2022

The Instrumental Case for Corporate Diversity

Naomi Cahn
University of Virginia School of Law

June Carbone
University of Minnesota Law School

Nancy Levit
University of Missouri - Kansas City, School of Law

Recommended Citation
Naomi Cahn, June Carbone & Nancy Levit, *The Instrumental Case for Corporate Diversity*, 40 Journal of Law & Inequality (2022).
Available at: https://irlaw.umkc.edu/faculty_works/333

The Instrumental Case for Corporate Diversity

Naomi Cahn[*], June Carbone[**], and Nancy Levit[***]

Forthcoming in 40 JOURNAL OF LAW & INEQUALITY ___ (2022).

A growing body of evidence indicates that diverse businesses outperform those with less diversity. These findings have fueled calls for mandating diversity on corporate boards and for undertaking greater efforts to ensure diversity in the corporate ranks. The question of where diversity fits in a corporate reform agenda, however, has yet to clearly defined. Doing so requires resolving the following issues.

First, why does greater diversity appear to be correlated with better performance? Innumerable studies find that more diverse companies do better. The critics correctly observe that the "diverse companies do better" studies do not prove that simply adding diversity causes the improvement; instead, they posit that the improvement is likely to be "endogenous," that is, the factors that encourage and sustain diversity, such as greater transparency,[1] also improve financial performance, and the variables may interact in multifaceted ways.[2] We argue that an examination of the ways in which the variables that affect diversity and those associated with improved business performance interact provides a basis for what we call "the instrumental case for diversity." If the same factors that correlate with greater diversity also correlate with improved performance, then greater diversity can be a benchmark for better corporate management. It can make diversity metrics a tool (though not necessarily an exclusive or necessary tool) in measuring the reform of dysfunctional corporate cultures. Diversity might then become part of an iterative process; maintaining diversity will require management reforms such as greater transparency that will in turn fuel transformations in management cultures that further both greater diversity and better overall performance.[3]

---

[*] Justice Anthony M. Kennedy Distinguished Professor of Law, Nancy L. Buc '69 Research Professor in Democracy and Equity, University of Virginia School of Law.

[**] Robina Chair in Law, Science and Technology, University of Minnesota Law School.

[***] Associate Dean for Faculty and Curators' Distinguished Professor and Edward D. Ellison Professor of Law, University of Missouri – Kansas City School of Law. We thank Max Larson for research assistance.

[1] A comprehensive NASDAQ report, for example, found that "gender-diverse boards or audit committees are associated with: more transparent public disclosures and less information asymmetry; better reporting discipline by management; a lower likelihood of manipulated earnings through earnings management; an increased likelihood of voluntarily disclosing forward-looking information; a lower likelihood of receiving audit qualifications due to errors, non-compliance or omission of information; and a lower likelihood of securities fraud." NASDAQ, SEC filing (2020), https://listingcenter.nasdaq.com/assets/RuleBook/Nasdaq/filings/SR-NASDAQ-2020-081.pdf. *Cf.* Stephen Miller, *Transparency Shrinks Gender Pay Gap*, SHRM (Jan. 31, 2020), https://www.shrm.org/ResourcesAndTools/hr-topics/compensation/Pages/transparency-shrinks-gender-pay-gap.aspx.

[2] On the meaning of business performance, see *infra* text at notes 5, 93-98.

[3] *See, e.g.,* Yaron Nili, *Beyond the Numbers: Substantive Gender Diversity in Boardrooms*, 94 IND. L.J. 145 (2019) (arguing that when women serve on corporate boards, their tenure is shorter than that of their male counterparts, they are overextended, and they lack clout). Reversing these patterns can serve as a metric for genuine corporate reform.

The second question is also a puzzle: if greater diversity correlates with better business performance, then why has it taken so long for companies to embrace it, and what accounts for the persistence of largely white male boards and upper management? The answer could be path dependence: a largely white and male management team may not recognize the importance of greater diversity or how to accomplish it. The existing literature on privilege, unconscious bias, and microaggressions emphasizes these factors, and diversity training has been designed to address them, albeit with limited success.[4] The persistent lack of diversity, however, may be more explicable as a design feature of flawed management practices. A 2020 Nasdaq report, for example, links greater diversity to the lesser incidence of opaque governance procedures, earnings management, weak internal controls, and securities fraud.[5] Other studies find that lack of diversity is often associated with indifferent, harassing, or bullying bosses.[6] What these negative workplace attributes have in common is that they can also be used to enhance top executive power and compensation at the expense of other corporate objectives.[7] The instrumental case for diversity maintains that where such attributes, which involve conflicts of interest between top management and longer-term company interests, exist, an emphasis on greater diversity is also likely to make it easier to root out such practices.

The third question involves how our instrumental case relates to the moral and more traditional business cases for diversity. The simple answer is that the moral case treats diversity as an end in itself, a necessary part of a just society.[8] The traditional business case for diversity maintains that, even if diversity is not morally or legally compelled, it is a positive good that businesses should embrace because it will promote their own financial interests.[9] The instrumental

---

[4] Indeed, Mike Selmi questions just how "unconscious" unconscious bias is. Michael Selmi, *The Paradox of Implicit Bias and a Plea for a New Narrative*, 50 ARIZ. ST. L.J. 193, 197-98 (2018) ("Rather than defining implicit bias as unconscious and uncontrollable . . . it should be treated as one possible step, usually the initial step, in a more elaborate deliberative process."). *See also* Jessica Clarke, *Explicit Bias*, 113 NW. U. L. REV. 505 (2018)(exploring the ways in which courts overlook explicit bias and accept justifications for it); Frank Dobbin & Alexandra Kalev , *Why Doesn't Diversity Training Work?: The Challenge for Industry and Academia*, 10 ANTHROPOLOGY NOW, Sept. 2018, at 48, 49, https://scholar.harvard.edu/files/dobbin/files/an2018.pdf ("There is ample evidence that training alone does not change attitudes or behavior, or not by much and not for long. In their re-view of 985 studies of antibias interventions, Paluck and Green found little evidence that training reduces bias. In their review of 31 organizational studies using pretest/posttest assessments or a control group, Kulik and Roberson identified 27 that documented im-proved knowledge of, or attitudes toward, diversity, but most found small, short-term improvements on one or two of the items measured. In their review of 39 similar studies, Bezrukova, Joshi and Jehn identified only five that examined long-term effects on bias, two showing positive effects, two negative, and one no effect.").

[5] Nasdaq, *supra* note 1.

[6] *See* Jennifer L. Berdahl et al., *Work as a Masculinity Contest*, 74 J. SOC. ISSUES 422, 422 (2018); Kenneth Matos et al., *Toxic Leadership and the Masculinity Contest Culture: How "Win or Die" Cultures Breed Abusive Leadership*, 74 J. SOC. ISSUES 422, 502-3 (2018); Shannon L. Rawski & Angela Workman-Stark, *Masculinity Contest Cultures in Policing Organizations and Recommendations for Training Interventions*, 74 J. SOC. ISSUES 607 (2018).

[7] *See, e.g.,* June Carbone & William K. Black, *The Problem with Predators*, 43 SEATTLE U. L. REV. 441 (2020) (describing how CEOs acquire greater power vis-à-vis boards by producing short term earnings gains).

[8] *See* David Wilkins, *From "Separate Is Inherently Unequal" to "Diversity Is Good For Business": The Rise of Market-Based Diversity Arguments and The Fate of the Black Corporate Bar*, 117 HARV. L. REV. 1548, 1599-1600 (2004).

[9] *See, e.g.,* Douglas E. Brayley & Eric S. Nguyen, *Good Business: A Market-Based Argument for Law Firm Diversity*, 34 J. LEGAL PROF. 1, 2 (2009).

case we are making in this article exists alongside the moral and business cases. It argues that the promotion of diversity can in some cases become a tool for advancing corporate interests separate from diversity itself. The business case for diversity suggests, for example, that greater diversity may be beneficial in appealing to a more diverse customer base or in recruiting employees who prefer to work in diverse environments. The instrumental case, in contrast, suggests that diversity may also be useful in countering illegal or unethical practices that require a carefully selected crony network to stay hidden.[10] Such an argument does not replace the moral or business cases; it brackets them. Instead, it suggests a more fine-tuned analysis should regard the presence or absence of diversity as a signal tied to specific management practices.

To give an example of the difference, consider the traditional obstacles to diversity: women's greater family responsibilities or an emphasis on pathways into the executive suite that have historically not been open to underrepresented minorities or women. The moral case for diversity maintains that firms have an obligation to devise ways to overcome these obstacles. The business case suggests firms should reconsider whether it is in their interests to continue to maintain such narrow pathways to advancement, trading off traditional notions of merit for more representative inclusion of different groups. The instrumental case, instead, asks whether the presumed advantages of these factors are real. In the case of the emphasis on long hours at work, for example, a growing literature suggests the emphasis on long hours may result less from employer needs and more from an emphasis on zero sum (or often negative sum) competition that becomes an end in itself.[11] The three rationales may come together to question the emphasis on long or unpredictable work schedules as a barrier to the greater inclusion of women; the instrumental case, however, focuses greater attention on when and how such an emphasis is counterproductive.

This article will provide a framework for answering these questions by examining changes in business practices over the last forty years. During that time period, large corporations have shifted from the era of the "corporation man," which featured large, secure, predictable, and largely homogenous business environments, to the era of the "tournament," that is, business environments that place greater emphasis on internal competition and short-term measures of performance. The article will suggest that tournament-like workplaces make it harder to maintain diversity – and often produce worse business outcomes. This analysis will lay the foundation for a deeper inquiry into the relationship between diversity and corporate reform.

The focus of this article is on diversity among the corporate officers and directors who manage corporations. Outside of management, corporations often have no diversity "problems;"

[10] *See, e.g.* Kristin N. Johnson, *Banking on Diversity: Does Gender Diversity Improve Financial Firms' Risk Oversight?*, 70 SMU L. REV. 327, 376 (2017) (describing the value of diversity in valuing groupthink); *Cf.* Carbone & Black, *supra* note 7, at 460 (describing the way white collar criminals create seeming legitimacy for their predatory business practices); June Carbone, Naomi Cahn, & Nancy Levit, *Women, Rule-Breaking, and the Triple Bind*, 87 GEO. WASH. L. REV. 1105, 1109 (2019) (hereinafter "*The Triple Bind*") ("companies use intensely competitive bonus systems to produce insular "young boys' clubs" that promote a culture of rule-breaking; that is, the management systems deliberately and instrumentally select for alpha males who will flout the laws that stand in the way of these otherwise profitable business models.").

[11] Naomi Cahn, *Where Are All the Women Leaders?*, FORBES (Mar. 3, 2020), https://www.forbes.com/sites/naomicahn/2020/03/03/where-are-all-the-women-leaders/?sh=6290f2462ee7.

indeed, the problem is instead that lower-wage jobs are more likely to be filled by women and people of color.[12]

I. Diversity and Corporate Tournaments

Over the last several decades, the prevailing corporate ethos has become one of shareholder primacy; that is, a focus on short-term increases in share price to the exclusion of other considerations. A growing critique maintains that too great an emphasis on short-term metrics is ultimately bad for business. In addition, a different critique to which we have contributed argues that the practices associated with shareholder primacy, such as high stakes bonus pay, have also tended to drive women out.[13] The common denominator in these two critiques is the emergence of winner take all rewards; those calling the shots reorient institutions so that the CEO, influential shareholders, and a select group associated with the boss take a disproportionate share of the company's resources, often at the expense of other employees, customers, and the company's long-term health. In the section, we will, describe the changes and explain why they may undercut long term business performance. Then, we will consider why they may also be associated with less diversity. Considering the circumstances in which these factors may simultaneously undermine the company prospects and the inclusion of women may offer new insights into the instrumental case for diversity.

A. Shareholder Primacy, Short-Termism, and Corporate Boards

An overarching change in corporate management since the 1980's is the reorientation of publicly traded companies to emphasize short-term gains in share-price.[14] This shift can be thought of as involving three components: an insistence that officers and directors consider shareholder interests to the exclusion of other stakeholders such as customers and employees, an alignment of executive and shareholder interests through a restructuring of top executive pay to place greater emphasis on stock options, and, as a consequence of the first two changes, greater pressure on CEOs to produce short-term results.[15] Each of these factors, both individually and collectively, has been the subject of extensive management critiques for reasons unrelated to diversity.

---

[12] *See* Noreen Ahmed, *Exposing Wage Theft Without Fear Is Possible and Necessary*, NAT'L EMP. L. PROJECT (Sept. 16, 2019), https://www.nelp.org/blog/exposing-wage-theft-without-fear-possible-necessary/ [https://perma.cc/8T6Z-6GR4]; Martha Ross & Nicole Bateman, Metro. Pol'y Program, *Meet the Low-Wage Workforce EE* 9, BROOKINGS (2019), https://www.brookings.edu/wpcontent/up-loads/2019/11/201911_Brookings-Metro_low-wage-workforce_Ross-Bateman.pdf [https://perma.cc/U24P-QQEJ].

[13] *See* June Carbone, Naomi Cahn, & Nancy Levit, *Gender and the Tournament*: *Reinventing Antidiscrimination Law in an Age of Inequality*, 96 TEX. L. REV. 425 (2018); Carbone, Cahn, & Levit, *supra* note 10, *the Triple Bind*.

[14] *See* June Carbone & Nancy Levit, *The Death of the Firm*, 101 MINN. L. REV. 963, 966, 1003 (2017).

[15] Carbone & Black, *supra* note 7, at 463–64 ("to better align management and shareholder interests, top management compensation packages began to emphasize incentive pay tied overwhelmingly to stock options. Between 1993 and 2014, the percentage of CEO compensation attributable to incentive pay increased from 35% to 85%, and CEOs also faced greater risk of dismissal if share prices did not increase. The overall disparities in the pay of top executives at the same company increased, and between 1981 and 2013, the pay ratio between CEOs and average wage workers grew from 42:1 to 331:1").

First, while shareholder interests can be diverse, shareholder primacy has tended to identify shareholder interests with short-term fluctuations in share price. This has been true for a number of reasons. The most immediate is that corporate boards measure CEO success in terms of their ability to generate earnings, which in turn push up share price.[16] They exercise oversight in the name of protecting shareholder interests.[17] As a practical matter therefore, a CEO who has a strong initial run "creates greater autonomy by both enhancing his bargaining position over time and increasing the cognitive commitment of the board to him."[18] A decline in share price on the other hand can and has led to the CEO's termination.[19] Enforcing the system have been activist hedge funds that are waiting in the wings, ready to buy up stock, acquire board membership and push through changes that boost the value of their typically short-term investments in the company.[20]

Second, to better align management and shareholder short-term interests, a higher proportion of CEO pay is now tied to stock options that increase in value with reported earnings.[21] This increases the incentives for CEOs to focus their efforts on boosting short term earnings and share prices.[22] CEOs, in turn, have implemented bonus pay systems for top executives that align executive incentives with CEO objectives.[23] Critics allege that high stakes bonus pay has been associated with earnings management, accounting irregularities, increased use of stock buybacks,

---

[16] S*ee, e.g.*, Donald C. Langevoort, *Resetting the Corporate Thermostat: Lessons from the Recent Financial Scandals About Self-Deception, Deceiving Others and the Design of Internal Controls*, 93 GEO. L.J. 285, 295 (2004) (noting that the "preference of the firm's *current* shareholders is for increasing profitability reflected in either dividends or stock price, which sometimes is aided by concealing the truth rather than revealing it."); *id.* at 313.

[17] *See* Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 564 (2003). "[W]hile most of the operational decision-making can be, and is, delegated to management, the board is still required to be an active participant in some of the more important managerial business decisions, such as mergers, stock issuance, and changes to company governance documents." Yaron Nili, *Horizontal Directors*, 114 NW. U. L. REV. 1179, 1188 (2020).

[18] Langevoort, *supra* note 16, at 313.

[19] *See* Andrew C.W. Lund & Gregory D. Polsky, *The Diminishing Returns of Incentive Pay in Executive Compensation Contracts*, 87 NOTRE DAME L. REV. 677, 695 (2011) (indicating that CEO terminations can be linked to share price performance);

[20] *See* Brian R. Cheffins & John Armour, *The Past, Present, and Future of Shareholder Activism by Hedge Funds*, 37 J. CORP. L. 51, 75, 80–82 (2011) (noting that a high percentage of publicly traded companies experience pressure to increase short term earnings because of the role of hedge funds and other activist investors). As Virginia Harper Ho notes, however, there are two other camps of shareholder activists: "public pension funds, labor unions, religious orders, and individual "gadflies," whose activism has often aligned with particular values and interests [and] mainstream institutional investors like Vanguard and Fidelity [that] have generally voted with management. *From Public Policy to Materiality: Non-Financial Reporting, Shareholder Engagement, and Rule 14a-8's Ordinary Business Exception*, 76 WASH. & LEE L. REV. 1231, 1236 (2019).

[21] *See* Carbone & Black, *supra* note 7, at 444, 465-66.

[22] *See* Lynne L. Dallas, *Short-Termism, the Financial Crisis, and Corporate Governance*, 37 J. CORP. L. 265, 320-21 (2012) (describing how executive compensation increases emphasis on short-term increases in share price).

[23] Lynne L. Dallas, *A Preliminary Inquiry into the Responsibility of Corporations and Their Officers and Directors for Corporate Climate: The Psychology of Enron's Demise*, 35 RUTGERS L.J. 1, 37 (2003)(hereinafter *Enron*) (describing how Enron management used its bonus system to reorient company behavior in counterproductive and unethical ways): *See, e.g.*, Lynn A. Stout, *Killing Conscience: The Unintended Behavioral Consequences of "Pay for Performance"*, 39 J. CORP. L. 525, 534 (2014) (describing bonus systems and concluding that they are associated with ."earning manipulations, accounting frauds, and excessive risk-taking.")

and outright fraud.[24] Indeed, a major advantage of such bonuses systems is that they allow CEOs to emphasize their desired metrics while looking the other way at how subordinates achieve their results.[25] Critics call the system "plausible deniability" as executives can use bonuses to signal the desired behavior without complicity in the resulting illegal, unethical, or shortsighted tactics that executives use to produce results.[26] The association of modern executive compensation with abusive practices has become sufficiently widespread that some of the original supporters of the move to bonus pay have withdrawn their support.[27]

Third, the single-minded focus on short-term shareholder primacy has led to concern about the effect on other stakeholders. For example, large investors like Blackrock have begun to pay greater attention to environmental issues, reasoning that climate change may affect the world economy more generally in ways that share price fluctuations in individual companies may not reflect.[28]

Taken together, the combination of a short-term focus, the use of incentive to disguise CEO objectives and company health, and the failure to recognize more generalized challenges to global markets have persuaded many critics that corporate reform is in order. These critics observe that CEOs can often produce an immediate boost in share prices by cutting labor costs through layoffs or reductions in training, slashing investment in research and equipment, engaging in stock buybacks, or concealing negative information.[29] All of these actions have been known to increase

---

[24] *See* Shane A. Johnson, Harley E. Ryan, Jr. & Yisong S. Tian, *Managerial Incentives and Corporate Fraud: The Sources of Incentives Matter*, 13 REV. FIN. 115, 115 (2009) (observing that managers with larger linear incentives may be more likely to commit fraud in an attempt to avoid severe price declines): Sharon Hannes & Avraham Tabbach, *Executive Stock Options: The Effects of Manipulation on Risk Taking*, 38 J. CORP. L. 533, 545 (2013) (discussing the link between executive incentive compensation, excessive risk taking, and the pressure to manipulate reported outcomes to influence share price); Lucian Arye Bebchuk et al., *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69 U. CHI. L. REV. 751 (2002) (arguing that executive ability to set compensation facilitates the ability to benefit from short-term and "rent extraction" strategies)

[25] *See* Carbone & Black, *supra* note 7, at 461-62,

[26] *See* Charles W. Calomiris, *The Subprime Turmoil: What's Old, What's New, and What's Next*, J. STRUCTURED FIN., Spring 2009, at 6, 16 (describing how plausible deniability allowed those overseeing mortgage-backed securities to escape accountability during the financial crisis). *See also* Carbone, Cahn, & Levit, *Gender and the Tournament*, *supra* note 13, at 1159.

[27] Michael C. Jensen & Kevin J. Murphy, *Remuneration: Where We've Been, How We Got to Here, What Are the Problems, and How to Fix Them* 44-45 (Harvard Bus. Sch., Working Paper No. 44, 2004), http://ssrn.com/abstract=561305 (discussing how equity-based compensation led to unwise acquisitions, increased risk, aggressive accounting, and even corporate fraud).

[28] *See* Michal Barzuza et. al., *Shareholder Value(s): Index Fund Esg Activism and the New Millennial Corporate Governance*, 93 S. CAL. L. REV. 1243, 1274 (2020) (describing how Black Rock started to emphasize environmental considerations, including the impact of climate disruption and potential regulatory reactions, in its portfolio as early as 2015).

[29] Langevoort, *supra* note 16, at 295 (observing that the "preference of the firm's *current* shareholders is for increasing profitability reflected in either dividends or stock price, which sometimes is aided by concealing the truth rather than revealing it."). *See also* Dallas, *supra* note 22, at 280 (describing CEO willingness to research, development, and marketing even if it would hurt the firm's medium to long term prospects). William Lazonick calls stock buybacks "weapons of value destruction" and argues executives who make these corporate allocation decisions use stock buybacks to boost their companies' stock prices and manage quarterly earnings "because, through their stock-based

short-term share prices; all have the potential to threaten companies' medium to long term interests.[30] The Corporate Roundtable and other influential actors have started to back away from that short-term shareholder focus, arguing that it is economically destructive.[31]

In addition, some investors now pay increased attention to environmental, social, and governance (ESG) factors. Moody's Investment Service announced in 2020 that it expected ESG considerations "to be of growing importance" in its assessment of issuer credit quality." Moody's analysts wrote, "While our ratings have always reflected our views of ESG risks, the materiality of key environmental and social issues continues to increase."[32] ESG investing often combines two different motives: some funds market ESG investments in an effort to appeal to socially conscious investors.[33] Other investors emphasizing ESG factors maintain that share prices do not fully take into account medium to long term risks arising from greater societal inequality, potential regulatory responses to inequitable business practices, or the inevitable transition to new energy sources.[34]

---

pay, they are personally incentivized to make these allocation decisions." *See* William Lazonick, *The Financialization of the U.S. Corporation: What Has Been Lost, and How It Can Be Regained*, 36 SEATTLE U. L. REV. 857, 888 (2013).

[30] Carbone, Cahn, & Levit, *The Triple Bind, supra* note 10, at 1115. *See also* Mark Desjardine & Rodolphe Durand, *Activist Hedge Funds: Good for Some, Bad for Others?*, HEC (Mar. 26, 2021), https://www.hec.edu/en/knowledge/articles/activist-hedge-funds-good-some-bad-others#:~:text=While%20we%20typically%20think%20of,with%20an%20aim%20to%20make (showing that while such strategies boost share price in the short run, they depress it over time).

[31] *Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans,'* BUS. ROUNDTABLE (Aug. 19, 2019), https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans; *Statement on the Purpose of a Corporation* (2019, updated 2021), https://system.businessroundtable.org/app/uploads/sites/5/2021/02/BRT-Statement-on-the-Purpose-of-a-Corporation-Feburary-2021-compressed.pdf. Martin Lipton (of Wachtell Lipton) argued at the World Economic Forum in 2016 that "A short-term mindset in managing and investing in businesses has become pervasive and is profoundly destructive to the long-term health of the economy." *The New Paradigm A Roadmap for an Implicit Corporate Governance Partnership Between Corporations and Investors to Achieve Sustainable Long-Term Investment and Growth* (2016), https://www.wlrk.com/webdocs/wlrknew/AttorneyPubs/WLRK.25960.16.pdf. *See also* Nadelle Grossman, *Turning a Short-Term Fling into a Long-Term Commitment: Board Duties in a New Era*, 43 U. MICH. J.L. REFORM 905, 906 (2010) ("[B]oard short-termism also seems to be due to some investors with short investment horizons who use activism to influence boards to make decisions that yield short-term returns despite the longer-term impairing effects those decisions might have on the corporate enterprise.")

[32] David Caleb Mutua, *ESG Is Increasingly Important in Credit Ratings, Moody's Says*, BLOOMBERG (Apr. 14, 2020 8:19 AM, CDT), https://www.bloomberg.com/news/articles/2020-04-14/esg-is-increasingly-important-in-credit-ratings-moody-s-says.

[33] *Id.* (emphasizing that millennials are much more socially conscious and that the competition to attract them is intense.).

[34] *See* Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of Esg Investing by a Trustee,* 72 STAN. L. REV. 381, 398 (2020) (distinguishing between the different motivations and arguing that what they terms "risk-return ESG" analysis of a fossil fuel company might conclude that the company's litigation and regulatory risks are underestimated by its share price, and explain that a "risk-return ESG analysis of a fossil fuel company might conclude that the company's litigation and regulatory risks are underestimated by its share price."). *See also* Stavros Gadinis & Amelia Miazad, *Corporate Law and Social Risk,* 73 VAND. L. REV.

The rise in ESG investing also produces greater emphasis on diversity.[35] Particularly in the wake of #MeToo and Black Lives Matter protests, the failure to attend to diversity issues can be a risk factor for major companies on the same order as energy transition and accounting irregularities. But, as we will show below, it also provides a farther-reaching barometer of corporate governance issues.

B. Toxic Management Drives Women Out

In the shareholder primacy era, management styes have changed in ways that make diversity hard to maintain. CEOs have become more likely to be hired from outside a company, and CEO tenure has declined.[36] Given the pressure to accomplish quick results, CEOs may adopt top-down management systems, the use of reductionist metrics to measure success, or high stakes bonus systems that incentivize management priorities.[37] The CEO's focus, especially a CEO coming from outside the company or one with a mandate to produce immediate results, may be on how to gain control of what can be large, sprawling, and bureaucratic institutions. The goal may be to outflank the established players in the organization to find those willing to put the CEO's priorities first, especially where the CEO seeks to slash expenses, cut employment, or shake up the corporate mission. High stakes bonus systems can be an attractive way to do so.

Jack Welch, the GE CEO identified with the modern era of corporate management, was a master in imposing his will on a large bureaucracy. He developed an innovative management training program that regularly moved executives from division to division, and an executive compensation system that introduced high stake bonuses.[38] The company regularly ranked the companies' employees against each other, identifying perhaps twenty percent or so who were groomed for promotion and notifying the bottom ten percent that they were at risk of dismissal.[39] He repeated the process each year, rewarding some with stock options that could be incredibly lucrative as the company's share price increased, and encouraging the ever changing group receiving low marks to consider other employment. For a time, his system proved incredibly

---

1401, 1401–02 (2020)(concluding that "[s]ocial risk has proven highly destructive for corporate value even when the company's key failure is not violating laws, as the recent crises at Facebook and Uber demonstrate.").

35 *See, e.g.*, Veronica Root Martinez & Gina-Gail S. Fletcher, *Equality Metrics*, __ YALE L.J. __ , https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3772895 (forthcoming 2021); *See also* Afra Afsharipour, *Bias, Identity and M&A*, 2020 WIS. L. REV. 471, 488; Lisa Fairfax, *All on Board? Board Diversity Trends Reflect Signs of Promise and Concern*, 87 GEO. WASH. L. REV. 1031, 1032 (2018); Michal Barzuza et. al., *Shareholder Value(s): Index Fund Esg Activism and the New Millennial Corporate Governance*, 93 S. CAL. L. REV. 1243, 1265 (2020) (observing that "index funds are typically reticent followers when it comes to corporate governance reforms, but when the subject matter of activism turns from conventional governance reforms to demands for increased gender diversity on boards, index funds have been notably outspoken, both in communications directed primarily at corporate managers and in marketing efforts directed at the general public.")

36 Carbone & Levit, *supra* note 14, at 1002 n.196.

37 Carbone, Cahn & Levit, *The Triple Bind*, *supra* note 10, at 1109-15.

38 Jack Welch, *Jack Welch: 'Rank-and-Yank'? That's Not How It's Done*, WALL ST. J. (Nov. 14, 2013), https://www.wsj.com/articles/8216rankandyank8217-that8217s-not-how-it8217s-done-1384473281.

39 *See* NAOMI CAHN, JUNE CARBONE, & NANCY LEVIT, SHAFTED: WHY WOMEN LOSE IN A WINNER-TAKE-ALL WORLD ___ (forthcoming 2021 Simon & Schuster); Welch, *supra* note 38.

influential, with over half of publicly traded companies in America adopting it.[40] The specific system has since fallen out of favor; still, variable pay remains the norm, with bonus pay in the form of stock options or year-end cash grants often dwarfing base pay for higher level employees in tech, finance and other fields.[41] Such awards, as Jack Welch emphasized, allow corporate CEOs to incentivize their priorities.

Introducing such high-stakes bonus systems changes firm dynamics. Lynne Dallas observes that such systems, particularly where employees feel they are in competition with each other, produces a greater emphasis on self-interest, higher levels of distrust that undermine teamwork, greater homogeneity in the selection of corporate management, less managerial accountability and more politicized decision-making.[42] In short, "supposedly meritocratic bonus systems have been found to replicate many of the attributes of 'old boys clubs' that protect insiders at the expense of outsiders."[43]

Even without the extremes of an Enron or a GE, competitive workplaces can lead to "masculinity contest cultures"[44] that pit employees against each other in high stakes, negative sum competition, that often lower morale and increasing turnover.[45] Such cultures emphasize the internal competition between employees, including, for example, an emphasis on long hours as proof of devotion to the firm, over more job-related performance measures.[46] These cultures often select for bosses who thrive in such competitive environments and bully or harass their subordinates, particularly women and less traditional men.[47] Where such cultures take hold, turnover, sexual harassment, and demoralization increase – and diversity may be harder to maintain.[48]

Critics of performance pay emphasize that these systems also change the characteristics of the employees who rise to the top. Such systems become more likely to select for narcissism and overconfidence bias and less likely to select for humility, honesty, or empathy.[49] Studies find that

---

[40] Alan Murray, *Should I Rank My Employees?*, WALL ST. J. GUIDES, http://guides.wsj.com/management/recruiting-hiring-and-firing/should-i-rank-my-employees/ [https://perma.cc/7Q99-AULE].

[41] Lawrence Mishel & Julia Wolfe, *CEO Compensation Has Grown 940% Since 1978: Typical Worker Compensation Has Risen Only 12% During That Time*, EPI (Aug. 14, 2019), https://www.epi.org/publication/ceo-compensation-2018/.

[42]. Dallas, *Enron*, *supra* note 23, at 37.

[43] Carbone, Cahn, & Levit, *Gender and the Tournament*, *supra* note 13.

[44] *See* Jennifer L. Berdahl et al., *Work as a Masculinity Contest*, 74 J. SOC. ISSUES 422, 422 (2018).

[45] *See id.* at 429 (observing that masculinity contests are "most prevalent—and vicious—in male-dominated occupations where extreme resources (fame, power, wealth) or precarious resources . . . are at stake . . . .").

[46] *Id*. at 430.(observing that "men compete at work for dominance by showing no weakness, demonstrating a single-minded focus on professional success, displaying physical endurance and strength, and engaging in cut-throat competition.")

[47] *Id.* at 428 ("The need to repeatedly prove masculinity can lead men to behave aggressively, embrace risky behaviors, sexually harass women (or other men), and express homophobic attitudes, when men feel that their masculinity is threatened.").

[48] *See* Peter Glick et al., *Development and Validation of the Masculinity Contest Culture Scale*, 74 J. SOC. ISSUES 449, 449 (2018).

[49] Tomas Chamorro-Premuzic, *Why Do So Many Incompetent Men Become Leaders?*, HARV. BUS. REV. (Aug. 22, 2013), https://hbr.org/2013/08/why-do-so-many-incompetent-men [https://

greater power diminishes functional empathy—higher social status and situational power are "associated with a reduced tendency to comprehend how other individuals see the world, think about the world, and feel about the world."[50] It turns out that these traits describe a distinct subset of the general population that is much more likely to be male[51] – and more likely to discriminate against outsiders.[52]

Accordingly, corporate environments that place greater emphasis on zero (or worse, negative) sum competition systems introduce a reinforcing set of effects. As law professor Donald Langevoort explained, traits "such as over-optimism, an inflated sense of self-efficacy and a deep capacity for ethical self-deception . . . are survival traits, not weaknesses, in a very Darwinian business world."[53] Such business worlds tend to select not just for men, but for a certain type of male leader, a type of leader who is also more likely than other men to drive women out. And while bonus pay systems vary, they tend to be associated with greater gender pay disparities, further affecting the ability to retain female employees.[54]

The net effect of these environments, which produce cutthroat corporate cultures, an emphasis on long hours as an end in themselves, and the promotion of misogynist managers, may literally be boys' clubs. The McKinsey/Lean In survey of more than 300 firms and 40,000 employees found that the percentage of women decreases at every step along the management pipeline, beginning at 47% at the entry level and ending at 21% of the C-Suite positions.[55]

This analysis above suggests that the presence of women – and often other underrepresented groups – in upper management is likely to be associated with better firm financial performance because of the dynamic described above. The most pernicious management

---

perma.cc/9QBH-ZW27]; (observing that "when it comes to leadership, the only advantage that men have over women . . . is the fact that manifestations of hubris—often masked as charisma or charm—are commonly mistaken for leadership potential, and that these occur much more frequently in men than in women.").

[50] Adam D. Galinsky et al., *Power and Perspectives Not Taken*, 17 PSYCHOL. SCI. 1068, 1072 (2006). *See also* DACHER KELTNER, THE POWER PARADOX 101 (2016)(identifying "The Abuses of Power" as: "Power leads to empathy deficits and diminished moral sentiments;" "Power leads to self-serving impulsivity;" "Power leads to incivility and disrespect;" and "Power leads to narratives of exceptionalism.").

[51] Emily Grijalva et al., *Gender Differences in Narcissism: A Meta-analytic Review*, 141 PSYCHOL. BULL. 261, 283 (2015); *See* Lynn A. Stout, *Killing Conscience: The Unintended Behavioral Consequences of 'Pay for Performance,'* 39 J. CORP. L. 2, 11, 35 (Mar. 2014).

[52] Berdahl et al., *supra* note 44, at 435 (concluding that those who *thrive* in such environments tend to identify with the workers who have the same traits they see in themselves, and to exploit others' weaknesses, leading to the "exclusion and harassment toward historically disadvantaged groups and men with resistant masculinities.")

[53] Langevoort, *supra* note 16, at 288 .

[54] Mita Goldar et al., *Rethinking Gender Pay Inequity in a More Transparent World,* ADP RES. INST. 2 (Aug. 2020), https://www.adpri.org/wp-content/uploads/2020/08/21032437/Rethinking-Gender-Pay-Inequity-in-a-More-Transparent-World-Exec-Summary.pdf; Stefania Albanesi, *How Performance Pay Schemes Make the Gender Gap Worse,* WORLD ECON. FORUM (Dec. 23, 2015), https://www.weforum.org/agenda/2015/12/how-performance-pay-schemes-make-the-gender-gap-worse/.

[55] McKinsey & Co., *Women in the Workplace 2020,* (Sept. 30, 2020), https://www.mckinsey.com/featured-insights/diversity-and-inclusion/women-in-the-workplace.

techniques, such as earnings management, stock buybacks,[56] and other practices focused on the shortterm at the expense of a company's long term health depend on the CEO's ability to enlist the support of a small group of insiders to subvert standard business practices.[57] The CEO's most common way of identifying compatriots is through high stakes incentive pay that allows the CEO to signal the desired performance and reward it, without being directly involved in questionable behavior.[58] Even if the company is not engaged in illegal practices, the internal competition pits employees against each other, undermining cooperation and trust[59] and often leading to the promotion of what business psychology professor Tomas Chamorro-Premuzic suggests is too many "incompetent men."[60]

II. The Business Case for Diversity

The business case for diversity combines the commitment to diversity as a moral obligation with the argument that diverse institutions produce better results. Promoting diversity, in accordance with this argument, produces win-win outcomes; business entities can to "do the right thing" and promote diversity at no cost to the bottom line. This argument has become increasingly influential; it has led to efforts to mandate greater diversity on corporate boards. California has joined a number of European and Asian countries requiring a minimum percentage of women on the governing boards of publicly traded companies.[61] Some jurisdictions, including California, have gone further and added quotas for other underrepresented groups.[62]

The pure "business case," however, faces two significant limitations: first, it is difficult to prove that it is diversity per se that causes the improvements, and second, even if diversity in fact accounts for the outcomes, an explanation is missing for why the appropriate focus should be on diversity on corporate boards, rather than in upper management. This section examines the existing empirical basis for the business claims in the light of the analysis in Section. It describes the empirical work linking diversity to better business outcomes, acknowledges the

[56]William Lazonick, Mustafa Erdem Sakinç, & Matt Hopkins, *Why Stock Buybacks Are Dangerous for the Economy*, HARV. BUS. REV. (Jan. 7, 2020), https://hbr.org/2020/01/why-stock-buybacks-are-dangerous-for-the-economy ("With the majority of their compensation coming from stock options and stock awards, senior corporate executives have used open-market repurchases to manipulate their companies' stock prices to their own benefit").

[57] Carbone & Black, *supra* note 7, at 456-57 (describing the role of the CEO in creating "criminogenic" environments). This is particularly true where the conduct involves plausibility deniability with respect to illegal or unethical conduct. *Id*. (describing plausible deniability). Even where the conduct is perfectly legal and visible, as with stock buybacks or layoffs, however, it may involve neutralizing internal opposition.

[58] *Id*. at 469-70 (describing practices that give subordinates substantial authority without oversight).

[59]. Dallas, *Enron, supra* note 23, at 37.

[60] TOMAS CHAMORRO-PREMUZIC, WHY DO SO MANY INCOMPETENT MEN BECOME LEADERS? 172-73 (2019).

[61] Anne Steele, *California Rolls Out Diversity Quotas for Corporate Boards*, WALL ST. J. (Oct. 2, 2020 12:01AM), https://www.wsj.com/articles/california-rolls-out-diversity-quotas-for-corporate-boards-11601507471. *See also* Jennifer Rankin, *EU Revives Plans for Mandatory Quotas of Women on Corporate Boards*, GUARDIAN (Mar. 5, 2020), https://www.theguardian.com/world/2020/mar/05/eu-revives-plans-for-mandatory-quotas-of-women-on-company-boards. Other states have introduced legislation to increase the representation of women on corporate boards. *Women on Corporate Boards: Quick Take*, CATALYST (Mar. 13, 2020), https://www.catalyst.org/research/women-on-corporate-boards/.

[62] In this article, we focus specifically on women. Some of the argument we are making applies to other underrepresented groups and some of it does not.

methodological limitations, and concludes, that in explaining outcomes, the links between the factors that promote pernicious business practices and those obstruct efforts to promote greater diversity may be so deeply intertwined as to be impossible to separate. We conclude that the factors we describe in Section I, rather than diversity as an end in itself, therefore form the core of the instrumental case for diversity.

A. Corporate Boards

There is increasing scholarly inquiry into whether diverse firms outperform less diverse firms.[63] The easy (and uncomplicated) answer appears to be that diversity pays; more diverse firms, measured by the percentage of women on corporate boards, outperform those with fewer women, when performance is measured by factors such as returns to equity or other measures of financial performance.[64] The studies, however, particularly once they attempt to control for factors other than the mere presence of women, are not uniform in finding better performance. In short, the studies do not (and we will argue cannot) demonstrate that it is the presence of women per se that that causes better results.[65] Instead, the arrows linking diversity to better performance may run in multiple directions. It may be, for example, that better managed companies are more likely to achieve greater diversity, rather than from diversity leading to better company performance.[66] It is also possible that the presence of women is associated with better management practices for reasons that empirical studies find difficult to tease out. It is entirely possible that better-run firms hire more women rather than that the women themselves necessarily cause the better outcomes.[67] The research that gained initial attention focused on corporate boards. Perhaps the most influential of the early studies is one performed by Catalyst.[68] This widely-cited study examined Fortune 500 companies from 2001 to 2004, determined the percentage of women on the

---

[63] *See, e.g.*, Vijay Eswaran, *The Business Case for Diversity in the Workplace Is Now Overwhelming*, WORLD ECON. FORUM (Apr. 29. 2019). https://www.weforum.org/agenda/2019/04/business-case-for-diversity-in-the-workplace/

[64] Alice H. Eagly, *When Passionate Advocates Meet Research on Diversity, Does the Honest Broker Stand a Chance?*. 72 J. SOC. ISSUES 199, 201 (2016).

[65] For a summary of the research, see *id.*.

[66] Juan M. Garcua Lara et al., *The Monitoring Role of Female Directors over Accounting Quality*, J. CORP. FIN. (May 30, 2017), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2732588 ("Using a large sample of UK firms we find that a larger percentage of women among independent directors is significantly associated with lower earnings management practices. However, we show that this relation disappears if we focus on firms that do not discriminate against women in the access to directorships.").

[67] And there any number of other confounding correlations. For example, most studies find hat large companies have more diversity on boards. Large companies may become large because they are better run or they may find it easier to increase diversity by simply adding more members to their boards. Either way, the presence of more women may not be the proximate cause of financial performance. *See, e.g.*, Eagly, *id.* at 202 (noting that large firms have more women on their boards and that the failure to control for firm size skews the results of some studies); McKinsey & Co., *Delivering Through Diversity* (Jan. 2018), https://www.mckinsey.com/~/media/mckinsey/business%20functions/organization/our%20insights/delivering%20through%20diversity/delivering-through-diversity_full-report.ashx#:~:text=We%20found%20that%20companies%20with,likely%20to%20experience%20higher%20profits.

[68] CATALYST, THE BOTTOM LINE: CORPORATE PERFORMANCE AND WOMEN'S REPRESENTATION ON BOARDS (2007), *archived at* http://perma.cc/ZP5N-PA3E (finding a positive relationship between gender diversity on corporate boards and firm performance).

firm boards, and found that companies in the highest quartile of female representation outperformed those in the lowest quartile.[69] The study, however, simply reported the differences between the two groups without any effort to include control variables that might explain the results, and acknowledged that the correlation could not establish that it was the presence of women per se that caused the better performance.[70] Indeed, the strength of the relationships did not hold up in Catalyst's follow-up study, looking at the same relationships during the 2004-2008 time period.[71] A later Credit Suisse Research Institute Study looking at over 2000 firms across the globe also found that firms with at least one woman on the board outperformed firms with all-male boards, reporting that among firms with a market capitalization of over $10 billion, the firms with female board representation had a 26% better performance in share price.[72] This study, too, lacked controls that might identify causal factors, and some scholars suspect that larger firms may find it easier to recruit and retain female board members in ways that skew the results.[73] A number of studies have shown similar correlations.[74]

While other studies have found a positive relationship using more sophisticated statistical techniques, some have not.[75] Overall, "an accurate description of this extensive empirical literature is that correlational findings relating percentages of women on corporate boards to firms' financial performance are mixed, and on the average lean very slightly in the positive direction but

---

[69] *Id*. at 1.

[70] Terry Morehead Dworkin & Cindy A. Schipani, *The Role of Gender Diversity in Corporate Governance* , 21 U. PA. BUS. L. 105, 107 (2018) ("Some industry studies, like those conducted by Catalyst, include an explicit footnote that 'correlation does not prove or imply causation.'").

[71] *See* Deborah L. Rhode & Amanda K. Packel, *Diversity on Corporate Boards: How Much Difference Does Difference Make?,* 39 DEL. J. CORP. L. 377, 384 (2014) (critiquing the study's limitations).

[72] CREDIT SUISSE RES. INST., GENDER DIVERSITY AND CORPORATE PERFORMANCE 12-16 (Aug. 2012), *archived at* http://perma.cc/TC6U-FAH2.

[73] Rhode & Packel, *supra* note 71, at 386 (noting lack of controls). *See also* Eagly, *supra* note 63, at 202 (speculating on the impact of firm size on studies of this type).

[74] For example, the Morgan Stanley Capital International found that U.S. companies with at least three women on the board in 2011 experienced median gains in return on equity of 10% and earnings per share of 37% over a five year period, whereas companies that had no female directors in 2011 showed median changes of -1% in return on equity and -8% in earnings per share over the same five-year period. *See* Meggin Thwing Eastman et al., *The Tipping Point: Women on Boards and Financial Performance* 3, MSCI (Dec. 2016), https://www.msci.com/documents/10199/fd1f8228- cc07-4789-acee-3f9ed97ee8bb (analyzing U.S. companies that were constituents of the MSCI World Index for the entire period from July 1, 2011 to June 30, 2016). The 2018 Calvert report found that, over an eleven-year period, "companies with higher percentage of Women in Leadership positions (WLP) and higher [percent] of Women in Board positions (WBD) outperform companies with the lowest [percent] of WLP and WBD as measured by ratios" for returns on sales, returns on assets, and returns on equity. noting that 33%-70% was the critical number. *Just Good Investing* 11, CALVERT IMPACT CAPITAL (Dec. 2018), https://www.calvertimpactcapital.org/storage/documents/calvert-impact-capital-gender-report.pdf. The report also noted that it was not just the number of women in leadership or in board positions that mattered to returns, but the ratio of women to men: "Once a borrower exceeds 33% WLP, we observe a more significant increase in financial performance that tapers off around 70% WLP." *Id.* at 12.

[75] *See* Rhode & Packel, *supra* note 71, at 385-86 (summarizing the studies finding a positive relationship); *id.* at 387-390 (summarizing the studies finding either no relationship or a negative one); *id.* at 384 (Rhode and Packel conclude: "[d]espite increasing references to acceptance of the business case for diversity, empirical evidence on the issue is mixed").

only for companies' accounting outcomes," though not necessarily other factors such as returns to equity.[76] In the international context, the relationship between female board representation and market performance is stronger in countries with greater gender equality.[77] The varying results reflect differences in methodology, sample selections, and time periods.[78]

Relatively few of the studies attempt to tease out causation and doing so is difficult. For one thing, "women" are hardly a single uniform category; the women on one board may not be identical to the women on other boards. As a general matter, women appointed "to corporate boards may not in fact differ very much in their values, experiences, and knowledge from the men."[79] A study in 2019 by Crunchbase, Him for Her, and Kellogg Professor Lauren Rivera of privately-held companies showed that women on boards are more likely to be independent members rather than investors or members tied to management.[80] This suggests they are less likely to be either CEO acolytes or hedge fund activists pushing a short term agenda. Accordingly, any rigorous study would have to look not just at the overall number of women, but what type of women produced the best results – any women, the women most similar to the men, or women who bring distinctly different perspectives?[81]

For another, the most important causal relationships, including those producing statistically significant results, almost always involve multiple factors with different effects. This may be intrinsic in this type of research because of the difficulty in ruling out endogeneity – the possibility, for example, that an unidentified factor influenced both better financial performance and greater diversity.[82] Nonetheless, the studies that attempt to identify potential causal factors are intriguing to the extent they identify characteristics that may be associated with alternative – and potentially better – *management practices.*

The single factor that comes up most frequently in studies of the relationship between board diversity and firm performance is increased monitoring. Adams and Ferreira found in 2009 that the presence of women on corporate boards was associated with better attendance at board meetings and closer company monitoring.[83] The greater monitoring increased the likelihood that

---

[76] Eagly, *supra* note 64, at 203 (defining accounting outcomes as profit and loss). *See also* Paul Gompers & Silpa Kovvali, *The Other Diversity Dividend*, HARV. BUS. REV. (July-Aug. 2018), https://hbr.org/2018/07/the-other-diversity-dividend characterizing the metanalyses as producing results that are "either non-existent (effectively zero) or very weakly positive."

[77] *Id.*

[78] *Id*. at 390 (concluding that "the empirical research on the effect of board diversity on firm performance is inconclusive" and that the "mixed results reflect the different time periods, countries, economic environments, types of companies, and measures of diversity and financial performance."). .

[79] *Does Gender Diversity on Boards Really Boost Company Performance?*, KNOWLEDGE@WHARTON (May 18, 2017), https://knowledge.wharton.upenn.edu/article/will-gender-diversity-boards-really-boost-company-performance/.

[80] Ann Shepherd & Gene Teare, *2020 Study of Gender Diversity on Private Company Boards*, CRUNCHBASE (Mar.1, 2021), https://news.crunchbase.com/news/2020-diversity-study-on-private-company-boards/.

[81] *See, e.g.*, Gompers & Kovvali, *supra* note 77, https://hbr.org/2018/07/the-other-diversity-dividend (describing how homogenous venture capital firms tend to be, with Harvard Business School graduates dominating the firms).

[82] Eagly, *supra* note 64, at 202. Investopedia defines an "endogenous variable" as "a variable in a statistical model that's changed or determined by its relationship with other variables within the model." https://www.investopedia.com/terms/e/endogenous-variable.asp

[83] Eagly, *supra* note 64, at 202 (referring to a study by Renée Adams and Daniel Ferreira and observing that women board members had higher attendance rates at board meetings, were more likely to serve on monitoring committees,

CEOs would resign after poor company performance.[84] The same study, however, also found that increased monitoring was associated with weaker performance in stronger firms, producing a negative aggregate effect.[85] The authors could not explain the overall negative result, indicating their inability to rule out investor bias in the stronger firms – or other unidentified factors – in producing the negative results.[86] The significance of the study, for our purposes, is that it found that greater monitoring is correlated both with the greater presence of women and with firm performance (both positively and negatively). What it did not explain was why the factor is correlated with the greater presence of women, or why it produced stronger performance in weak firms and weaker performance in strong firms. What it suggested, however, is that when more women are present, more monitoring takes place, and more monitoring correlates with changed business performance.

Subsequent studies have contributed to the explanations of why factors associated with greater diversity such as monitoring might explain the relationship between diversity and stronger firm performance. In its report advocating gender diversity, Nasdaq reviewed elements associated with gender diversity that may explain the impact of diversity on firm performance. A 2015 study, for example, found "strong evidence" that a greater number of women on boards was correlated with less securities fraud.[87] A later study suggested gender diversity is associated with stronger

---

and these factors correlated with more monitoring, and better performance at low performing companies); *see also* Renée B. Adams & Daniel Ferreira, *Women in the Boardroom and Their Impact on Governance and Performance*, 94. J. FIN. ECON. 291, 291-92 (2009) (describing the impact on board performance, and finding that while more gender-diverse boards allocated more resources to monitoring, the "average effect of gender diversity on firm performance is negative. This negative effect is driven by companies with fewer takeover defenses").

[84] Eagly, *supra* note 64, at 202 (observing that women board members had higher attendance rates at board meetings, were more likely to serve on monitoring committees, and these factors correlated with more monitoring, and better performance at low performing companies). One reason for the correlation between more gender-diverse boards and increased monitoring is some indication that women may be more conscientious about attendance and demonstrate greater responsibility for oversight efforts. Adams and Ferreira note:

> Women appear to behave differently than men with respect to our measure of attendance behavior. Specifically, women are less likely to have attendance problems than men. Furthermore, the greater the fraction of women on the board is, the better is the attendance behavior of male directors. Holding other director characteristics constant, female directors are also more likely to sit on monitoring-related committees than male directors. In particular, women are more likely to be assigned to audit, nominating, and corporate governance committees, although they are less likely to sit on compensation committees than men are.

Adams & Ferreira, *supra* note 83, at 292. Other commentators have theorized that women have been trained toward detail orientation and are more likely to "engage in constructive dissent." Sandeep Gopalan & Katherine Watson, *An Agency Theoretical Approach to Corporate Board Diversity*, 52 SAN DIEGO L. REV. 1, 17 (2015).

[85] *Id.*

[86] *Id.* (observing that institutional investors are often attentive to board governance).

[87] *See* Douglas J. Cumming et al., *Gender Diversity and Securities Fraud*, 58 ACAD. MGMNT J. 34 (Feb. 9, 2015), https://ssrn.com/abstract=2562399 (analyzing China Securities Regulatory Commission data from 2001 to 2010, including 742 companies with enforcement actions for fraud, and 742 non-fraudulent companies for a control group).

internal controls over financial reporting.[88] Some studies found correlations between the percentage of women on audit committees and the better reporting results,[89] while other studies suggested that more female board members produced better monitoring even if women board members did not sit on the audit committees directly.[90] The Nasdaq report also found board gender diversity "to be positively associated with more transparent public disclosures."[91] What all of these studies have in common is that they found that greater diversity is linked with greater transparency, more accurate reporting – and less fraud. Nasdaq concluded:

> There is substantial evidence that board diversity enhances the quality of a company's financial reporting, internal controls, public disclosures and management oversight. In reaching this conclusion, Nasdaq evaluated the results of more than a dozen studies spanning more than two decades that found a positive association between gender diversity and important investor protections, and the assertions by some academics that such findings may extend to other forms of diversity, including racial and ethnic diversity.[92]

In short, Nasdaq reported that firms with greater diversity were less likely to be engaged in the practices most closely associated with short-termism and competitive pay: earnings management, accounting manipulation and fraud, and the suborning of internal controls.[93]

An Australian study looked at different factors, finding that adding women to boards strengthened a company's willingness to take prosocial actions, which produced higher levels of corporate social responsibility (CSR). CSR, in turn, was positively linked to financial performance. Once the study controlled for the CSR effect, the women's impact on firm performance became statistically insignificant. The study concluded that increasing CSR, not the

---

[88] *See* Yu Chen et al., *Board Gender Diversity and Internal Control Weaknesses*, 33 ADVANCES IN ACCT. 11 (2016) (analyzing a sample of 4267 firm-year observations during the period from 2004 to 2013, beginning "the first year internal control weaknesses were required to be disclosed under section 404 of SOX" [Sarbanes-Oxley]).

[89] *See* Maria Consuelo Pucheta-Martínez et al., *Corporate Governance, Female Directors and Quality of Financial Information*, 25(4) BUS. ETHICS: EUR. REV. 363, 363, 378 (2016) (analyzing a sample of non-financial companies listed on the Madrid Stock Exchange during 2004-2011) (finding that "the percentage of females on [audit committees] reduces the probability of [audit] qualifications due to errors, non-compliance or the omission of information.").

[90]NASDAQ, *supra* note 1, at 25, citing Chen et al., *supra* note 89; Aida Sijamic Wahid, *The Effects and the Mechanisms of Board Gender Diversity: Evidence from Financial Manipulation*, J. BUS. ETHICS (forthcoming) (Dec. 2017); Rotman School of Management Working Paper No. 2930132 at 1, https://ssrn.com/abstract=2930132 (analyzing 6,132 U.S. public companies during the period from 2000 to 2010, for a total of 38,273 firm-year observations).

[91] NASDAQ, *supra* note 1, at 27-28 ("Gul, Srinidhi & Ng (2011) concluded that "gender diversity improves stock price informativeness by increasing voluntary public disclosures in large firms and increasing the incentives for private information collection in small firms."66 Abad et al. (2017) concluded that companies with gender diverse boards are associated with lower levels of information asymmetry, suggesting that increasing board gender diversity is associated with "reducing the risk of informed trading and enhancing stock liquidity.").

[92] *Self-Regulatory Organizations; The Nasdaq Stock Market LLC; Notice of Filing of Proposed Rule Change to Adopt Listing Rules Related to Board Diversity* 22, SECURITIES & EXCHANGE COMM'N (Dec. 4, 2020), https://www.sec.gov/rules/sro/nasdaq/2020/34-90574.pdf.

[93] *See supra* discussion in text at notes 20-30, 56.

presence of women per se, turned out to be the decisive factor on firm performance.[94] Nonetheless, although it is difficult to establish the causal mechanism,[95] it appears that "female directors tend to be less conformist and are more likely to exhibit activism and express their independent views than male directors because they do not belong to 'old-boy' networks."[96] The relationship between gender diversity and CSR is stronger than that "between gender diversity and company performance."[97] This effect, as the authors of the Australian study suggest, may depend less on the presence of women than on which women are selected. Nonetheless, the study finds that greater diversity, whatever the cause, tends to counter an exclusive focus on shareholders to the exclusion of other stakeholders who might affect the company's long-term prospects.

These studies cannot tease out the effect women board members have on financial reporting with any precision. Instead, the relevant factors the studies identify are associated with both the presence of more women and better business performance. Any casual relationships are likely to be multidirectional. Firms that operate in a more transparent way may be more hospitable to diverse boards, and firms that diversify by bringing in board members through less conventional networks – or simply networks less closely tied to existing management -- may find that their new board members ask different questions and probe in different ways from board members who rise through more insular networks. The issue of the relationship between board diversity and performance may thus be more about openness to outsiders than about the inclusion of women per se.[98]

B. The Business Case for Diverse Management

---

[94] Jeremy Galbreath, *Is Board Gender Diversity Linked to Financial Performance? The Mediating Mechanism of CSR*, 57 BUS. & SOC'Y 863 (2018).

[95] "It's worth noting that even *if* the meta-analyses revealed a stronger relationship between board gender diversity and firm performance, we couldn't conclude that board gender diversity *causes* firm performance. To establish causal effects, you need to conduct a randomized control trial. But, that's impossible here; we can't randomly assign board members to companies." *Does Gender Diversity on Boards Really Boost Company Performance?*, *supra* note 79. Indeed, "The women named to corporate boards may not in fact differ very much in their values, experiences, and knowledge from the men who already serve on these boards." *Id.*

[96] Jie Chen et al, *Why Female Board Representation Matters: The Role of Female Directors in Reducing Male CEO Overconfidence*, 53 J. EMPIRICAL FIN. 70 (2019).

[97] *Does Gender Diversity on Boards Really Boost Company Performance?*, *supra* note 79.

[98] *See, e.g.*, Barbara Shecter, *Diverse Boards Tied to Fewer Financial 'Irregularities,' Canadian Study Finds*, FIN. POST (Feb. 5, 2020), https://business.financialpost.com/news/fp-street/diverse-boardstied-to-fewer-financial-irregularities-canadian-study-finds ("If you're going to introduce perspectives, those perspectives might be coming not just from male versus female. They could be coming from people of different ages, from different racial backgrounds . . . [and] [i]f we just focus on one, we could be essentially taking away from other dimensions of diversity and decreasing perspective"). On avoiding groupthink, see Lynne L. Dallas, *Does Corporate Law Protect the Interests of Shareholders and Other Stakeholders?: The New Managerialism and Diversity on Corporate Boards of Directors*, 76 TUL. L. REV. 1363, 1391 (2002); *See also* AARON A. DHIR, CHALLENGING BOARDROOM DIVERSITY: CORPORATE LAW, GOVERNANCE, AND DIVERSITY 124, 150 (2015) (emphasis removed) (sample included 23 directors of Norwegian corporate boards, representing an aggregate of 95 board appointments at more than 70 corporations); Gennaro Bernile et al., *Board Diversity, Firm Risk, and Corporate Policies* 38 (Mar. 6, 2017), https://ssrn.com/abstract=2733394 (analyzing 21,572 firm-year observations across non-financial, non-utility firms for the years 1996 to 2014, based on the ExecuComp, RiskMetrics, Compustat and CRSP databases)..

A primary purpose of corporate boards is monitoring, and abuses such as earnings manipulation and accounting fraud cannot flourish once boards shine a spotlight on the practices; at that point, a series of processes come into play that are likely to lead to reform of those practices.[99] Accordingly, to the extent more diverse boards are more inclined to look into the shadows of corporate operations, the more likely they are to discover abuses – with benefits for the long-term health of companies.[100]

The case for diverse management is more complex. Management sets the tone for the entire company. As we indicated in Section I, corporate reformers have focused on high stakes bonuses systems as a source of both ineffective management and workplaces hostile to diversity. These systems, whether at corrupt companies like Enron[101] or more conventional companies like Microsoft,[102] have been identified with greater distrust, higher turnover, lower productivity, lesser diversity, and greater gender disparities in compensation.[103] Such systems tend to emphasize reductionist, short-term, transactional metrics: Jack Welch, for example, at the height of GE's earnings management era, emphasized how important it was that his managers "hit their numbers." At their worst, these systems encourage "masculinity contest cultures" that produce higher turnover, sexual harassment, bullying and lower morale.[104] The literature on diversity and upper management should accordingly be interpreted through this lens.

The studies show that diverse management, just like diverse boards, creates value in multiple ways: it leads to greater profitability, market share growth, and more inclusive organizational cultures.[105] These analyses, however, suffer from the same issues that affect studies of corporate boards: the correlations have been repeatedly documented while causation is difficult to establish. Like the board literature, they also point to certain management factors as potential causal factors associated with both greater diversity and better firm performance.

Some of the most influential studies look at the relationship between diversity and performance without controls that attempt to establish causation. The *Wall Street Journal*, for example, in a 2019 study, ranked the diversity of S&P 500 companies and then compared the most- and least-diverse companies along various performance metrics.[106] The top twenty companies, with the greatest amount of diversity, had an annual return in share performance of 10% over a

---

[99] While the risk of liability for corporate board members is typically low, participation in or countenance of fraud can expose directors to liabilty. Urska Velikonja, *Leverage, Sanctions, and Deterrence of Accounting Fraud*, 44 U.C. DAVIS L. REV. 1281, 1328 (2011).

[100] *See, e.g.,* Michael C. Jensen, *Paying People to Lie: the Truth About the Budgeting Process*, 9 EUR. FIN. MGMT. 379 (2003), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=267651 (explaining that accurate accounting increases corporate performance). .

[101] Dallas, *Enron*, *supra* note 23, at 37.

[102] Carbone, Cahn, & Levit, *Gender and the Tournament*, *supra* note 13, at 1159.

[103] *See supra* discussion in Section I, at 5-7, 45-46.

[104] *See supra* discussion in Section I, at 5-7, 47.

[105] Indeed, many companies achieve a significant degree of diversity in their entry level ranks without much diversity in their more significant decision-making levels. McKinsey & Co., *Delivering Through Diversity* (Jan. 2018), https://www.mckinsey.com/~/media/mckinsey/business%20functions/organization/our%20insights/delivering%20through%20diversity/delivering-through-diversity_full-report.ashx#:~:text=We%20found%20that%20companies%20with,likely%20to%20experience%20higher%20profit.

[106] Dieter Holger, *The Business Case for More Diversity*, WALL ST. J. (Oct. 26, 2019), https://www.wsj.com/articles/the-business-case-for-more-diversity-11572091200.

five-period and 14% over a ten-year period, compared to the twenty least-diverse firms' returns of 4.2% and 12%.[107]

Three studies by McKinsey (published in 2015, 2018, 2020) show a strong association between diversity and financial performance. The most recent such study focused on the companies in the top quartile for gender diversity on management teams and found that these companies "were 25 percent more likely to have above-average profitability than companies in the fourth quartile—up from 21 percent in 2017 and 15 percent in 2014."[108] A 2009 study found that racial workforce diversity is correlated positively with a range of economic indicators, including larger market share and greater sales revenues, while gender diversity also correlates with greater sales revenue and increased profits.[109] A Credit Suisse study similarly "demonstrated that investment returns are 10 percent higher at companies with policies inclusive of LGBT+ people."[110]

A meta-analysis of studies, however, by Jeong & Harrison, looked at 146 primary studies conducted in 33 different countries and found that "female representation in the upper echelons in general is positively and weakly related to forms of long-term financial performance, but negatively and weakly related to short-term stock market returns."[111] The meta-analysis found that there is a "short-term drop in stock market returns following the announcement of female CEO appointments, " rather than a response to firm performance.[112] Overall, the meta-analysis found that studies of upper management, much like board studies, produced mixed results; that is, once appropriate controls were added, much of the increased performance from greater diversity disappeared. There are, nonetheless, also intriguing indications of what some of the causal relationships might involve.

The meta-analysis's most important finding involved the comparison between short-term and long-term performance. Short-term performance appeared to reflect investor bias.[113] The authors asserted that long-term performance, on the other hand, involved firm decision-making that reduced strategic risk-taking and "explains why financial performance is improved."[114] They found correlations between greater inclusion of women in upper management and better decision-making, postulating that the inclusion of women moderated the tendency of all-male decision-

---

[107] *Id.*

[108] McKinsey & Co., *Diversity Wins: How Inclusion Matters* (May 19, 2020), https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters.

[109] Cedric Herring, *Does Diversity Pay?: Race, Gender, and the Business Case for Diversity,* 74 AM. SOCIOLOGICAL REV. 208 (2009)

[110] Stephanie Sandberg, *It's 2017: Do You Know Where Your LGBT+ Board Candidates Are?*, HUFFINGTON POST (Apr. 4, 2017), https://www.huffingtonpost.com/entry/its-2017-do-you-know-where-your-lgbt-board-candidates_us_58e3c8cbe4b09deecf0e1a91.

[111] Seung-Hwan Jeong & David A. Harrison, *Glass Breaking, Strategy Making, and Value Creating: Meta-Analytic Outcomes of Women as CEOs and TMT Members*, 60 ACAD. MGMNT. J. 1219, 1232-34 (2016). The largest group of studies was from the United States.

[112] *Id*. at 1234.

[113] *Id*. at 1233-34.

[114] *Id.*

making groups to take more risks, in part because of the tendency of homogeneous groups to reach more extreme conclusions.[115]

In explaining their conclusions, Jeong & Harrison hypothesized that it may not be women, per se, but the impact of greater diversity on deliberations that creates the causal effect. Other studies suggest that these results may be context dependent. In finance, for example, a major purpose of hedge funds and other investment firms is to manage risk, and there is no suggestion that women fund managers are more risk averse than the men in finance.[116] Indeed, women-run funds routinely outperform those run by men, with some observers attributing the differences to better decision-making practices.[117] Economist Cristian Dezsö, one of those who finds that funds run by women outperform those run by men, adds a different wrinkle to the analysis. His data show that women in women-dominant groups take more risks than women in male-dominant environments, suggesting that, freed from gender stereotypes, the women feel freer to do so.[118] In contrast with the Jeong and Harrison meta-analysis, though, he discovered that men also took greater risks when more women were present. "Borrowing a conclusion from psychology research," he speculated that men in finance "feel threatened when they see females taking on more risk. So, they respond by taking more risk, too."[119] Either way, these findings suggest it is the dynamic of the group rather than the sex of the decision-maker that determines outcome quality.[120]

Other studies of diversity find that these effects may vary by industry. In considering innovation, for example, the findings may be particularly robust. One study found "a strong and statistically significant correlation between the diversity of management teams and overall

---

[115] "Our meta-analytic path analysis shows this reduction in strategic risk-taking— empirically captured through financial leverage, capital expenditures, and stock volatility—is one reason why female representation is linked to improved financial performance in the long run." *Id.* at 1235. An underlying premise of the focus on risk-taking in the meta-analysis assumed that women are more risk averse. *Id.* at 1223 ("While several ´ studies report evidence that existing patterns of gender differences in risk-taking might not apply to some managerial contexts []), such evidence is outweighed by the larger and broader body of robust evidence which has established that females in general [], and in their roles as CEOs []), are risk-averse compared to males.") That assumption may not be accurate. *See* Lara et al., *supra* note 66.

[116] Michael Brush, *Here's Why Women Fund Managers Regularly Outperform Men, Based on Newer Research*, MARKETWATCH (Oct. 23, 2020 8:26 AM), https://www.marketwatch.com/story/heres-why-women-fund-managers-regularly-outperform-men-and-seven-stocks-thatll-help-you-do-the-same-11603382699.

[117] Eric McWhinnie, *Women Are Mostly Better Investors than Men*, USA TODAY (Mar. 9, 2014), https://www.usatoday.com/story/money/personalfinance/2014/03/09/women-better-investors-than-men/6176601/. *See also* Steve Garmhausen, *Women: Better Advisors?*, BARRON'S (June 2, 2012), https://www.barrons.com/articles/SB50001424053111904081004577438301140635494.

[118] *How Risk and Gender Affect Fund Manager Performance*, SMITH BRAIN TRUST (Oct. 28, 2020), https://www.rhsmith.umd.edu/faculty-research/smithbraintrust/insights/how-risk-and-gender-affect-fund-manager-performance.

[119] *Id*.

[120] Indeed, a different study attempting to tease out the relationship between women board members and risk in non-financial firms found no relationship once appropriate controls were introduced. *See* Vathunyoo Sila et al., *Women on Board: Does Boardroom Gender Diversity Affect Firm Risk?*,
36 J. CORP. FIN. 26-53 (2016).,

innovation." [121] The firms with greater than average diversity on their management teams "reported innovation revenue that was 19 percentage points higher than that of companies with below-average leadership diversity."[122] The study did not just consider gender diversity, however. It examined diversity across a number of different dimensions and found "the most significant gains came from changing the makeup of the leadership team in terms of the national origin of executives, range of industry backgrounds, gender balance, and career paths."[123] Hiring managers from a different industry and hiring more women had similarly positive effects on firm innovation.[124] Other studies, looking specifically at new ventures, have also found a relationship between a management team's gender diversity and the innovation performance of the firm.[125]

Like the studies of board diversity, the studies focused on management find that openness to different views matters. [126] They also found that "participative leadership" that encourages "frequent and open communication" and fair employment practices contributes to effective workplaces innovation.[127]

What these studies generally suggest is a contrast between the intense, competitive, negative sum workplaces that characterize masculinity contest cultures[128] and the more productive, innovative workplaces that pay greater attention to employee morale.[129] Economists George Akerlof and Rachel Kranton, for example, have argued that workers who think of themselves as insiders rather than outsiders require less in the way of extra compensation to produce desired results and become less likely to game the compensation systems that do exist.[130] They conclude that "[w]orker identification may therefore be a major factor, perhaps even the dominant factor, in the success or failure of organizations" and suggest that high stakes bonus systems are often counterproductive.[131] More conventional management theorists similarly emphasize factors such

[121] Rocio Lorenzo et al., *How Diverse Leadership Teams Boost Innovation*, BCG HENDERSON INST. (Jan. 23, 2018), https://www.bcg.com/publications/2018/how-diverse-leadership-teams-boost-innovation

[122] *Id.*

[123] *Id*.

[124] *Id.*

[125] Ye Dai et al., *The Direct and Indirect Impact of Gender Diversity in New Venture Teams on Innovation Performance*, 43 ENTREPRENEURSHIP THEORY & PRAC. 505 (2019).

[126] *Id.*

[127] *Id.* Other studies of gender based differences in leadership styles suggest that gender diverse leadership styles tend to be "more participative, democratic, and communal" and to encourage "more productive discourse and the airing of different points of view" than exclusively male leadership styles. Galbreath, *supra* note 94.

[128] "These cultures make winning at all cost the test of success, and tolerate self-interested, unethical and counterproductive behavior." Carbone & Black, *supra* note 7.

[129] *See, e.g.,* DONALD HISLOP, KNOWLEDGE MANAGEMENT IN ORGANIZATIONS 230 (2013) (describing how the most effective way to deal with problems such as employee turnover is to develop institutional identity and employee loyalty and observing that institutional identity that encourages employees to identify with firm objectives creates stronger loyalty than instrumental measures such as merit pay or bonuses).

[130] GEORGE AKERLOF & RACHEL KRANTON, IDENTITY ECONOMICS: HOW OUR IDENTITIES SHAPE OUR WORK, WAGES, AND WELL-BEING 59 (2010).

[131] *Id.*

as engaging workers, staying committed, creating trust and keeping open lines of communication.[132]

A meta-analysis of management styles, for example, found that for both men and women, "transformational" practices that communicate a compelling vision and pay attention to subordinates' individual needs produce the strongest positive results.[133] In contrast, managers who rely on a "transactional" approach based on incentive systems, bottom line metrics defining organizational objectives, and attention to problems rather than successes do not do as well.[134] Women leaders were more likely than the men to adopt transformational leadership styles.[135] The study authors speculate that this may be true, in part, because transformational styles conformed more closely to female gender stereotypes and thus women who adopted other styles faced greater challenges from role incongruity.[136] The authors conclude that the differences in leadership styles may explain why some studies find women to be more effective leaders – the women who rise through the leadership ranks tend to use (and may be selected because they use) more effective techniques than the men; techniques, however, that work for men just as well as women.[137]

These studies suggest that adding women – and, indeed, increasing diversity generally – can have a positive impact on corporate performance, but that it may not simply be the presence of women per se that has the effect. Instead, it is the interaction of diversity with the broader corporate context that produces the result.[138] Indeed, recruiting, retaining, and promoting women executives may require reforming the most destructive aspects of competitive business cultures and that may account for a significant part of the reason for the improved performance associated with greater diversity. [139]

III. Diversity as a Tool of Management Reform

The current generation of corporate reformers advocates both greater diversity as an end in itself and reforms that challenge shareholder primacy and its related emphasis on short-termism

---

[132] *See, e.g., 8 Best Practices in Business Management*, UNIV. OF ST. MARY, https://online.stmary.edu/mba/resources/8-best-practices-in-business-management (last visited Apr. 19, 2021). Eagly summarizes this is of leadership advice observing that "textual analysis of mass-market books on management shows, managers are exhorted to 'reorient themselves toward a new role of coordinating, facilitating, coaching, supporting, and nurturing their employees.'" Alice H. Eagly et al., *Transformational, Transactional, and Laissez-Faire Leadership Styles: A Meta-Analysis Comparing Women and Men*, 129 PSYCHOL. BULL. 569 (2003).

[133] Eagly et al., *supra* note 132, at 570-72.

[134] *Id*.

[135] *Id*. at 578-79.

[136] *Id*. at 572-73.

[137] *Id*. at 586.

[138] *See, e.g.,* Galbreath, *supra* note 94 (suggesting that increasing the representation of women on boards increase the corporate focus on community social responsibility and that doing so increases performance over time).

[139] For an example of a destructive workplace culture that combines seven figure bonuses, unethical conduct and gender disparities, *see* Complaint, Messina v. Bank of Am. Corp., et al., (S.D.N.Y. 2016) (No. 1:16cv3653)

and bonus-based competitive pay.[140] Given the lack of conclusive findings on the impact of diversity in isolation, the classic justifications for greater diversity combine a moral case for diversity (including those who have been systematically excluded in the past is the right thing to do) and a business case for diversity (more diverse firms, at worst, do as well as other companies and at best do better so there is no reason not to pursue diversity). This article, however, suggests that while social science research cannot isolate causal links in a statistically rigorous way, it can identify the circumstances in which management reform and diversity efforts are most likely to reinforce each other.

A. Finding the Buried Bodies

The literature on corporate boards suggests that the correlations between greater diversity and improved medium to long-term firm performance may involve greater monitoring and a lesser incidence of accounting irregularities, earnings management, and fraud.[141] Companies that expand the number of diverse board members, particularly within a short period, may have to expand their search efforts to find board members, breaking the insularity of some existing boards. And, indeed, as we pointed out above, women are more likely to be appointed to independent board positions than to be appointed either from the hedge funds engaged in activist investing or the management board positions more directly under the control of the CEO.[142]

The impact of bringing in newcomers may be particularly great in companies that "manage" earnings, cover up unfavorable developments, disguise unethical conduct, or engage in legally dubious activities that create potential exposure to negative publicity, enforcement actions, or other risks.[143] Effective board monitoring is expected to police such activities; the creation of more diverse boards may well have maximum impact in circumstances where diversity recruiting increases the likelihood of effective monitoring or greater firm transparency. As we demonstrated in Sections I.B and II.B above, women who make it to upper management often demonstrate different qualities from the men who thrive in corporate tournaments. In addition, given the paucity of women in upper management, CEOs may be less able to handpick women they know well. So long as upper management is a boys' club, women board members are less likely to reflect the amoral, misogynist, narcissistic mindset that characterizes the corporate environments ripe for reform. Over time, of course, women on corporate boards may come to reflect the same perspectives as the men. Indeed, corporate board members, male or female, have innumerable incentives to look the other way with respect to management irregularities. The push for women on corporate boards may well come from the fact that it is relatively easy: firms can simply expand

---

140 *See, e.g.*, Michal Barzuza et. al., *Shareholder Value(s): Index Fund Esg Activism and the New Millennial Corporate Governance*, 93 S. CAL. L. REV. 1243, 1279 (2020) (describing generational differences in ESG investing and describing how ESG investing differs from hedge funds focused on short term results).

141 NASDAQ, *supra* note 1.

142 Ann Shepherd & Gene Teare, *2020 Study of Gender Diversity on Private Company Boards*, CRUNCHBASE (Mar.1, 2021), https://news.crunchbase.com/news/2020-diversity-study-on-private-company-boards/.

143 "Nasdaq observed that "studies suggest that certain groups may be underrepresented on boards because the traditional director nomination process is limited by directors looking within their own social networks for candidates with previous C-suite experience." NASDAQ, *supra* note 1, at 15.

the size of the boards and add more women without significantly changing firm dynamics.[144] Sam Walton, after all, dealt with pressure to increase diversity in the eighties by adding Hillary Clinton to the Walmart board.[145] As the board's first woman, youngest member and one of few lacking business experience, she had little impact.[146] The much more important changes in corporate cultures would come from greater diversity not just on boards but in upper management.

B. Eliminating the Incompetent Bullies

While the stock market (and CEO salaries) have soared, conventional measures of firm performance, such as increases in productivity, show that companies have performed less well over the last forty years than they did during the supposedly complacent managerial era.[147] A global study of CEO efficacy indicates that CEOs of the shareholder primacy era contribute little to improved firm function, with CEOs who are paid more not performing any better, concluding that the results suggest that the performance of CEOs "tend[s] to follow the performance of their firms.[148] Although women constituted less than 10% of the sample, the authors found that "the overperformance of CEOs in top companies is driven by female CEOs . . . [and] the underperformance of CEOs in the worst-performing companies is mostly due to male CEOs."[149]

At the same time, the literature identifying the factors that drive women out emphasizes the same factors that depress teamwork and innovation: negative sum internal competition, lack of trust, emotionally distant – or abusive – managers, and the lack of loyalty and commitment between employers and employers.[150]

Business psychology professor Tomas Chamorro-Premuzic argues that, instead of establishing gender quotas,

> a more reasonable goal would be to focus instead on selecting better leaders, as this step would also take care of the gender balance. Putting more women in leadership roles does not necessarily improve the quality of leadership, whereas putting more talented leaders into leadership roles will increase the representation of women.[151]

---

[144] *See, e.g.*, Alexander Osipovich & Akane Otani, *Nasdaq Seeks Board-Diversity Rule That Most Listed Firms Don't Meet*, WALL ST. J. (Dec. 1, 2020), https://www.wsj.com/articles/nasdaq-proposes-board-diversity-rule-for-listed-companies-11606829244?mod=article_inline (commenting increasing board diversity should not cost much).

[145] *See* Michael Barbaro, *As a Director, Clinton Moved Wal-Mart Board, but Only So Far*, N.Y. TIMES (May 20, 2007), https://www.nytimes.com/2007/05/20/us/politics/20walmart.html.

[146] *Id.*

[147] Brett Arends, *CEO Pay Has Gone Up 10-fold in the Past 40 Years—Do They Deserve It?*, MARKETWATCH (Apr. 16, 2021), https://www.marketwatch.com/story/hey-honchos-give-us-back-our-money-11618519002?mod=hp_minor_pos19&adobe_mc=MCMID%3D05280436024580085122294529340144801967%7CMCORGID%3DCB68E4BA55144CAA0A4C98A5%2540AdobeOrg%7CTS%3D1618590882

[148] Arturo Bris & Maryam Zargari, *A Bullshit Job? A Global Study on the Value of CEOs* 31 (Mar. 16, 2021), https://ssrn.com/abstract=3805610 or http://dx.doi.org/10.2139/ssrn.3805610

[149] *Id.* at 30.

[150] *Compare* PATRICK LENCIONI, THE FIVE DYSFUNCTIONS OF A TEAM (2020), *with* Kim Williams, *Women in Tech: How to Attract and Retain Top Talent*, INDEED (Nov. 6, 2018), http://blog.indeed.com/2018/11/06/women-in-tech-report/ (describing poor managers and harassment as major reasons for women leaving tech).

[151] CHAMORRO-PREMUZIC, *supra* note 60, at 172-73.

That is, while firms seem quite willing to promote "incompetent" or bullying, amoral, and narcissistic men, they are less willing to promote such women.[152] Simply selecting more competent managers would thus increase the percentage of women.

Focusing on a company's ability to retain a more diverse workforce may help to identify and reform toxic workplaces. A telling factor at Uber was the fact that while the company initiated hired women as 20% of its workforce, that number fell to 7% given the company dysfunctional management practices.[153] Similarly, a sex discrimination class action brought against Microsoft persuaded the company to eliminate its stack ranking evaluation system, a system that many observers believe contributed not just to gender disparities but to Microsoft's loss of its competitive edge in designing new technology.[154] The problems at these companies came to light only when they became the subject of high profile sex discrimination complaints.[155] Diversity can be an effective barometer of management effectiveness.

Conclusion

Using diversity as an instrument of corporate reform requires more than adding a few women and stirring. Corporate leaders, after all, are adept at window dressing.[156] Nor is it simply a matter of diversity training or increased sensitivity to cultural differences.[157] Instead, it requires taking the idea of teamwork and trust seriously. The areas in the economy with the greatest gender disparities, including finance and tech, have turnover rates for everyone – and even higher rates for women.[158]

---

[152] For discussions of the classic double bind in which women are treated more harshly for engaging in the same conduct as the men, see *When Harry Fired Sally: The Double Standard in Punishing Misconduct* 2 n.2 (2018) (unpublished manuscript), https://www.nber.org/papers/w23242.); Alicia R. Ingersoll, *Power, Status and Expectations: How Narcissism Manifests Among Women CEOs*, J. BUS. ETHICS 1 (Nov. 2017) ("[W]omen leaders who display narcissistic personalities are perceived by men subordinates as less effective leaders than equally narcissistic men leaders, which suggests narcissistic women leaders may face biases that narcissistic men leaders do not).

[153] Complaint ¶ 22, Avendano v. Uber Tech., Inc. (No. CGC-18-566677), https://images.law.com/contrib/content/uploads/documents/403/15670/Complaint-1.pdf.

[154] *See* Erika Anderson, *The Management Approach Guaranteed to Wreck Your Best People*, FORBES (July 2012).); Kurt Eichenwald, *Microsoft's Lost Decade*, VANITY FAIR (July 24, 2012), http://www.vanityfair.com/news/business/2012/08/microsoft-lost-mojo-steve-ballmer.

[155] *Reflecting on One Very, Very Strange Year at Uber*, SUSAN FOWLER (Feb. 19, 2017), https://www.susanjfowler.com/blog/2017/2/19/reflecting-on-one-very-strange-year-at-uber.

[156] *See, e.g.*, Sam Walton's appointment of Hillary Clinton as the only woman on Walmart's corporate board in 1986. Clinton encouraging Walmart to hire more women but did not challenge its rampant anti-unionism. Michael Barbaro, *As a Director, Clinton Moved Wal-Mart Board, but Only So Far*, N.Y. TIMES (May 20, 2007), https://www.nytimes.com/2007/05/20/us/politics/20walmart.html

[157] Alexandra Kalev et al., *Best Practices or Best Guesses? Assessing the Efficacy of Corporate Affirmative Action and Diversity Policies*, 71 AM. SOC. REV. 589 (2006).

[158] *See A 2015 Report of*: *Elephant in the Valley*, https://www.elephantinthevalley.com/ (last visited Sept. 19, 2019);

Conversely, the workplaces that best promote innovation are also more effective at promoting diversity. The qualities that promote both diversity and innovation in such environments are "fair employment practices, such as equal pay; participative leadership, with different views being heard and valued; a strategic emphasis on diversity led by the CEO; frequent and open communication; and a culture of openness to new ideas."[159]

Along these lines, diversity should not just be a matter of adding a few women to corporate boards. Doing so in one sense is easy; legislatures can require increased board diversity without significant disruption to the corporate bottom line(or male careers).[160] If diversity is important to business performance, management policies, or gender justice, however, then the inquiry should be extended beyond board representation.

And sustaining diversity requires a critical mass. Diversity is an iterative process that spurs more progressive change.[161] Once workplaces become genuinely more diverse from entry level positions to the corporate boardroom, it spurs other changes that may have nothing to do with diversity per se. In the instrumental view, therefore, diversity is both a result and an architect of change.

The instrumental case for diversity we advocate in this Article concludes that better diversity is intertwined with better management. Diversity is a signal both internally and externally of a company's values. While adding women and stirring has not yet been shown to be a causal factor, the failure of a company to be able to maintain a diverse board or diverse management is a sign that something other than path dependence or unconscious bias and microaggressions is occurring at the company. Accordingly, for ESG investors who want to reform management practices – short termism, accounting fraud, ripping off customers, low productivity because of poor management – diversity is both a metric and a tool, signaling problems or serving as a marker of change.

Corporate reform per se cannot address structural issues such as the lack of affordable childcare or deeply entrenched racial inequality, but it can address the dysfunctional aspects of corporate governance that have arisen in the shareholder primacy era.

Kim Williams, *Women in Tech: How to Attract and Retain Top Talent*, INDEED (Nov. 6, 2018), http://blog.indeed.com/2018/11/06/women-in-tech-report/.

[159] *Id.*

[160] *See, e.g.*, Alexander Osipovich & Akane Otani, *Nasdaq Seeks Board-Diversity Rule That Most Listed Firms Don't Meet*, WALL ST. J. (Dec. 1, 2020), https://www.wsj.com/articles/nasdaq-proposes-board-diversity-rule-for-listed-companies-11606829244?mod=article_inline (commenting increasing board diversity should not cost much).

[161] On the level of political theory, "the value of diversity is instrumental because . . . cultural and national diversity reduces the concentration of political power within a state." Rainer Bauböck, *Cherishing Diversity and Promoting Political Community*, 1 ETHNICITIES 109, 113 (2001). This idea of diversity and power undoubtedly works on the micro level within companies as well as the macro level in nation states. Changing management practices to ensure ongoing diversity may also provide a basis for improved working conditions throughout the company. But guaranteeing a live-able minimum wage and health care and retirement benefits for all requires the rule of law.