all associates (Id.).

David Wilkins argues further that law firm management does not seem to view this managerial deficiency “as a significant...issue....Indeed, it is not clear whether law firms give significant weight at all to management considerations when making partnership decisions” (Wilkins 2004, 1585). Partnership decisions are based more on

associates' rain-making ability and legal skills and less on their management skills (Id.). This is not altogether surprising in light of the reality that, in most elite corporate law firms, most junior associates have very little, if any, contact with the "managers" (i.e., partners). This paucity of interaction stems from the rigid hierarchical/pyramidal structure that is common among these law firms, in contrast to other business sectors where there is much more manager-subordinate interaction and where we would therefore expect managerial demographics to matter. Furthermore, empirically there does not seem to be any significant deliberate effort among elite law firms to promote diverse partners so as to manage a diverse cadre of associates (Wilkins 2004).

### 3. Implications for Elite Law Firms

Several institutional features of elite American law firms raise doubt about whether the purported organizational efficiency benefits of diversity apply to such firms. As David Wilkins argues, despite "the tremendous changes that have occurred in large law firms during the past thirty years, the basic structure pioneered by Cravath, Swaine and Moore at the turn of the twentieth century remains largely in place" (Wilkins 2004, 1589). That "basic structure" is essentially conservative, is rooted in traditional values and viewpoints, and is rigidly hierarchical. What this means is that entering female and minority associates likely "must conform to the traditional values of the firm...rather than the other way around" (Wilkins 2004, 1589). In such a conservative environment, there is reason to be skeptical about the weight that partners will be willing to ascribe to "alternative" or non-mainstream perspectives. David Wilkins even questions whether, in light of the legal profession's past commitment to homogeneity, law partners, are truly

convinced of the “business case for diversity”, leaving aside “their public protestations” in favor of diversity (Wilkins 2004, 1591).

Finally, the nature of the work conducted by most junior associates – the rank where minority associates tend to be clustered in elite law firms – is often not of the sort that can benefit from diverse viewpoints or the corrections diversity allows. Much, if not most, of the work that is done by junior associates does not involve significant problem solving or client contact in large part due to the hierarchical nature of law firms and the task assignment process (Gulati and Wilkins 1996).<sup>19</sup> Rather, a significant part of the work carried out by junior associates seems to be “grunt” work (or, more euphemistically, “paperwork”) (Gulati and Wilkins 2004).

#### D. Synopsis

The neoclassical economic theory of discrimination is poorly equipped to address diversity (let alone discrimination) in elite law firms. That theory seems to suggest that there is little, if any, value in pursuing diversity. Third party effects (client demand) is a more promising approach and might better explain why elite law firms are increasingly committed to diversity. Indeed, there is evidence that some corporate clients are encouraging firms to pursue greater diversity. However, the significance of client pressure for more diversity is questionable and, where it exists, seems to be more of a carrot than a stick. Finally, organizational efficiency arguments for diversity do not seem to apply very well to the elite law firm context.

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<sup>19</sup> This is also my personal experience.

### III.A Social Norms Theory of the Diversity-Performance Nexus

#### A. Some Empirical Puzzles

Although the above analyses suggest there are at best only weak pressures for firms to actively promote diversity, it is the case that:

- Many elite law firms *do* actively pursue diversity, even though their clients are still predominantly white institutions and individuals, the majority of which, although they might have no discriminatory preferences, have no special desire to be served by non-white attorneys.
- Many elite law firms make public their commitment to diversity and publish their diversity statistics on a regular basis.<sup>20</sup>
- Many of the same elite law firms appear to devote insufficient resources to the training, retention and promotion of minority associates to partnership ranks.<sup>21</sup>

These activities require an alternative theory of diversity commitment.

Devon Carbado and Mitu Gulati suggest that employers' ostensible commitment to diversity is a matter of "institutional legitimacy". In particular, they argue that, although employers face strong incentives (particularly in the short-term) to maintain homogeneity "there are institutional legitimacy concerns that militate against the establishment of homogenous [white-only] workplaces. White-only work forces can create public relations problems" (Carbado and Gulati 2003, 1791). Their suggestion

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<sup>20</sup> For example, the National Law Journal (NLJ) annually publishes the *Diversity Scorecard*. The *Diversity Scorecard* is compiled from data self-reported by the 250 largest U.S. law firms. It reports the "minority percentage" as the percentage of a firm's total lawyers who are African American, Asian American, Hispanic or Native American, excluding non-U.S. citizens. NLJ assigns each firm a "Diversity Rank" based its percentage of minority lawyers.

<sup>21</sup> For instance, in 2000 although minorities comprised 13.2% of all lawyers in the largest 250 U.S. firms, they comprised a mere 3.8% of all partners in such firms.

does not, however, explain the existence of such “legitimacy concerns” and “public relations problems.” I suggest that social norms perspective is most likely to provide an explanation.

### B. Diversity as a Discount Signaling Social Norm

I start with the most parsimonious (and, for that reason, probably the most provocative) approach to social norms, Eric Posner's (2000) signaling model of social norms. In Posner's (2000) framework, the basic problem confronting transacting parties is to induce cooperation and mutually beneficial transactions. This problem is solved through the non-legal mechanism of reputation in a repeated game context. Parties that develop a bad reputation over time will not be able to enter cooperative and beneficial transactions in the future. A party who cares about the future has a relatively low discount rate and thus will not defect today (Posner 2000). In short, parties establish their reputation for cooperation or defection via their track records as a cooperators or defectors over time. In addition to establishing a past track record, parties also indicate their reputation “by sending signals [of their low discount rate] at every opportunity” (Posner 2000, 21). In order meaningfully to distinguish “good” and “bad” types,<sup>22</sup> the signal must be sufficiently costly so that only the good types can afford to send such a signal and everyone must be aware of this fact.<sup>23</sup>

What is the content of the signal? In the model, the signal consists of adherence to a social norm. Adherence to the social norm must be sufficiently costly to distinguish cooperative and non-cooperative types. At the same time, adhering to the social norm

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<sup>22</sup> The types may be continuous, which is more realistic.

<sup>23</sup> “Superficially direct forms of signaling...are...quite inadequate. Credible signaling requires more complex behavior and...complex institutions supplied by the market” (Posner 2000, 226).



must not be too costly. If adhering to the social norm is too cheap, it will have no meaning as a signal of reputation, since both good and bad types will follow the social norm, rendering them indistinguishable. And, if adhering to the social norm is too costly, it will not be worthwhile, even for the good types. The signaling framework circumscribes the social norm in that it “has no independent power, it is not an exogenous force, it is not internalized” (Posner 2000, 26). As such, the social norm always concerns *visible* behavior, that is, behavior that can be observed by other parties. Consequently, “people are more willing to tolerate the violation of norms when the agent tries to conceal his behavior than when norms are openly violated, publicly flouted” (Posner 2000, 24).

How does this framework apply to the diversity-performance nexus among elite American law firms that is the subject of this article? I argue that diversity functions (at least as) an instrumental social norm among these law firms. That is, these firms adhere to a norm of diversity as a signal of their reputation for cooperation.<sup>24</sup> Adhering to diversity signals a low discount rate (i.e., a cooperative reputation) to third parties, including current and prospective clients, current and prospective associates, the government, judges, jurors, etc. As such, diversity is “good for business”.

Consistent with Eric Posner’s social norms signaling framework, adherence to the diversity norm is sufficiently costly that not all law firms can afford to adhere to it. That is because it requires more resources to recruit minority associates than it does to recruit white associates (Wilkins and Gulati 1996). In addition, more diverse firms might have

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<sup>24</sup> I think *pro bono* plays a similar reputational role among many of these firms (see e.g., Lardent 2000). However, diversity might be more untenable than *pro bono* as a reputation signaling norm to the extent that offsetting social norms motivate discrimination. Indeed, a question worthy of further consideration is the potential conflict between diversity and discrimination norms. Which prevails?

to invest in some degree of “diversity management”, which is costly.<sup>25</sup> Neither is the diversity norm too costly, however. It is not too costly precisely because firms can hire “but for” minorities, that is, minorities who are virtually identical in outlook and attitude to their white colleagues. They are substantially the same as their white counterparts, “but for” their racial phenotype Wilkins (2004) and Carbado and Gulati (2003). Because it is sufficiently costly but not too costly, then, the diversity norm is a meaningful marker of “good” versus “bad” law firms.

The signaling framework seems more consistent with several of the observed institutional and behavioral regularities among elite American law firms (noted above) than some of the existing theories. First, the framework might help to explain the fact that many elite law firms actively pursue diversity, even though their clients are still predominantly white institutions and individuals who are probably largely indifferent as to the race or cultural background of the attorneys who advise them. Adhering to the diversity norm is not so much client demand-driven as it is a reputation signal to third parties of the firm’s cooperativeness.<sup>26</sup> Thus, reputable firms pursue diversity irrespective (and perhaps sometimes in spite of) client preferences and attitudes toward diversity.

Second, the framework seems to explain the fact that many elite law firms regularly make public their commitment to diversity and/or publish their diversity

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<sup>25</sup> Kochan et al. (2003) find that diversity may have a negative impact on group processes among corporate work groups that receive inadequate diversity management training. Krawiec (2004) argues that discrimination might actually benefit employers by reducing the costs of diversity management.

<sup>26</sup> In a similar vein, Painter (2001) argues that many law firms voluntarily have opted into bar association quantitative diversity goals and “[p]reservation of the reputational capital that a firm acquires by opting in is the incentive to comply” (Painter 2001, 723). According to Painter, opt-in affirmative action ethical rules “could address some [collective action] problems that firms might be less likely to address on their own” (Painter 2001, 724-725). However, Painter’s analysis is not a signaling approach.

statistics. Firms are not required to publicize their demographics; indeed, some firms might want to obscure them. However, many elite law firms make pronouncements about their commitment to diversity on their websites and in other media. In addition, many of these firms voluntarily reveal the demographic composition of their attorneys in professional publications, like the *NALP Directory of Legal Employers*. This behavior appears consistent with the signaling model, in which “social norms are always about *observed* behavior.” Why would firms feel compelled to publicize their diversity policies and/or statistics, if not to send a signal of their reputation?<sup>27</sup>

Finally, the signaling framework might also explain why many of the same elite law firms that publicize their diversity figures and policies appear to devote insufficient resources to the training, retention and promotion of minority associates to partnership ranks. I noted above that the signal must not be too costly. Diversity is not too costly a signal if a law firm simply pursues a policy of “skin-deep” diversity, as noted above. However, pursuing diversity arguably becomes prohibitively costly if the firm goes beyond the “numbers game” to pursue a deeper, more meaningful commitment to diversity. The latter commitment would require a significant investment of resources in

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<sup>27</sup> One might argue that they publicize such information in order to attract corporate clients and minority associates to whom diversity matters. Another potential counter-argument is that diversity could signal low quality, to the extent that observers believe that firms with a higher proportion of minority associates have more minorities precisely because they have lowered their selection standards. However, as Gulati and Wilkins (1996) argue, elite law firms do not need to lower their standards to hire more minority attorneys. To the contrary, “firms have an incentive to seek out superstars...and protect themselves against unacceptable workers. In the middle...they are...indifferent since they know that differences among candidates in this range are not worth the trouble of investigating. Given what we know about the work these associates will do when they arrive at the firm, this middle/average range is much broader and much less differentiated than the standards critique would lead one to believe. So long as the black lawyers being hired under an affirmative action program come from this middle/average range, any claim that the quality of the firm’s work will diminish, lacks credibility” (Gulati and Wilkins 1996, 601). In addition, based on a study of 3,200 employers in Atlanta, Boston, Detroit and Los Angeles between 1992 and 1994, Holzer and Neumark (1998) find that affirmative action and its attendant human resource policies (e.g., search, evaluation and training) do not lead to the displacement of white males by less productive minorities and women.

training, retaining and promoting minority associates, something that very few elite law firms have succeeded in doing thus far (Wilkins, 2004). Such a commitment might also require individual partners to overcome their discriminatory attitudes regarding their preferred co-partners.<sup>28</sup> The apparent lack of a deep commitment to diversity, beyond the “numbers game” is also consistent with the notion that the signaling norm is always about observed behavior.

In short, the social norms signaling framework outlined here seems consistent with David Wilkins’ (2004) skepticism about the extent and depth of elite law firms’ “diversity imperative.” Under this approach, there is a positive diversity-performance nexus. However, the positive association between diversity and performance in this framework does not necessarily derive from diversity per se. Rather, diversity functions as a signal of a law firm’s underlying quality.

#### C. Limitations of the Signaling Model of Diversity Norm

[THIS SECTION TO COME]

### **IV. SUMMARY AND FUTURE WORK**

The article has considered several theoretical approaches to the diversity-performance nexus in elite American law firms. The following table summarizes the various approaches and their predictions about the diversity-performance nexus.

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<sup>28</sup> Such discriminatory attitude could be fueled by an associational preference as in Becker’s (1957) model or could be the behavioral manifestation of status-driven norms as in McAdams’ (1995) model, or a combination of both (McAdams, 1995).

<i>Theory</i>	<i>Diversity-Performance Nexus</i>
Neoclassical Economic Theory	None (possibly negative)
Client Demand	Ambiguous
Decision-Making	Ambiguous
Management of Diverse Workforce	Ambiguous
Discount Signaling Diversity Norm	Positive (but not causal)

Of the various theories, only the signaling social norms approach appears to yield a clear-cut prediction about the relationship between diversity and performance. The neoclassical economic theory is neutral (or negative) and the other theories yield ambiguous predictions. Since no theoretical exploration is satisfactory without empirical testing, the next stage of project is to study the diversity-performance nexus empirically.

Moreover, a significant drawback of the signaling approach is that it does not illuminate how and why a diversity norm might have emerged among elite law firms in the first place. Rather, it assumes that the diversity norm is exogenous and that diversity has no intrinsic value beyond its instrumental value as a discount rate (reputation) signal. These premises are problematic for at least two reasons.

First, reputation signaling models of social norms ignore the fact that people and institutions often abide by norms because they really believe in them and not merely to enable beneficial market transactions (Blair and Stout 2001). Many obligational norms are maintained for both instrumental and non-instrumental reasons (Eisenberg 1999). In fact, “most obligational norms will originate and stabilize only if they are internalized by

a significant portion of the relevant social group” (Eisenberg 1999, 1260).<sup>29</sup> A particular norm might emerge from novel beliefs about the world based on changed objective facts or “reasoned persuasion” (Eisenberg 1999, 1262).<sup>30</sup> In the present context, “reasoned persuasion” would include the rhetoric and initiatives of diversity advocates, like minority bar associations and corporate general counsel.

Second, the premises of the signaling model are inconsistent with the growing societal commitment to diversity that might be motivated by more than material self-interest. Some law firms might share this commitment to diversity, however remotely, as part of their broader commitment to social justice. Whether they always shared this commitment is irrelevant to the question whether they are becoming increasingly committed to (some notion of) diversity. In the next stage of this project, therefore, I plan to consider whether a diversity norm is in fact becoming internalized and valued apart from material considerations among elite American law firms, as well as the obstacles to internalization (e.g., the persistence of conflicting discrimination norms, as contemplated, for example, by McAdams (1995)).

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<sup>29</sup> See also Cooter (2000).

<sup>30</sup> In the present context, “reasoned persuasion” would include the rhetoric and initiatives of diversity advocates, like minority bar associations and corporate general counsel.

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