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# Upper Echelon Theory Revisited: The Relationship Between Upper Echelon Diversity, the Adoption of Diversity Practices, and Organizational Performance

Lisa Hisae Nishii  
*Cornell University, lhn5@cornell.edu*

Anne Gotte

Jana L. Raver  
*Queen's University*

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Using data from 260 U.S. organizations, we found partial support for our hypotheses that demographic diversity of senior management would be positively associated with the diversity of the workforce, adoption of diversity practices, and power of an organization's diversity/EEO officer, and that diversity practices impact organizational performance.

Organizations wishing to attract, retain, and benefit from diverse talent are often advised to begin by increasing the diversity of their senior management. Data collected from 260 U.S. organizations supports this idea. We found that the demographic diversity of senior management teams is positively associated with the demographic diversity of workforces at large and with the adoption of diversity practices, and that, furthermore, those firms that adopted diversity initiatives outperformed those that did not. Organizations that have diversity/EEO officers with real power and clout were more likely to benefit from these effects.

## **Keywords**

CAHRS, ILR, center, human resource, job, worker, advanced, labor market, satisfaction, employee, work, manage, management, health care, flexible benefit, HRM, employ, model, industrial relations, job satisfaction, job performance, productivity, measurement, compensation, pay, voluntary turnover, salary, pay level, benefit, pay raise, job growth, managerial, employment growth, college degree

## **Disciplines**

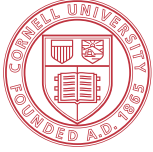
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**Cornell University**  
School of Industrial and Labor Relations  
Center for Advanced Human Resource Studies

CAHRS at Cornell University  
615B Ives Hall  
Ithaca, NY 14853-3901 USA  
Tel. 607 255-9358  
[www.ilr.cornell.edu/CAHRS](http://www.ilr.cornell.edu/CAHRS)

WORKING PAPER SERIES

# Upper Echelon Theory Revisited: The Relationship Between Upper Echelon Diversity, the Adoption of Diversity Practices, and Organizational Performance

Lisa Nishii  
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Working Paper 07 – 04



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Using data from 260 U.S. organizations, we found partial support for our hypotheses that demographic diversity of senior management would be positively associated with the diversity of the workforce, adoption of diversity practices, and power of an organization's diversity/EEO officer, and that diversity practices impact organizational performance.

Organizations wishing to attract, retain, and benefit from diverse talent are often advised to begin by increasing the diversity of their senior management. Data collected from 260 U.S. organizations supports this idea. We found that the demographic diversity of senior management teams is positively associated with the demographic diversity of workforces at large and with the adoption of diversity practices, and that, furthermore, those firms that adopted diversity initiatives outperformed those that did not. Organizations that have diversity/EEO officers with real power and clout were more likely to benefit from these effects.

## **Upper Echelon Theory Revisited: The Relationship Between Upper Echelon Diversity, The Adoption Of Diversity Practices, And Organizational Performance**

Organizations wishing to attract, retain, and benefit from diverse talent are often advised to begin by increasing the diversity of their senior management (Cox, 1994; Gelfand, Nishii, Raver, & Schneider, 2004). Doing so has been proposed to help not only because of the signal that it sends to diverse employees about their advancement potential, but because a diverse senior management team is more likely to be sensitive to the issues requiring attention for the retention and advancement of diverse employees. Thus, organizations with more diverse senior managers are expected to adopt diversity initiatives, which help organizations attract diverse talent and also facilitate organizational functioning through more careful attention to the needs of diverse (and not just “traditional”) employees.

The notion that the characteristics of senior management, or the upper echelon of an organization, can influence the decisions made and practices adopted by an organization dates back to early upper echelon theory (Hambrick & Mason, 1984). Hambrick and Mason argued that managers’ characteristics (e.g., demographic) influence the decisions that they make and therefore the actions adopted by the organizations that they lead. They suggest that this occurs because demographic characteristics are associated with the many cognitive bases, values, and perceptions that influence the decision making of managers. Several studies have supported the relationship between upper echelon characteristics and organizational strategies and performance. For example, there is evidence that top management team (TMT) job-related diversity is related to the internationalization of firms (Lee & Park, 2006); TMT diversity in age, tenure, and education have been associated with organizational innovation (Camelo-Ordaz, Hernandez-Lara, & Valle-Cabrera, 2005; Bantel & Jackson, 1989), changes in corporate strategy (Wiersema & Bantel, 1992), and information use (Dahlin, Weingart, & Hinds, 2005); and finally, TMT gender diversity interacts with organizational culture and growth orientation in affecting organizational performance (Dwyer, Richard, & Chadwick, 2003).

To our knowledge, however, there has not yet been research examining the influence of

upper echelon demography on *diversity* issues within organizations. As mentioned previously, there is ample reason to believe that the demographic diversity that is represented in upper echelons should have positive consequences for diversity-related issues within organizations. Consistent with an early distinction made by Ilgen and Youtz (1986) regarding different types of discrimination in organizations, we focus specifically on two foci of diversity initiatives: efforts to reduce *access discrimination*, or to increase the sheer representation of minority employees within organizations, and efforts to decrease *treatment discrimination* by removing obstacles to the success of minority employees. Our expectation is that organizations with greater demographic diversity in senior management will be characterized by greater demographic diversity throughout the employee population at large, and will also be more likely to have in place diversity initiatives designed to decrease treatment discrimination. Moreover, we expect that organizations that adopt diversity practices that have been identified in past research as being vital for the effective management of diverse workforces to outperform those that do not.

### **Enhancing The Access Of Diverse Employees**

Our first hypothesis about the effects of upper echelon diversity has to do with the diversity of the workforce at large. Given the tendency for demography to perpetuate itself because of “homosocial reproduction” in which people hire and promote those individuals who are similar to themselves (Kanter, 1977; Perry, Davis-Blake & Kulik, 1994; Pfeffer, 1985; Ragins & Sundstrom, 1989), we expect that the demography of senior management will be positively associated with the demography of the workforce at large. In support of this idea, Baron and colleagues (1991) found that organizations with female executives achieved higher levels of gender integration throughout the organization than organizations with male executives. The diversity of the workforce is likely to be positively affected by upper echelon diversity not only because diverse senior managers are more likely to hire diverse others, but because the diversity of senior management sends important messages to the rest of the organization. In particular, when “non-traditional” individuals (i.e., ethnic minorities, women, and people with

disabilities, etc.) hold leadership positions, they help to create new schemas in the minds of employees, in which leadership attributes and competence become associated not only with white males, but also with minority characteristics (Perry et al., 1994). While a single minority individual in senior management is unlikely to have this schema-changing effect, repeat examples of minority status being associated with leadership competence (as would be the case in diverse senior management teams) is likely to change employees' perceptions of the competence of non-traditional employees (Perry et al., 1994). As a result, selection decisions should be less likely to be contaminated by biases about the relative lack of competence of minority individuals, as reflected in higher overall levels of diversity within the organization (cf. Morrison, 1992).

H1: The demographic diversity of senior management (ethnic, gender, and disability) will be positively associated with the demographic diversity of the workforce at large.

The positive influence of the demographic diversity of senior management on the demographic diversity of the workforce at large is a moot point, however, if an organization lacks diversity in senior management. Indeed, a lack of demographic diversity in senior management as a result of the "glass ceiling" continues to be one of the most pervasive diversity-related (i.e., access discrimination) problems in organizations. For instance, women make up only 34% of "officials and managers" in U.S. corporations, whereas they constitute 47% of the private workforce. Moreover, only 15% of "officials and managers" are racial minorities despite the fact that they represent 30% of the private U.S. workforce (U.S. Equal Employment Opportunity Commission, 2001). A number of studies have documented the fact that the status of women and minorities has not improved in recent years, despite wider-spread recognition of the problem (e.g., Catalyst, 2005; U.S. General Accounting Office, 2002). Thus, in our second hypothesis, we take a step back and consider an important predictor of the demographic diversity of senior management teams.

The inability of organizations to successfully change their cultures and practices such that

more women and minorities will be promoted to senior management has been blamed on the lack of power and prestige associated with diversity initiatives. That is, unless change efforts are led by the most senior officials in an organization, they are not likely to be successful. One way in which organizations can provide senior-level commitment to diversity is to allocate a formal position for the Diversity (or EEO) Officer (Arvey, Azevedo, Ostgaard & Raghuram, 1996). When diversity officers are highly respected and powerful, their organizations are more likely to be well integrated, as reflected in high proportions of women and racial minorities in senior management (Pfeffer, Davis-Blake & Julius, 1995). Accordingly, we expect that:

H2: The power and prestige held by the diversity officer in an organization will be positively associated with the proportion of women, racial minorities, and people with disabilities in senior management.

### **Enhancing The Treatment Of Diverse Employees**

It is no secret that simply increasing the diversity of a workforce is insufficient. Once hired, diverse employees need to be fairly treated and integrated into the social fabric of the organization. Many scholars have argued that the commitment of senior managers is necessary for the success of diversity initiatives (e.g., Cox & Blake, 1991; Gelfand et al., 2004; Wentling, 2004), and that given resource constraints, the senior management team is instrumental in determining whether or not an organization will adopt certain initiatives designed to reduce discrimination and promote the advancement of diverse employees. The more leaders believe in the need to include all employees and remove obstacles to their success (Stoner & Russell-Chapin, 1997), the more likely they are to see to it that their organization takes proactive measures toward this end.

We expect that senior managers who are women, ethnic minorities, or disabled will be more aware of and sensitive to the systemic factors that can bias against minorities in the workforce, in large part because of their own experiences in organizations. Therefore, diversity in the senior management team will be positively associated with the adoption of practices aimed at



reducing discrimination against and enhancing the success of minority workers. We expect that diverse senior management teams will be more likely to act as “diversity champions” and take an active role in ensuring that the organization, for example, monitors selection and promotion rates to detect evidence of bias, conducts targeted recruiting, implements diversity training, and hold line managers accountable for achieving diversity goals, than senior management teams dominated by White, able-bodied men. This hypothesis is consistent with upper echelon theory in that we expect senior managers to have an important impact on the adoption of diversity practices because they are empowered to make company decisions that are consistent with their values and personal experiences (Hambrick & Mason, 1984; Smith, Smith, Olian, Sims, & O’Bannon, 1994).

H3: The diversity of senior management (race, gender, disabilities) will be positively associated with the adoption of diversity practices.

Finally, given that competitive advantage is predicated on the effective management and utilization of human resources, we expect that in an era of increased labor force diversity, those organizations that implement diversity practices designed to reduce discrimination and facilitate the development and advancement of diverse employees will outperform those organizations that do not. Our hypothesis is based on the idea that implementing diversity practices designed to reduce barriers to the success of minority employees is an important foundational step for capitalizing on the potential benefits of a diverse workforce. Unless diverse employees feel that their needs are being addressed and efforts are being made to help them succeed, they are unlikely to reciprocate in the form of commitment to, and hard work for, the organization (Gelfand et al., 2004). In addition, the adoption of such programs may help organizations to enhance their reputations with potential customers, since women and minorities may be more inclined to purchase from organizations that exhibit a commitment towards diversity (Cox & Blake, 1991). Finally, organizations that implement diversity practices may be more likely than those that do not to benefit from better problem-solving capabilities because of their better

integrated diverse workforces (Cox, 1994). Thus:

H4: The adoption of diversity practices will be positively associated with the profitability and rate of innovation of organizations.

### **Method**

In order to test our hypotheses, we collected online data from a sample of U.S. organizations that were listed in a commercially available directory called the *Leadership Directory*. Senior HR officials from 260 out of 510 organizations responded to our online survey, for a response rate of 43%. The distribution of organizations represented in our sample is largely representative of the U.S. economy in terms of industry type.

#### *Measures*

*Power of the diversity officer.* Survey respondents were first asked to indicate whether their organization has someone who's main responsibility is managing diversity/EEO. If they reported having such a diversity officer, they were directed to a follow-up question in which they were asked, "to what extent does this person have power and clout within the organization?" Response choices ranged from 1 = "not at all," to 5 = "extremely." Responses to this follow up question were used to test hypothesis 1.

*Diversity of senior management.* We focused on 3 of the legally protected classes when assessing the diversity of the senior management team and of the workforce more generally: gender, race, and disabilities. Respondents were asked to provide the percentages (separately) of racial minorities, women, and people with disabilities in the workforce, and then in senior management, and were also given the option of indicating that they did not know. Because their responses were in the form of percentages, we simply examined the proportion of each of these groups in senior management and the workforce at large when testing our hypotheses.

*Diversity programs.* In order to assess the attention being paid to diversity through the adoption of diversity practices, survey respondents were asked to indicate, on a 5 point Likert-type scale (1=not at all, 5=extremely), the extent to which their organization: 1) emphasizes inclusiveness and/or diversity as part of the organization's mission; 2) includes diversity-related

goals in managers' performance assessments; 3) engages in targeted recruiting to increase numbers of underrepresented groups; 4) monitors selection rates of under-represented groups; 5) provides diversity training; 6) provides mentoring programs for members of underrepresented groups; 7) monitors promotion decisions to ensure fairness to underrepresented groups; and 8) offers grievance procedures. We asked respondents about the adoption of these practices based on the growing literature on diversity management which emphasizes these as important components of diversity initiatives (e.g., Cox, 1994; Gelfand et al., 2004). A principal components factor analysis using varimax rotation indicated that the 8 items comprised a single factor that explained 54% of the variance. The reliability of this 8 item scale was  $\alpha = .88$ .

*Organizational performance measures.* Recent research has shown that subjective measures of organizational performance are positively associated with objective measures and that they exhibit equivalent relationships with independent variables (Wall, et al., 2004), and thus we felt confident about our decision to assess the gross revenue, profitability, and rate of innovation of participating organizations using subjective measures. Specifically, we assessed profitability and rate of innovation using relative measures in which respondents were asked, "Compared to other organizations in your sector, where would you rate the performance of your organization in relation to profitability (rate of innovation): 1 = lower half; 2 = upper half; 3 = top 10%."

### **Results – need to write out properly**

We tested our hypotheses using a series of partial correlation analyses controlling for organizational size. In partial support of hypothesis 1, in which we argued that the diversity of senior management would be positively associated with the diversity of the workforce at large, we found that the proportion of women in senior management was significantly associated with the proportion of women in the workforce (partial  $r=.46$ ,  $p<.01$ ), and that the proportion of racial minorities in senior management was significantly related to the proportion of racial minorities in the workforce (partial  $r=.77$ ,  $p<.01$ ). However, correlations involving proportions of people with

disabilities were all non-significant. In hypothesis 2, we stated our expectation that the power and prestige held by the diversity officer in an organization will be positively associated with the proportion of women, racial minorities, and people with disabilities in senior management. Our data supported this general notion, for after controlling for organization size, the power and prestige of the diversity officer was positively associated with proportion of racial minorities (partial  $r=.29$ ,  $p<.05$ ) and women (partial  $r=.34$ ,  $p<.01$ ), but not with the proportion of people with disabilities in senior management. Hypothesis 3 stated that the proportion of women, racial minorities, and people with disabilities in senior management would be positively associated with the adoption of diversity practices. Our results indicated that the relationship involving the proportion of racial minorities in senior management and the adoption of diversity practices was surprisingly non-significant, but the partial correlations involving the proportion of women in senior management ( $r=.15$ ,  $p<.05$ ) and people with disabilities ( $r=.17$ ,  $p<.05$ ) were significant. Finally, with regard to hypothesis 4, that the adoption of diversity practices would be positively associated with organizational performance, we found that the partial correlation involving the adoption of diversity practices and profitability (partial  $r=.13$ ,  $p<.05$ ) was significant, although the one involving rate of innovation (partial  $r=-.06$ ,  $p>.05$ ) was non-significant.

### **Discussion**

Overall, our results, which were largely supportive of our hypotheses, suggest that the demographic diversity of senior management can have profound effects on organizations. Upper echelon diversity is associated with the demographic diversity of the workforce, with evidence of homosocial reproduction taking place in organizations, particularly with regard to gender and race. In addition, the demographic diversity of senior management is also associated with the adoption of diversity practices, which in turn is associated with higher profits. Furthermore, those organizations in which diversity officers are highly respected and powerful are more likely to exhibit this pattern in that they are more likely to have the diversity in senior management teams that is associated with the adoption of diversity practices. This

supports past arguments that the success of diversity initiatives hinges on support from the top.

Although we found at least partial support for all of our hypotheses, we did not assess the mediating psychological mechanisms that make it more likely for diverse senior management teams to be champions of diversity efforts, and thus future research should examine these factors. However, the fact that our hypotheses were supported despite the noise associated with assessing the effects of TMT demographic characteristics rather than the psychological constructs for which the demographic characteristics are proxies (Hambrick & Mason, 1984), suggests that our significant findings are indicative of a robust effect.

As with any study there are a few notable limitations of our study. First, because of the cross-sectional nature of our data, we were unable to assess causality in the relationships between variables. For example, although we suggested in our second hypothesis that the integration of minorities into senior management is more likely to occur in organizations that have powerful diversity officers, it is entirely possible that the direction of this relationship runs in the opposite direction such that diverse senior management teams create more powerful diversity officer positions. The cross-sectional nature of our data also makes it possible that the findings reported here are inflated due to common method bias, although that threat is not as great as would be the case had the data collected been about respondents' attitudes rather than objective facts about their organization (Podsakoff, MacKenzie, Lee, & Podsakoff, 2003). Furthermore, the fact that there were a number of non-significant relationships among variables also suggests that common method bias may not be too big a concern, for if it were, we would expect to see all variables correlated with each other.

## **Conclusion**

Given rapid increases in the demographic diversity of the working population in the U.S., few people would argue that diversity initiatives are now a must for organizations. However, there continues to be significant variability in the extent to which diversity initiatives are adopted by organizations. The purpose of this study was to examine the predictors of the adoption of diversity programs that matter for the bottom line, and we found that, as with many things in organizational life, success starts at the top. We hope that our results will encourage organizations to take diversity initiatives seriously, and to do so first by creating formal and very powerful diversity officer positions. Individuals who fill these positions should have direct access to, and voice in, the decision making of the senior executive team. When diversity initiatives are backed by strong leadership support, and therefore are successful at accomplishing the cultural change they are designed to accomplish, the investment made in their adoption pay dividends to organizations in the form of increased competitive advantage.

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