

WHAT DO RECENT LAWSUITS IN THE WAKE OF SUPREME COURT DECISIONS ON AFFIRMATIVE ACTION MEAN FOR YOUR DISCLOSURES AND DEI PROGRAMS?

Aug 15, 2023

A flurry of recent lawsuits in the wake of the Supreme Court's June decision on affirmative action have further muddied the waters for public companies trying to thread their way through competing interests.

CONSERVATIVE ACTIVISTS CLAIM MISLEADING SEC DISCLOSURES AND REVERSE DISCRIMINATION

Conservative groups have launched efforts to push back against diversity, equity and inclusion (DEI) programs, challenging public company disclosures and alleging reverse discrimination. For example, last week the America First Legal Foundation (AFLF), which is led by former Trump Administration senior advisor Stephen Miller, asserted claims against Target Corporation and The Kellogg Company.

Disclosure claims against Target. The [complaint](#) (filed in the Middle District of Florida) alleges that Target's board failed to oversee the risk of "adopting divisive and extreme ESG and DEI mandates, such as triggering a customer backlash [over LGBTQ+-themed merchandise], and misleading investors about both the mandates and these risks." It focuses on disclosures that the board and its committees:

- Oversaw social and political issues and risks arising from the company's pursuit of ESG and DEI mandates.
 - The complaint alleges that the board only considered risks of failing to achieve those mandates.
- Adopted those mandates in order to advance shareholders' pecuniary interests in the value of Target's stock.
 - The complaint alleges that the board also considered collateral, non-shareholder interests and delegated execution of those mandates to individuals with conflicting duties that

prevented them from advancing shareholder value in good faith.

- Proposed executive compensation plans that were aligned with shareholders' pecuniary interests in the value of Target's stock.
- The complaint against Target also alleges that a short-term incentive plan included a component tied to achievement of DEI objectives.

Reverse discrimination and mismanagement claims re: Kellogg's. AFLF's [letter to the EEOC](#) alleges that Kellogg's engages in unlawful employment practices by seeking to "balance" its workforce based on race, color, national origin and sex, citing percentage targets for "underrepresented talent" at different levels of the company. It also references an accelerated development program and fellowship program for Black employees.

AFLF also sent a [letter to the Chair and CEO of Kellogg's](#) claiming that the company's DEI/ESG programs constitute "mismanagement threatening the waste of Company assets and breaches of fiduciary duty," citing:

- Recent marketing programs that allegedly "politicize and sexualize" products, focusing on LGBTQ-related messages.
- Allegedly misleading disclosures that "failed to properly warn investors of the risks associated with the apparent misalignment of management's political and social values with Kellogg's customers' values or taken steps to mitigate them".
- Alleged failures to comply with nondiscrimination laws and commitments, based on the allegations contained in the letter to the EEOC.

In addition to the above matters relating to Target and Kellogg's, the *Wall Street Journal* recently reported about other significant challenges to public companies in "[The Legal Assault on Corporate Diversity Efforts Has Begun](#)": "Comcast settled a case accusing it of illegally favoring minority-owned small-business customers with grants and marketing advice. Amazon has been sued in Texas over a program offering an extra \$10,000 to Black- or Latino-owned delivery-service contractors. Starbucks directors and executives are being sued by a shareholder arguing they violated their duty to investors by supporting diversity policies." However, according to [Reuters](#), last Friday the federal district court in Spokane, Washington dismissed the lawsuit against Starbucks "saying the lawsuit centered on public policy questions that are for lawmakers and corporations, not courts, to decide [and, stating:] 'If the plaintiff doesn't want to be invested in 'woke' corporate America, perhaps it should seek other investment opportunities rather than wasting this court's time.'"

THE BACKGROUND: SUPREME COURT REJECTION OF AFFIRMATIVE ACTION IN COLLEGE ADMISSIONS

On June 29, 2023, the U.S. Supreme Court issued a decision in two cases (*Students for Fair Admissions, Inc. v. President and Fellows of Harvard College, No. 20-1199*, and *Students for Fair Admissions, Inc. v. University of North Carolina*, collectively the “SFFA decision”) which, although not directly changing the legal parameters for corporate diversity, equity and inclusion (DEI) programs, is likely to place such DEI programs under much greater scrutiny. This issue warrants a closer look at all company communications addressing DEI initiatives, including, but not limited to statements in Corporate Responsibility Reports and the “Human Capital” section of corporate annual reports.

The Court’s Decision. The Supreme Court’s recent SFFA decision held that the use of race as a “plus factor” in higher education admissions decisions was a violation of the Equal Protection Clause and Title VI of the Civil Rights Act of 1964. The Court did acknowledge, however, that race can still be considered in the admissions decision when it is raised in a context of evidencing the applicant’s leadership, advocacy or character, such as an applicant essay regarding overcoming discrimination or being the leader of an affinity group.

Impact on Corporate DEI Initiatives. The Court’s SFFA decision does not directly address employment, and it is uncertain how broadly courts will apply the decision outside of higher education admissions. In the employment context (unlike in higher education prior to the SFFA decision), companies are prohibited from using set-asides, preferences or quotas. Companies are already engaged in a balancing act, being faced with potential DEI-related challenges from both sides. DEI proponents argue that companies are failing to live up to stated goals relating to creating and maintaining a diverse workplace, while DEI opponents claim that companies are engaging in reverse discrimination in implementing their DEI initiatives. The SFFA decision is likely to provide further fuel to affirmative action opponents to launch attacks in various contexts, including corporate DEI initiatives.

For example, 13 Republican state attorneys general issued a [letter](#) to the management teams of all Fortune 100 companies reminding them of their “obligations as an employer under federal and state law to refrain from discriminating on the basis of race, whether under the label of ‘diversity, equity, and inclusion’ or otherwise. Treating people differently because of the color of their skin, even for benign purposes, is unlawful and wrong.” The 13 Republican attorneys general go on to ask the companies to “comply with race-neutral principles in [their] employment and contracting practices.” Six days later, Democratic attorneys general from 20 states and the District of Columbia issued their own [letter](#) rejecting “the baseless assertion that any attempts to address racial disparity are by their very nature unlawful” and arguing that the Republican “letter’s attempts to equate ... permissible diversity efforts with impermissible hiring quotas is a clear effort to block opportunities for women and people of color—especially Black people. Aspirational diversity goals and concerted

recruitment efforts to increase the diversity of a company's workforce are not hiring quotas, which were already unlawful..."

RECOMMENDED ACTIONS

In the current polarized environment, where companies are subject to pressures from the investor community, the political community and the public generally, companies are challenged from a variety of perspectives. Companies should be prepared to explain and defend their DEI efforts by, among other things:

1. Formulating a clear explanation of the rationale for their programs, including how such programs serve the interests of the company and its shareholders and, to the extent taken into account, other stakeholders, such as communities, employees or customers, addressing how supporting those stakeholders serves the short or long-term interests of shareholders.
2. Considering DEI initiatives that focus on eliminating implicit bias and increasing equal employment opportunities for all (*g.*, standardized interview procedures, expanding recruiting efforts, increasing employee training opportunities), rather than solely meeting specific demographic goals.
3. Ensuring there is nothing that could be interpreted as a quota, preference or use of race/gender as a "plus factor" in employment decisions. DEI initiatives that include specific numerical targets may be particularly subject to challenge.
4. Taking a close look at any race-conscious programs, particularly those that implicate (even indirectly) hiring and promotion decisions. For example, fellowship, internship, training and hiring programs that are not open to all demographic groups may be vulnerable.
5. Ensuring that all efforts to increase diversity are well-articulated and supported by specific evidence (most often an analysis of specific company data) that shows:
 - There is a specific problem that warrants action (*i.e.*, there is a manifest imbalance in the specific area being targeted); and
 - That the program is narrowly focused (in scope and timeframe) on the elimination of past discrimination.
6. Establishing employment decisions that are robust and well-documented. Those involved in hiring, promotion and firing decisions should be properly trained to conduct and document a robust and multi-factored decision-making process.
7. Carefully considering language in social responsibility reports, human capital management disclosure, and similar documents that could be misread to suggest the use of quotas and

thereby attract challenge or criticism.

8. Review any DEI metrics used in incentive compensation programs to avoid their potential characterization as promoting hiring or promotion decisions based on quotas or unlawful preferences related to protected characteristics.

RELATED CAPABILITIES

- Securities & Corporate Governance
- Employment & Labor

MEET THE TEAM



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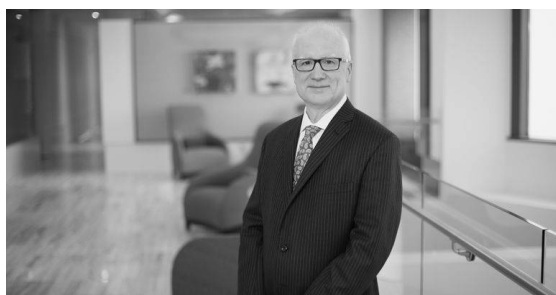


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