The Diversity Factor © 2010
ISSN 1545-2808
Fall 2010 (3rd Qtr, 2010)
Measuring Diversity Return on Investment (ROI)
Volume 18, Number 3
Return to the Table of Contents

Print Friendly Version
Your subscription allows you to print one copy of this article for your own personal use.

A new way to build the business case for diversity based on the numbers: The Diversity Profit Equation (d/PE™)

Craig B. Clayton, Sr., founder and CEO of The Spartacus Group and director and diversity strategist with the University of Houston's International Institute for Diversity and Cross-Cultural Management, located in the C. T. Bauer College of Business. (craig@craigclayton.com)

Craig B. Clayton is an organization development consultant and director and diversity strategist with the University of Houston's International Institute for Diversity and Cross-Cultural Management. He is also the CEO & founder of The Spartacus Group.

Today, as the U.S. economy pulls out of the recession/depression, companies are putting a strong emphasis on productivity and regaining momentum in terms of profits. This environment has impacted diversity programs. One major question today is, "What is the [financial] Return on Investment?" In this article, the author presents an analytic, business-based framework for measurement, showing companies how continued derailing behaviors and/or micro-inequities including subtle forms of discrimination can impact companies in terms of lost work time and productivity.

SIDEBARS

Derailing Behaviors
Constituent Impact
Diversity Incivility
Fiscal Impact
Case Study

For years, associations and best practice groups have been working on solutions to the challenge of diversity Return on Investment (ROI)—that is, how to measure the return on their diversity investment. Before the economy worsened during 2008–2010, many practitioners didn't spend a lot of energy validating the ROI. Instead, their efforts were aimed at getting the organization to understand valuing diversity as "The right thing to do."

Today, another approach is emerging. Companies are increasingly looking at more quantitative ways to link corporate diversity efforts to ROI. Taking this approach is the first step to positioning diversity management, not as another cost center, but as a strategic initiative. In this paper, we will discuss the results of a study done by the University of Houston's International Institute for Diversity and Cross Cultural Management and how it has laid the groundwork for us to develop a useful measurement —diversity return on investment—or more specifically, diversity impact on earnings through the use of a Diversity Profit Equation (d/PE™), which is explained later in this article.

The reality of a diverse workforce

"Companies are increasingly looking at more quantitative ways to link corporate diversity efforts to ROI."

Having a diverse workforce is not an accomplishment; it's an inevitability. Many organizations cite the increased level of diversity that exists within their organization as though they have made great strides to achieve those increases. The numbers are quoted on their Web sites and in their corporate documents with a tremendous sense of pride. However, becoming diverse should not be thought of as a goal. In reality it's a train that has already left the station.

So what does diversity mean in today's corporate world? Many organizations have rapidly become diverse. With shifting populations in the United States, achieving diversity doesn't require much effort.

But for many, diversity is still a code word for affirmative action. Many companies have developed diversity programs, but their only metric for success is measuring the hiring and promotion of women and people of color. Yet progressive companies understand that diversity management extends far beyond "hitting the numbers" or compliance. It includes a wide range of activities designed to proactively create an inclusive work culture—succinctly described by the U.S. Military's Officer Training Corp. as an environment that gives "all members of the workforce the opportunity to be productive, without disadvantaging anyone."

"Having diversity, while inevitable, does not automatically bring harmony, success and profitability."

So the challenge looks something like this: Having diversity, while inevitable, does not automatically bring harmony, success and profitability. In fact, it can cause more problems if the differences in values, cultures and behaviors are not effectively managed. With the increasing importance of intellectual and human capital on organizational success, managing the increasing diversity of today's global workforce is a critical enabler for all successful organizations.

The University of Houston's Institute for Diversity conducted a case study using 13 companies and more than 10,000 respondents to measure the degree to which derailing behaviors and corporate culture impacted an organization's ability to leverage the goal of increased numbers of high-performing work groups. This study provided a foundation for linking inclusion and equitable human capital management processes to the top line (revenue growth), the bottom line (cost reductions), and the pipeline (recruiting, retention and talent management). The official title of the study was "Quantitative Analysis of the Consequences of Derailing Behaviors on Employee Commitment and Corporate Culture." The subtitle was "Linking Discretionary Effort to Profitability and Providing a Process for Framing the R.O.I. for Human Capital Management and Diversity Programs."

The link with performance

The primary human capital goal/target for most organizations is not the ethnic or gender composition of their workforce, though in the United States, there are specific exceptions to this fact such as situations involving government contracts. But the goal for most organizations is to increase profitability while reducing or at least holding the line on costs. Human capital productivity factors have long been linked to high-performing work teams (HPW).

HPWs are teams that, by comparison, consistently outperform other work groups, when all else is equal. Their productivity, quality and enthusiasm about their efforts are measurable. They are in workplaces that people are proud of and want to be a part of. They have higher percentages of people willing to give their "discretionary effort" on a consistent basis. Discretionary effort is when an employee wants to help the company achieve and exceed its goals and is willing to give more than the minimum requirements for the job. When the majority of employees on a given work team are giving this discretionary effort, it leads to high performing work teams.

"Human capital productivity factors have long been linked to high-performing work teams (HPW)."

What is asset utilization?

In today's competitive workplaces, full utilization of resources is an expectation all stakeholders have. Production capabilities are expected to be maximized; general and administrative costs are expected to be reduced and/or leveraged. Margin enhancement is expected to be everyone's concern. Improving the market to book value is expected to be a part of every organization's focus. Effective utilization of human capital is the difference between meeting expectations and exceeding them.

In a recent University of Houston Case Study, 57 percent of respondents stated they give less than 100 percent of their best efforts on a regular basis. One of the top two things that would cause employees to give more effort, according to this study is "a manager who treats me with dignity and respect."

Having managers who understand the need to effectively manage the differences in the workplace is not an option; it is a business necessity. Some may call this just a matter of good management practices, and they would be correct. One fact to keep in mind, however, is that according to the U.S. Department of Labor, more than 75 percent of the people currently entering the workforce in the United States now are women, immigrants or people of color. Good management practices involve understanding how to motivate, communicate with and manage an increasingly diverse workforce. After all, if your competition does it better than you do, they win. It's that simple.

Diversity, then, is a bottom line issue, presenting not only cost challenges but also profit opportunities. In monitoring companies for activities that return investment value, shareholders are increasingly interested in diversity management. They are seeking to invest in companies committed to building respectful, inclusive and productive workplaces and are asking for measurements that can accurately gauge this commitment. It is clear, then, that human capital management is a bottom-line issue, presenting cost and profit issues and opportunities, including diversity management. This relationship is illustrated below.

"Good management practices involve understanding how to motivate, communicate with and manage an increasingly diverse workforce."

The Link Between Increased Levels of Incivility and the Bottom Line

Acts of Incivility		Effects		Impact		Results		Fiscal Link
Increased Acts Witnessed	➔	**Reduced Level of Ownership Attitude**	➔	**Reduced Commitment/ Effort**	➔	**Emotional Separation/ Withdrawal**	➔	**Increased Costs/ Decreased Productivity**

The question isn't whether you can afford to increase spending in diversity management programs. The real question is whether you can afford not to invest in the maintenance and upkeep of one of your most critical assets—your people. The environment that people work in, often referred to as the "Corporate Culture," is critical to the ability to maximize performance and productivity. When it comes to people in your organizations, the underlying question is whom can you afford to underutilize?

For most organizations, the answer to this question is very clear: no one. Yet the case study showed that many people are not giving their best efforts in the workplace. The data showed correlations between behaviors, programs, processes and policies that negatively affect profitability.

Four types of derailing behaviors

Derailing behaviors do exist in all organizations. These behaviors manifest themselves in many ways. The first step in beginning to reduce them is to get some conceptual clarity about what derailing behaviors are, how prevalent they are and how they affect business metrics.

Our definition of derailing behaviors is this: Derailing behaviors are actions, whether intentional or not, that sabotage, undermine or weaken employees' commitment, passion or willingness to conduct their responsibilities at their full potential. The four primary types of derailing behaviors are described in more detail in Sidebar 1 at the end of this article:

- Broken dignity entitlements
- Micro-inequities
- Corporate bullying
- Acts of incivility

Each of these terms were coined in other studies that began the process of identifying the impact of derailing behaviors, but those studies didn't carry their research far enough to quantify the link to the bottom line, top line or pipeline.

Details of the research study

The study conducted by the Institute for Diversity in 2006 found more than 71 percent of employees had witnessed on average four derailing behaviors per year. When asked about these acts in a follow-up study, also conducted in 2006, two out of three acts of incivility were said to be diversity related. These diversity related acts of incivility (DRIs) were believed to be associated with the primary dimensions of diversity—race, gender, age, religion, and sexual orientation.

The impact on employees who are on the receiving end of DRIs is devastating. The negative impact is not limited only to the individual experiencing the act of incivility, but it influences those who observe it. It is reasonable to assume that some employee turnover is directly associated with acts of disrespect or discrimination in the workplace.

Business links to productivity

While researching the proprietary tool Employee Commitment Inventory (ECi), as part of our study, we found a significant link between the amount of acts of incivility in the workplace and measurable business indicators that impact earnings and the bottom line. Some of the constituencies affected are shown in Sidebar 2. But in general, here are some areas influenced are the following:

- Amount of discretionary effort given
- Sick days and company medical expenses
- Frequency of safety incidents
- Overall propensity to leave (turnover)
- Impact on employee ideas and suggestions (creativity)
- Lost revenue per FTE
- Effect on regrettable losses
- Impact on unexcused absences
- Quality of customer service given

"These diversity related acts of incivility (DRIs) were believed to be associated with the primary dimensions of diversity—race, gender, age, religion, and sexual orientation."

Why create a ratio to measure diversity profit

Part of our survey included the creation of the d/PE™ to measure the fiscal impact of diversity programs on organizations profitability. The purpose of these measurements is to provide a snapshot of the strategic and fiscal significance of managing diversity as a business strategy. The metric is a time series comparative analysis that provides a snapshot of the impact of managing the revenue, costs and human capital implications of diversity management. The metrics represent the opportunity costs associated with a best-in-class solution.

The d/PE™ measures diversity-related revenue growth, cost reductions, impact of derailing behaviors, turnover costs, and program management expenses and provides a baseline for comparative purposes. The fiscal impact can be indexed against organizational earnings and/or operational expenditure costs to develop internal accountability metrics.

This d/PE™ equation includes measures such as the impact of derailing behaviors and directly links the consequences of those actions to corporate earnings. For example, discretionary effort is the amount of exertion an employee gives above what is required, to avoid being seen as "slacking off." In an effort to reduce redundancy and drive down costs, fostering discretionary effort is critical to helping organizations get more out of less. Employers pay for 100 percent of an employee's effort. If the employee gives less effort than the employer is paying for, a "discretionary effort deficit" results. If an employee self-reports giving the employer 75 percent of his or her best efforts on a regular basis, and the total compensation for that person is $70,000, then the employer is actually getting $52,500 and is basically losing $17,500.

"This d/PE™ equation includes measures such as the impact of derailing behaviors and directly links the consequences of those actions to corporate earnings."

Many organizations measure the impact of turnover, which measures the impact when people quit and leave the organization. The diversity profit equation also takes into account the impact of what the primary research has called "turn-under™ ."

Turnover is the effect when people quit and leave the organization. Turn-under™ has a stronger effect because people in this category quit, and stay!

Our initial study indicated that 57 percent of employees self-report giving less than 100 percent of their best effort at work on a regular basis. (Turn-under™ !) Yet when employees feel a sense of ownership, engagement and commitment, their amount of discretionary effort increases in turn—leading to reduced costs and increased profitability. (See Sidebars 3 and 4)

For employees whose level of commitment and ownership attitude were adversely affected by derailing behaviors, we also found an increased numbers of sick days and unexcused absences. Unplanned absences include costs such as lost productivity, overtime paid to other staff members, payments to temporary workers hired to fill in, decreased productivity for workers having to put in extra hours, and decreased employee morale, which cause problems in performance and turnover. Some increases in sick leave are associated with physical ailments that result from stress. However, sometimes employees aren't physically ill; they're just "sick" of coming to work, especially when there are "toxins" in the organizational culture.

Case study showing fiscal impact—Xcorps

We have created a sample theoretical case in Sidebar 5 that shows an example of the fiscal impact derailing behaviors can have on a company. The case quantifies that behavior in terms of dollars and cents—eventually translating into impact on "earnings per share" (EPS).

"However, sometimes employees aren't physically ill; they're just 'sick' of coming to work, especially when there are 'toxins' in the organizational culture."

In a case study we created, a sample company, Xcorps, worked out the fiscal impact of derailing behaviors on the company's Earnings Per Share (EPS). EPS can be calculated by taking the total earnings of a company and dividing it by the number of shares outstanding. Any reduction in the EPS from quarter-to-quarter is viewed as negative.

In our sample case study company, 81 percent of employees report being impacted by some type of derailing behavior. Of those employees encountering these behaviors, 24 percent stated they had actually lost time either avoiding the person who committed the behavior or simply worrying. Further analysis shows that the company may well be losing $19 million a year due to these derailing behaviors—a figure sure to grab the attention of senior leadership.

Additional financial implications

Not taken into account in these calculations are numerous other fiscal metrics that can be calculated and linked to the ROI for diversity and inclusion programs. Not included would be financial metrics such as the following:

- Lost revenue per (Full Time Equivalent – FTE) e.g. the number of full-time employees or the equivalent thereof
- Lack of effort being given (e.g., 57 percent report giving less than 100 percent on a regular basis)
- Impact of productivity lost due to (Time to Fill - TTF) days (how many days it take to find and hire someone to take over the job responsibility of the departing employee)
- Impact of ideas and suggestions
- Impact of lawsuits and settlements linked to derailing behaviors
- Eight to 10 other metrics!

Defining the "d/PE™" and its connection to shareholder value

The d/PE™ (diversity profit equation) is an internal comparative metric that allows companies to establish goals and targets based on fiscal metrics and models that impact earnings. Using these metrics can give organizations a process-oriented approach to eliminating inappropriate behaviors from the workplace while linking to organizational strategic goals. The diversity profit equation, shown below, can also give companies an idea of where they stand with key constituents.

Diversity Profit Equation d/PE™

d/PE™ = $dR/RI + $dR/OC +$dR/PLI
dR/RI: Diversity Related Revenue Increase
dR/CR: Diversity Related Opportunity Costs
dR/PLI: Diversity Related Pipeline Impact Costs/Savings

Finding the impact of your diversity program on your organization's earnings

In today's global economy, becoming diverse is inevitable, but retaining and leveraging diverse talent is critical for success. Organizations that strive for sustained success must develop a corporate culture of fully engaged and committed employees—supported by a culture that values, monitors and continuously manages diversity.

In connecting organizational culture and diversity to the bottom line, the d/PE™ offers an organizational ROI model that enables buy-in from all corporate stakeholders. The d/PE™ also provides a financial performance measure to increase shareholder value and leverage investment capital. And it serves as a compliance tool to reinforce corporate ethics and drive best practices in diversity management.

"In today's global economy, becoming diverse is inevitable, but retaining and leveraging diverse talent is critical for success."

An organizational ROI model

As we mentioned before, companies and consulting firms have been looking for a solution to the diversity ROI challenge for many years. That challenge has become particularly important in light of the recent economic restraints; it has now become more critical to provide greater justification for diversity programs above and beyond being "the right thing to do."

Most organizations are currently experiencing a fiscally constrained environment. That frugality has caused people to take a second and third look at organizational expenditures. The term ROI is inevitably linked to financial restraint. As a result, when companies are forced to tighten their fiscal belt, diversity initiatives are often vulnerable. Linking corporate diversity efforts to an ROI process is the first step in positioning diversity management, not as another cost center, but as a strategic initiative.

In an environment of increased cost controls, the d/PE™ drives ROI to a bottom-line number that can serve to justify an organization's diversity budget. Strategic applications involve leveraging investment capital and developing organizational accountability models that have a positive impact on the profits (or losses) of the company, while increasing total shareholder value.

Most diversity ROI studies have looked at the impact on performance and productivity from "having" diversity but are inconclusive in providing empirical data that connect diversity benefits to the bottom line. Exceptions are studies highlighting the importance of niche marketing and ethnic marketing as ways to grow business opportunities or expand product offerings. Research conducted in 2001 by the Catalyst Organization, for example, has documented increased sales connected to organizations with diversity in their senior management teams. Yet these studies have not delivered the fiscal links that validate the business case for managing diversity in the workplace versus the marketplace. The equation we have created can help companies move from those more siloed measurements to a broader evaluation of the impact of their diversity programs and efforts on a companywide basis. They will be able to see the impact of not cultivating the right programs and/or environment—the first step toward improving employee productivity and thus company earnings. Δ

"The equation we have created can help companies move from those more siloed measurements to a broader evaluation of the impact of their diversity programs and efforts on a companywide basis."

STUDY NOTE: Major portions of this article are based on a study conducted by the University of Houston's Institute for Diversity in 2006 and 2009, which surveyed employees at 13 companies. More than 10,000 respondents participated in the study designed to measure the degree to which derailing behaviors and corporate culture impacted an organization's ability to leverage the goal of increased numbers of high-performing work groups. For more detailed information on this study, go to http://www.craigclayton.com.

AUTHOR'S NOTE: The Spartacus Group utilizes a Web-based survey tool to drive the numbers and integrate qualitative assessment techniques to link correlations in the data to causal factors that can be acted upon. More information is available at www.thespartacusgroup.com or from Craig Clayton, president of the group, at craig@craigclayton.com or through the Web site www.craigclayton.com.

SIDEBAR 1
Derailing Behaviors

Broken Dignity Entitlements[1] *Dignity entitlements* are not a part of an employee's written contract, yet they are part of what employees expect and should receive in the workplace. When dignity entitlements have been fulfilled it leads to the willingness of employees to give their best efforts on a regular basis.	**Corporate Bullying**[2] Corporate bullying includes interpersonal behaviors in the workplace that can manifest in several ways and in several forms such as persistent and unjustified criticism or unfair allegations of incompetence.
Micro-Inequities[3] Micro-inequities are subtle forms of demeaning behaviors that rarely violate organizational policies, yet still make people feel violated. These terms were coined in a 2001 study by MIT's Sloan School of Business.	**Acts of Incivility**[4] A study by Brookings Institute identified behaviors that were evidenced as disrespectful and/or demeaning which undermined the dignity and self-esteem of employees and creating unnecessary suffering in the workplace. These behaviors go way beyond just being impolite.
*See footnotes for Exhibit 1 at end of article.	

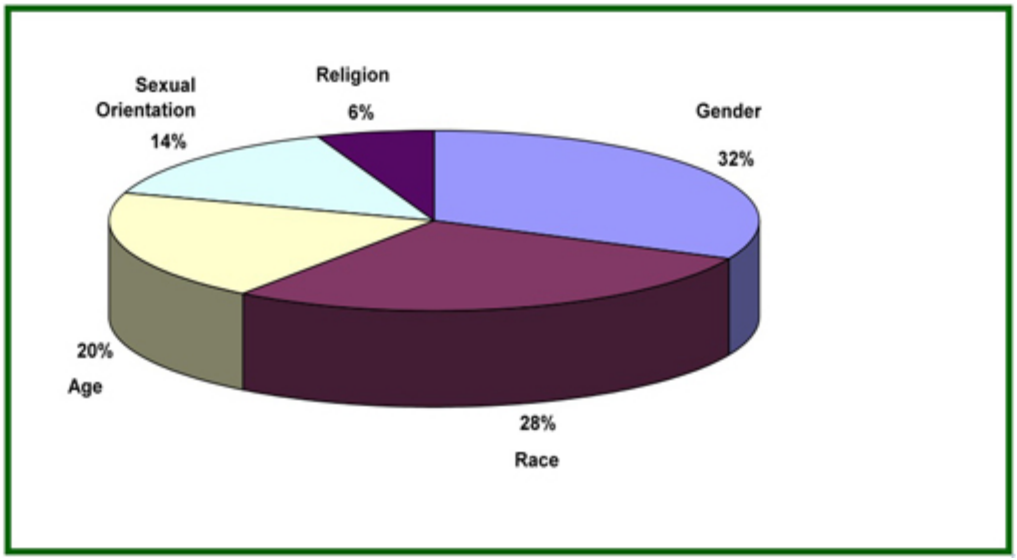
Endnotes:

1. Dignity Entitlements: See M. B. Arthur & D. M. Rousseau, "A New Career Lexicon for the 21st Century," *The Academy of Management Executive*, November 1996.
2. Corporate Bullying: See Craig B. Clayton, Sr., *The Brutus Syndrome: Linking Derailing Behaviors to the Bottom Line* (White paper for The Spartacus Analytics Group), January 2005, www.hrm-ri.org/whitepapers/The_Brutus_Syndrome_v6.0.pdf
3. Micro-Inequities: See M. P. Rowe, "Barriers to Equality: The Power of Subtle Discrimination to Maintain Unequal Opportunity," *Employee Responsibilities and Rights Journal, 3*: 153–163, 1990.
4. Workplace Incivility: See D. G. Zauderer, "Workplace Incivility and the Management of Human Capital: How to Build a Community Where People Feel Included, Welcomed, and Work Together With Mutual Respect to Enhance Individual and Organizational Productivity," *The Public Manager,* 3: 36+, 2002.

SIDEBAR 2
Impact of the Index on Various Constituencies

CONSTITUENT	BENEFIT
Employees	Improved workplace
Management	Increased employee performance and production
Labor Representatives	Enhanced value of labor and intellectual capital
Board Members	Improved shareholder value through increased performance
Investors	A fair return on investment through responsible practices

SIDEBAR 3
Diversity-Related Acts of Incivility (DRIs)



SIDEBAR 4
Fiscal Impact of Workplace Incivility

- 28% lost work time avoiding the instigator of the incivility
- 53% lost time worrying about the incident/future interactions
- 37% believe their commitment at work declined
- 22% have decreased their effort at work
- 10% decreased the amount of time that they spent at work
- 12% actually changed jobs to avoid the instigator

Pearson-Andersson & Porath, "Assessing and Attacking Workplace *Incivility*," *Organizational Dynamics*, Fall 2000.

SIDEBAR 5
Case Study Showing the Fiscal Impact of Derailing Behaviors

In our sample company, Xcorps, with 50,000 employees, 81 percent (40,500 people) had witnessed or experienced one or more of four derailing behaviors in the last 12 months, with the average number per person being 3.95. For this company, then, the total of incidents for the past 12 months was 159,975. Twenty-four percent of those witnessing and/or observing these behaviors (9,720 people) lost time because they were avoiding and/or worrying about the person who committed the behaviors.

For each incident, these 9,720 people reported spending an average of 53 minutes per day for 2.5 days each week over a 7.8-week period losing productive time avoiding and/or worrying—a total of approximately 17.2 hours per employee, per incident. At an average annual pay rate (salary and overhead) of $60,000 per employee, each employee's compensation averaged $231 per day. So if these 9,720 people experienced 3.95 incidents of derailing behavior each year (38,394), then the total cost of lost productivity each year came to approximately $19,068,357.

According to the University of Houston study, 65% of those experiencing derailing behaviors said that they would leave, or seriously consider leaving (Yes or Maybe) if a better job were offered. Of those surveyed, 81 percent said that they had experienced derailing behaviors in the last 12 months. These data suggest that many of those who have said they will leave their jobs are leaving for reasons linked to how they are treated in the workplace. Qualitative data subsequent to the survey has supported this link between derailing behaviors and employees who leave their jobs. There is a fiscal impact to companies from this effect.

In calculating the cost of turnover per percentage point, a company of 50,000 employees would expect to lose a total of 500 people for every percentage point of turnover. In determining replacement costs (the cost of recruiting and hiring a new employee to replace one who has left), the HR industry estimates 50 percent to 150 percent of total compensation. A conservative replacement estimate, then, for an employee earning $60,000 would be $30,000, and it could go as high as $90,000. Even at a $30,000 per person replacement cost, then, a company can expect to pay $15 million per each 1 percent of turnover. In our case study, if we assume that of the 81 percent (40,500 employees) who experience derailing behaviors only10 percent (4,050 people) actually quit their jobs, then based on these behaviors, at a per person replacement cost of $30,000, Xcorps could expect to spend $121,500,000. (That number could actually be as high as $363M if replacement costs were at the high end of that scale!)

Earnings per share (EPS) varies by company, but considering our case study company, Xcorps, the fiscal impact could be over 2 cents on an EPS basis—quite a hefty amount that would certainly get the attention of the CEO and leadership team.

Return to the Table of Contents