NACD CHAPTER
PROGRAM SUMMARY

NACD NEW ENGLAND CHAPTER

EVENT TITLE: ESG Update: Is Diversity Dead or Alive?
EVENT DATE: 11/12/2024
EVENT TIME: 5:00 p.m. ET

PROGRAM SUMMARY:

"Diversity" has been a stated goal of corporations for decades. The conversation was elevated to the board level by an influential McKinsey & Company report in 2015 that concluded that companies in the top quartile of racial and ethnic diversity and those in the top quartile for gender diversity were 35% and15%, respectively, more likely to have financial returns above their industry mean.

But Diversity, Equity & Inclusion (DEI) efforts have faced a blowback for the past several years. In June 2023, the Supreme Court struck down as unconstitutional the affirmative action policies used by admissions offices in colleges and universities across the country, and companies are still considering the ripple effects of this decision on their HR practices. A high-profile CEO recently called for renaming DEI as "MEI" (Merit, Excellence and Intelligence). Are companies retrenching on diversity? If diversity is no longer a factor in hiring, be it for an entry-level position or a board seat, will executives and directors revert to hiring from their personal networks? What are the implications for the composition of the C-Suite and the board? What can and should board members be asking and doing? What are the key considerations for directors from both legal and IR perspectives?

This NACD session explored the current state of DEI initiatives as part of the broader ESG framework, assessing how recent regulatory shifts, court rulings, and changing societal expectations are impacting corporate strategies. DEI programs, once widely adopted, now face intensified scrutiny. Key developments include a decline in new diverse director appointments (58% in 2024 compared with 72% in 2022). Companies are evolving their DEI approaches, with some still prioritizing DEI as integral to their mission, while others are adopting broader, more inclusive frameworks to meet the needs of a more diverse workforce and appeal to a broader range of stakeholders.

Threshold questions boards are asking about DEI include: What specific outcomes are DEI initiatives aiming to achieve? How should DEI be disclosed to stakeholders? How can DEI goals align with long-term business strategy and risk management? Boards are increasingly concerned with providing clarity and rationale behind their DEI goals and disclosures, given the polarized environment. While DEI remains a valuable component of corporate governance, companies are now broadening their inclusion efforts to appeal to a larger employee base and to mitigate reputational risks.

A key focus is the regulatory and legal landscape. Potential changes in SEC leadership could lead to fewer formal DEI mandates, putting the onus on companies to maintain these goals through “private ordering” and shareholder influence. Institutional investors continue to advocate for DEI as a driver of value, and they are expected to use their voting power to support companies with strong DEI commitments, especially if regulatory support diminishes. This shift suggests a growing need for companies to communicate their DEI objectives clearly to ensure alignment with investor expectations.

Board oversight should focus on understanding the impact of DEI on human capital and overall ESG risk management. Boards should balance active oversight with management’s authority, avoiding micromanagement while ensuring DEI is effectively integrated into broader strategic objectives. As DEI becomes a more sensitive topic, board members are encouraged to approach it thoughtfully, with attention to compliance, risk mitigation, and reputational concerns. Boards are increasingly considering how DEI aligns with the company’s long-term strategic goals, assessing its value as a driver of talent retention, innovation, and brand reputation.

Boards, particularly their compensation committees, are paying close attention to DEI metrics as they relate to executive compensation. More compensation committees are incorporating DEI goals into executive performance evaluations, though this is done with caution. The rationale is that DEI goals, when aligned with business objectives, can contribute to sustainable, long-term value creation. However, such metrics should be specific, measurable, and meaningful to avoid tokenism and ensure that DEI performance is genuinely driving a meaningful organizational impact.

From an IR perspective, companies should communicate their DEI and ESG initiatives the way they would any other strategic priority. For companies in consumer-facing industries, understanding and aligning with investor expectations is crucial, as these brands often face heightened scrutiny from both investors and the public. Companies should clearly disclose their DEI goals and provide transparent updates regarding progress. Transparency in DEI and ESG reporting can foster trust with investors and bolster a company's credibility in the market.

While some experts foresee the scaling back of DEI programs in the short term due to political and economic pressures, DEI will remain an important component of governance and risk management. A likely change in corporate approaches to DEI will reflect a shift from regulatory-driven mandates to one influenced by shareholder priorities, placing boards at the center of maintaining DEI as an adaptable yet essential component of corporate strategy. DEI will continue to play a critical role in enhancing long-term organizational resilience and stakeholder relationships.

KEY TAKEAWAYS:

Board Oversight on DEI Goals and Rationale: Boards should focus on clarifying DEI goals and ensuring disclosures align with long-term value creation.

Investor Influence Amid Regulatory Changes: Potential SEC changes could weaken formal DEI mandates, making shareholder-driven accountability key to sustaining DEI efforts.

Balanced Board Oversight in Human Capital Management: Boards should oversee DEI as part of their broader human capital and ESG strategies, supporting management without micromanaging.

Transparency in Stakeholder Communication: Clear, tailored DEI and ESG messaging is critical, especially for consumer-facing brands, to maintain investor trust and public credibility.

DEI's Enduring Role in Governance: DEI will continue to be an essential governance component but is likely to evolve to reflect shareholder expectations and strategic alignment with long-term goals.

MODERATOR:

Stephen Brown, Managing Director and Senior Advisor, KPMG Board Leadership Center

SPEAKER(S):

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