

How fund boards
can drive diversity,
equity and inclusion in
investment management

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Content

- 3 Why DEI matters
- 5 What DEI entails
- 8 How to act and drive change
- 11 Time to act

With so much changing in the world, organizations that can be proactive instead of reactive are better positioned to think strategically and thrive. This can be accomplished by relying on people from outside your sphere to ask the questions that you don't think about or are afraid to ask. Yet, too often, this is exactly the talent that the investment management industry lacks.

In a two-day event organized by Ernst & Young LLP (EY US) and the Mutual Fund Directors Forum (MFDF), fund directors gathered to discuss diversity, equity and inclusion (DEI) as both a moral and a business imperative. In doing so, we explored current trends and evolving topics, such as equity and neurodiversity, and strategized on how to effect change in their boardrooms as well as the industry at large.

The discussion covered:

- ▶ **A framework for discussion** – what, why and how: The aim was to ground directors on the evolving scope and focus of DEI activities, reinforce the benefits of amplifying the focus on this area from a fund board perspective and discuss practical ways to change.
- ▶ **Why DEI matters:** While many senior leaders take the case for DEI to be very much closed, there remains some who struggle with why fund boards should advance DEI – they wonder how it delivers more return for fund investors. In our session, we discussed the compelling evidence DEI is not just the right thing to do, it's the right thing to do for shareholders (and they know it).
- ▶ **What DEI entails:** The concepts and focus of DEI have been changing materially in recent years. We have moved from diversity and inclusion (D&I) to diversity, *equity* and inclusion, and now we are adding belonging and allyship. We have traditionally focused on traditional areas, such as gender and racial diversity, but are now also focused on socioeconomic, geographic and neurological diversity. Strategies on DEI have to expand to address these new areas.
- ▶ **How to act and drive change:** Fund boards can advance DEI at three levels: fund board composition, DEI across asset management and DEI in companies in which the funds invest. We discussed practical actions across all three levels.

This paper provides more detail on the why, the what and the how to inform important discussions on DEI and then turning them into action and driving change. Some of the issues discussed go beyond the direct scope and remit of fund boards, but given those boards' essential leadership role in the broader industry, it was important to discuss the evolving nature and complexity of diversity, equity and inclusion.



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If we agree that diversity in all its forms improves performance, then why not make the investment?

– Fund director



Why DEI matters

After years of focus on gender diversity – and more recently on racial diversity – one would assume the case for diversity was watertight and not worth airtime. Alas, like climate change, that isn't the case. Some directors still ask, “Why should fund boards focus on diversity? Does it drive shareholder value?”

However, across asset management – including mutual funds, hedge funds, private equity funds, and real estate funds – diversity is low; a 2019 report found that women- and minority-owned firms made up 3%-9% of the industry and controlled

A growing regulatory and listing focus on diversity

- ▶ In August 2021, the Securities and Exchange Commission (SEC) approved Nasdaq's proposal to set baseline disclosure requirements on board diversity and adopt a comply-or-explain requirement on having a baseline level of diversity (at least two diverse directors).
- ▶ In July 2021, the SEC Asset Management Advisory Committee – Subcommittee on Diversity and Inclusion called for more stringent mutual fund requirements on diversity (e.g., on advisors' diversity practices) and fund board diversity disclosures (on racial and gender diversity)⁴.
- ▶ In June 2021, the SEC announced it plans to propose and finalize new disclosures on workforce and board diversity as part of its forthcoming rules-making agenda.
- ▶ Companies with executive offices in California have to have minimum levels of gender (SB 826 took full effect at end of 2021) and racial (AB 979 takes full effect at end of 2022) diversity on their boards (the latter defined as underrepresented communities).
- ▶ There have been several bills in Congress focused on diversity in corporate boards (e.g., H.R. 1277 – Improving Corporate Governance Through Diversity Act of 2021).
- ▶ The UK Prudential Regulatory Authority (PRA) in 2020 explicitly linked board diversity to the board's ability to provide credible challenge of management as part of its broader requirements for strong corporate governance.
- ▶ Many countries – including Belgium, France, Germany, Italy, and Norway – have set minimum quotas for gender diversity on corporate boards.

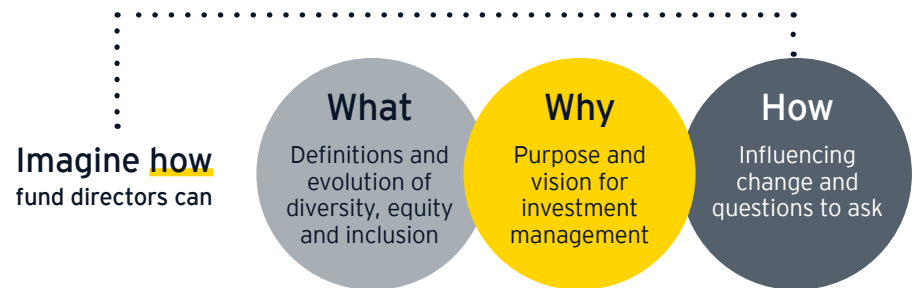
⁴ "Report and Recommendations on Diversity and Inclusion in the Asset Management Industry," SEC website, <https://www.sec.gov/files/spotlight/amac/amac-report-recommendations-diversity-inclusion-asset-management-industry.pdf>, accessed 30 August 2021

1%-5% of the assets under management.¹ That is dramatically less than the estimated 70% of the US population who are women and/or minorities.

And there is a price to pay for homogeneity and facts abound to say so. Across all industries, companies with diverse teams are 45% more likely to improve market share and 70% more likely to capture a new market, according to research from Coqual.² In very real terms, identifying and rectifying underrepresentation – whether ethnic or racial, cultural, socioeconomic, or any other group – encourages much-needed diversity of thought and talent in investment management.

The value of diversity is not lost on investors and they are becoming increasingly vocal on these matters. Through June 2021, both the volume and support of shareholder proposals on DEI matters have increased substantially: the EY Center for Board Matters tracked around 130 such proposals, averaging 42% support among those that went to a vote through May. For the entirety of 2020, DEI-related proposals totaled around 90 and averaged just 25% support.³ See *DEI areas of focus among shareholders* below.

What, why and how: a frame for discussion and action



- ▶ Encourage diversity of thought and talents in investment management
- ▶ Attract a wider breadth of talent to the industry through fund board diversity
- ▶ Ask better questions of advisors and their diversity programs
- ▶ Influence the diversity of the companies in which you invest

¹ "Diversity in Asset Management: Research and Practice," Mission Investors Exchange website, <https://missioninvestors.org/resources/diversity-asset-management-research-and-practice>, accessed 30 August 2021.

² "Innovation, diversity and market growth," Coqual website, https://coqual.org/wp-content/uploads/2020/09/31_innovationdiversityandmarketgrowth_keyfindings-1.pdf, accessed 30 August 2021

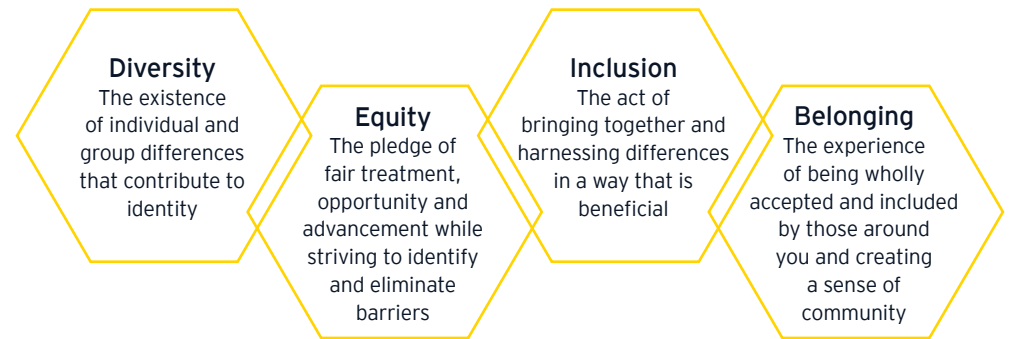
³ "What boards should know about ESG developments in the 2021 proxy season," EY website, https://www.ey.com/en_us/board-matters/esg-developments-in-the-2021-proxy-season, accessed 30 August 2021



What DEI entails

Once one gets past the “why” debate, it is essential to focus on the “what.” Here, there is a significant broadening of issues and themes, as shown in Figure 1. Indeed, it seems only a few years ago we were talking about D&I, and now equity has been emphasized. To that, we now add belonging and other key themes.

Figure 1: EY view of diversity, equity, inclusion, and belonging



“Diversity is not just a visual. We have to move leadership away from what is a superficial assessment—the mindset of ‘I ticked a box, now I can move on.’

– Fund director

	Perspectives	Key topics and considerations
Traditional	<ul style="list-style-type: none"> ▶ Gender ▶ Race ▶ Ethnicity ▶ Sexual orientation ▶ Age (including generational) ▶ Disabilities 	<ul style="list-style-type: none"> ▶ Unconscious bias ▶ Board/C-suite representation ▶ Mentorship and sponsorship ▶ Recruiting
Evolving	<ul style="list-style-type: none"> ▶ Neurodiversity ▶ Socioeconomic status ▶ Regional representation 	<ul style="list-style-type: none"> ▶ Equity ▶ Allyship

The ultimate goal for DEI is twofold: address underrepresentation in its ranks and create an environment where new creativity and new visions can thrive. There’s a recognition that diversity includes many more differences than those we can see. Gender and ethnic diversity is a critically important objective – it is perhaps the most visible sign of progress – but directors saw an imperative in moving beyond

Equity requires broad-based engagement

Various parts of the organization are essential to driving up equity:

- ▶ Strategic groups: those who maintain and improve the brand/corporate image, monitor business results (including employee engagement and turnover), and communicate with stakeholders, including shareholders
- ▶ Human resources: those who work to attract and retain talent, keep them engaged, develop benefits and compensation, and create unified HR policies, processes and resources
- ▶ Operational leaders: those who track efficiency and productivity and aim to create competitive advantage through gaining access to critical skill sets, while addressing requirements from investors and contract stipulations from the public sector
- ▶ Legal and risk: those involved in annual HR compliance/risk reviews and monitoring frameworks, mitigating the risk of (and preparing for) government filings, inquiries, penalties, and fines, as well as employee claims and lawsuits

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If every time we try to integrate an individual to be like someone else, we're creating a homogeneous teaming environment. There's no innovation there.

– Hiren Shukla, EY Global and Americas Neuro-Diverse Center of Excellence (CoE)

“photo op diversity” to truly benefit from differences. (As one example, see the sidebar on neurodiversity.)

The discussion among fund directors shone light on the fact that progressing on all these dimensions will be very challenging, as some may compete against the other:

Thinking style	Ethnicity
Leadership style	Education and work experience
Gender	Religious background
Diverse abilities	Sexual orientation
Country of origin	Generation
Location	Socioeconomic background

In the past year, **equity** – the middle component of what has become DEI – has moved up the agenda, driven by media attention, employee demands for social responsibility, shareholder activism, and new regulatory scrutiny. How talent is hired, compensated and advanced in the organization should be equitable, but study upon study show that gaps persist.

Achieving equity requires input across several functional areas, including C-suites, boards, HR, operational leaders, and legal and risk professionals

- see sidebar. It's a topic that not only affects your talent strategies but also how you communicate with shareholders and investors, as well as how you compete for government contracts and engage with the public sector.

However, having diversity and capitalizing on it are two different things. Often sustaining progress and gaining from it can be the biggest challenge, even in fund boardrooms. One director spoke of a “revolving door” of diverse board members after three years because the board itself had underlying issues, such as an unwillingness to tolerate different perspectives.

Two terms – **inclusion** and **belonging** – aim to address this gap: Inclusion is inviting those people from diverse backgrounds to participate, engage, collaborate, and contribute to your organization and the broader community. These people should also feel like they belong – to experience the support and security that other groups take for granted. In a sense, belonging is taking a step further from inclusion, to show participants that they're part of something bigger and can bring their authentic selves to work. This has been especially important in a virtual environment, where inclusion and belonging can be more challenging.

While driving fundamental improvements is not the job of just one person in an organization, each of us has a role to play as allies. **Allyship** plays a critical role in fostering a culture of inclusion in the workplace

Expanding one's perspective on diversity: the power of the neurodiverse

Neurodiversity is one metric of diversity that more corporate boards companies are starting to examine more closely, so it may be of interest to fund boards.

About 20% of the population has an inherent cognitive difference, and they are hardwired to think, approach and digest the world differently. They often have highly complex problem-solving skills and technical aptitude, including advanced degrees in data engineering, machine learning and statistics for artificial intelligence. Yet 85% of neurodiverse people are unemployed or underemployed because their ways of thinking can be framed as weaknesses instead of sources of strength.

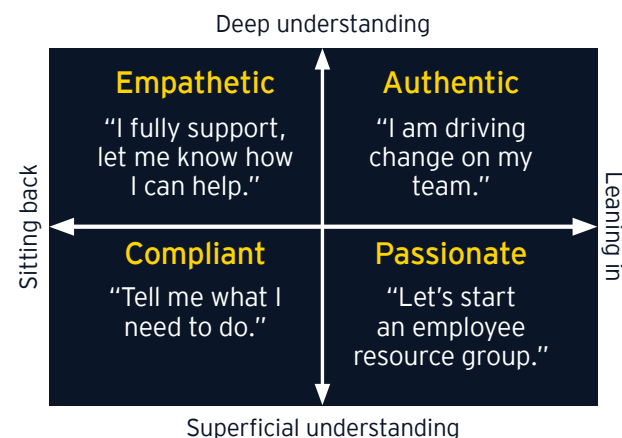
"This population is creative and agile. They are a bit of the workforce of the future," said Hiren Shukla, who leads this initiative at EY US as the EY Global and Americas Neuro-Diverse CoE Leader. "This is a talent innovation journey that adds speed, velocity and creativity to your existing team. And it sits at the intersection of transformation, purpose and DEI."

Many directors asked Hiren where to find this talent. It's not as hard as you might think: governments, academia, nongovernmental organizations, and nonprofits are already working with them and are ready to collaborate. EY US made accommodations in its hiring process – for instance, by using virtual meetings and technical exercises and not primarily one-on-one interviews – and made investments in noise-cancelling headphones for new hires. Now, it takes just three months to start a new CoE, and EY US and other companies are sharing what they have learned through Disability:IN's Autism @ Work initiative. "There is so much untapped potential," Hiren says. "We need others to join us."

To learn more about the EY Neuro-Diverse CoE visit: [How neurodiversity is driving innovation from unexpected places](#) | EY - US

across all dimensions. Being an effective ally is an ongoing journey that requires active education and action, both exercised at an individual level, in ways that also radiate change through the organization, as shown in Figure 2.

Figure 2: Effective allyship and fostering a culture of inclusion



	Individual	Organizational
Expand your understanding	1	Adopt both organizational and individual lenses on diversity, equity and inclusion
Reach out and check in	2	Assess leadership alignment
Become an advocate – speak up and speak out	3	Identify traits to keep, start and stop, and behavioral risks within the current culture
Amplify accomplishments in open forums and behind closed doors	4	Detect how motivate people and what leaders can do to create a movement
Create opportunities for visibility and growth	5	Prioritize operating model/ environment levers and influencers to start the shift



How to act and drive change

Moving from theory and discussion into action begins with asking better questions across organizational pillars. Changing one of these pillars is a start, but progress can easily be undermined without holistic effort. Figure 3 outlines some of the core dimensions of action-oriented DEI strategy and execution.

Figure 3: DEI in investment management



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You need to look for the underrepresentation: cultural, racial, socioeconomic. A ‘diverse’ board can be white men and white women. You have to look at this with great intention. I’m trying to find differences to enable us to ask different questions.

– Fund director

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Nice writeups in the 15(c) questionnaire are easy to produce, but walking the talk, so to speak, requires data and regular updates on progress.

– Fund director

Fund directors have three powerful levers to advise DEI. In breakout sessions, participants in our two-day event brainstormed and recommended specific, practical actions across the three dimensions.

Fund board composition: Through concerted efforts, fund boards can advance diversity in the fund boardroom and model what they expect of their advisors and what they’d like to see across the industry at large. If there is a glass ceiling in fund boards, it has a very negative ripple effect industrywide. Understand that the goal isn’t just to get diverse talent in the boardroom, but to improve the environment in which new creativity and new visions can thrive. They could:

- ▶ Develop clear parameters around how you define board diversity and be explicit on your aspirations in your board charter. Broaden the discussion beyond gender and race to include other traits, such as regional and socioeconomic diversity.
- ▶ Revisit retirement age and term limits, which are important factors for embedding board renewal and creating opportunities to bring on more diverse directors. It allows for younger directors to be appointed, without worrying about if they will stay on the board for decades.

Ask questions such as:

- ▶ Have you addressed “Why DEI?” in your boards to create a baseline for the need for exploring diversity, equity and inclusion in the boardroom?
- ▶ Have you defined what DEI means for your board?
- ▶ Has your organization explored how a “cultural fit” used in recruiting directors may discourage different ways of thinking?
- ▶ Are you turning to search firms or associations that are prioritizing diversity?
- ▶ During meetings, are certain board members not getting a chance to speak or afraid to ask certain questions? Are they not feeling like they belong? Is the board actively creating a sense of belonging for all board members?
- ▶ How well are you holding your board accountable through transparent reporting on diversity goals and progress?

Asset management DEI: Fund boards select a range of subadvisors and service providers and have the right – and power – to place DEI high on the agenda as it relates to expectations for selection and retention. What’s signaled as important to fund boards is,

without question, going to then become important for those seeking to work with those boards. They could:

- ▶ Make sure their (sub)advisors know DEI is a priority for the fund board.
- ▶ Demand DEI proof-points from the service providers you work with.
- ▶ Ask how DEI is applied in the context of succession planning.
- ▶ Continually ask questions of your (sub)advisors to understand what they’re doing on these topics in the aggregate and whom they have chosen to present to the board. Do the CEO or business leaders discuss DEI with the fund board, or just the talent leads? The team you see, and how key leadership responsibilities are allotted, hint at their broader strategy on building a pipeline of talent and promoting training and opportunities.
- ▶ As they get quarterly presentations, hold all groups accountable for reporting on DEI and make sure real progress is happening at the senior levels in their organizations, not just at lower levels.

- ▶ Advocate for change in industry organizations. Engage in association diversity efforts (such as writing to the SEC advocating for policy changes in DEI disclosures).

DEI in companies in which the fund invests: Funds vote proxies across the full spectrum of listed companies and seek to determine that advisors are using their votes to advance DEI and, as result, bringing the power of DEI to companies in which they invest and accrue superior returns from diversity. They could:

- ▶ Ask how the advisor addresses DEI in their proxy voting policy. What aspects of DEI are covered? Which issues need to be added?
- ▶ Ask for an update on the advisor's voting record on DEI matters. Did the advisor vote for any specific DEI-related shareholder proposals? If not, why not? See DEI areas of focus among shareholders.
- ▶ Ask what industry-level industry initiatives the advisor is involved in on DEI shareholder matters.

While fund directors appreciate that they have a powerful set of levers available to them to advance DEI, they also understand perhaps the biggest challenge is being consistent across levers: To the extent the fund board is homogenous, can it really say that DEI is a priority when engaging advisors? Similarly, if fund boards require their advisors to focus more on DEI in the proxy-voting context, can they credibly remain unfocused on advisor DEI? The reality is a comprehensive approach is not only required to make the advances needed, it's the only credible way to do so.

DEI areas of focus among shareholders⁵

According to the EY Center for Board Matters, the most prominent and supported shareholder proposals on DEI topics include those related to increasing diversity across the board and/or executive leadership (59% support on average) and those asking companies to publicly report data aligned to the disclosure framework of the United States Equal Employment Opportunity Commission's EEO-1 Survey (70% support on average). Most of these submissions were withdrawn, generally because companies and proponents found common ground and reached agreement.

Different proposals asked companies to publish a report assessing the effectiveness of their DEI programs, included as reflected in any goals, metrics and trends related to the promotion, recruitment and retention of protected classes of employees (49% support on average). Another prominent proposal related to the external impact of company business practices, products and services on communities of color and racial justice (34% support on average). About a third of each of these proposal types was withdrawn.

Other proposals focused on pay equality, board oversight of workforce equity issues, diverse candidate search policies, and the impact of the use of mandatory arbitration on the prevalence of harassment and discrimination in the workplace.

⁵ "What boards should know about ESG developments in the 2021 proxy season," EY website, https://www.ey.com/en_us/board-matters/esg-developments-in-the-2021-proxy-season, accessed 30 August 2021 "



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Diverse opinions and skills lead to the best answers for clients and our own organization. We don't get those diverse opinions and skills by bringing together people who look, think and act the same way, or who've had similar life experiences.

– Carmine Di Sibio,
EY Global Chairman and CEO



DEI at EY US

EY US has long focused on DEI. We strongly believe diversity, equity and inclusion matters. We also believe that setting meaningful goals is important, as is disclosing progress on those goals so we and our many stakeholders can hold us to account for that progress. We encourage you to read the latest [EY DEI transparency report: pathways to progress.](#)

Time to act

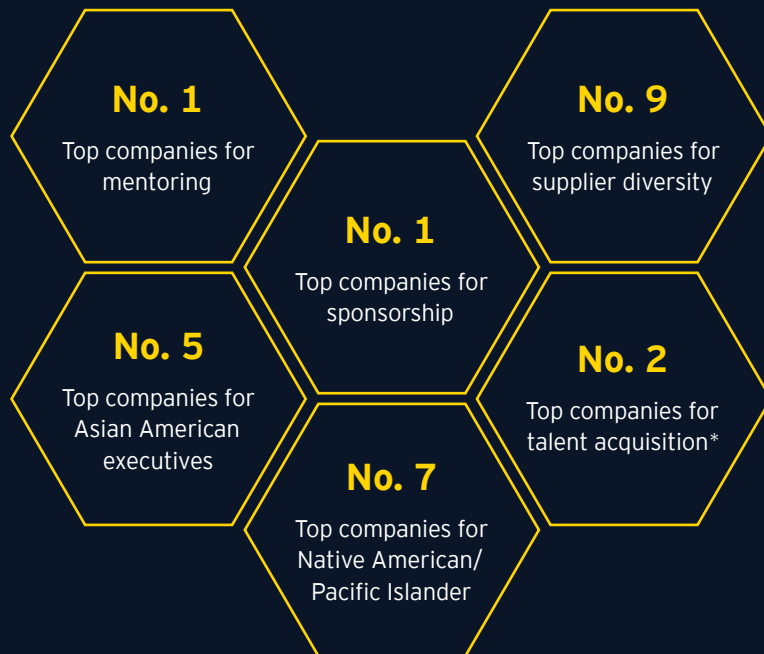
The job of fund directors is to see around corners and challenge (sub) advisors and service providers to anticipate what's next. Never has the maxim "great minds think alike" seemed less true than today. Beyond the moral and financial dimensions, regulators worldwide are increasingly asserting themselves on questions such as board diversity and financial inclusion, and reputational risk exists as a very real threat for those who see DEI only as a passing trend or an opportunity for a photo op.

DEI offers a lens for the mutual fund industry on how to capitalize to see diverse thought and new sources of innovation, drive new client opportunities, and address broader market segments, as well as to build trust and to attract and retain top talent. Building a better tomorrow – to prosper sustainably and widely – means leaving yesterday's modes of thinking behind.

EY US is proud of our accomplishments and we continue to strive to achieve excellence in the DEI space.

Diversity Inc magazine's Top 50 Hall of Fame

For demonstrating a long-standing and consistent commitment to diversity and inclusion, which features companies that have achieved a No.1 ranking on the publication's Top 50 Companies for Diversity list since 2012 and stands above the top 50 list. EY US was also recognized on the following 2020 specialty lists:



*Inducted in 2018 and maintained this status in 2019. No specific ranking in this category this year.

2020 Top 10 Companies for Executive Women

By the National Association for Female Executives (NAFE), which honors American corporations that identify and promote successful women (seventh year on NAFE's list)

No. 1 100 Best Companies for Working Mothers (Hall of Fame, Top 10)

By Working Mother magazine (15th consecutive and 24th overall appearance on the list)

Diversity Best Practices Top 10 Inclusion Index

Acknowledging our leading-class diversity and inclusion practices in recruitment, retention and advancement; company culture; and demographics/transparency (third consecutive year)

National Association of Black Accounts (NABA) Company of the Year

Recognizing our commitment to employing diverse professionals in positions of prominence, our innovative employee programs promoting the advancement of minorities, as well as our ongoing support of diverse community and organization initiatives

Human Rights Campaign 100% Corporate Equality

Index rating on policies pertinent to LGBTQ employees – 2020

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The EY Financial Services Center for Board Matters helps financial services boards of directors to identify, understand and navigate complex global and domestic sectors and regulatory risks and opportunities facing their firms. We help directors provide effective oversight of their firms by asking better questions of management and enhancing board, committee, and individual director performance and effectiveness. We help champion the benefits of strong board governance and facilitate engagement of directors with peers and other key stakeholders – such as shareholders and regulators – to stay abreast of trends and leading practices. We drive board refreshment by identifying, sourcing and introducing qualified, diverse director talent and promoting and enabling diversity and inclusion. Contact us at fs.board.matters@ey.com for more information.

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Three ways FS boards can advance diversity, equity and inclusion | EY – Global

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How fund boards elevate the focus on sustainable finance: risk and opportunities

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What happens when great minds don't think alike? | EY – US

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