Lawful DEI in Practice: What California Employers Need to Know Amid Federal Scrutiny

Corporate diversity, equity and inclusion (DEI) programs were once a widespread tool for improving equality in the workplace and reflecting a company's cultural values. But in 2025, they've rapidly become a complex compliance landscape.

Federal scrutiny of corporate DEI initiatives is intensifying, and legal challenges are mounting, with recent executive orders and lawsuits targeting any hint of race- or gender-based preferences. Meanwhile, California employers must still comply with some of the country's most proactive antidiscrimination laws. This tension has left corporate legal departments and in-house counsel navigating a confusing and high-stakes set of rules and risks.

Many companies have responded by scaling back their DEI efforts, scrubbing language from websites or quietly pausing affinity group events, hoping to fly under the radar. But for employers in California, where state law often imposes more expansive obligations on issues like pay equity and bias prevention, the path forward isn't necessarily to scale back but to reframe. In other words, the legal risk isn't just in doing too much — it could also lie in doing too little.

This sharp departure from the recent past demands a new, more compliance-focused approach from in-house counsel and legal teams. Here's what California attorneys need to know about navigating DEI considerations in 2025.

The regulatory shift: What's really changed?

Affirmative action and diversity tracking were once the standard for federal contractors. Recent executive orders, however, have rolled back federal DEI requirements and directed agencies to enforce civil rights laws more aggressively, particularly targeting what the White House describes as illegal preferences in hiring and promotion.

And while the U.S. Supreme Court's 2023 decision in *Students for Fair Admissions v. Harvard* banning affirmative action in college admissions didn't target private employers, it did send a clear message: Anything that looks like a quota or preference could be a landmine. Recent court decisions have blocked some executive orders, but the situation is evolving quickly.

Key changes include:

- **Executive orders rolling back DEI**: In early 2025, President Donald Trump signed sweeping executive orders that not only eliminated all federal DEI programs and positions but also revoked **Executive Order 11246**, ending affirmative action requirements for federal contractors. The **new federal policy** is to reward individual merit and expressly prohibit any consideration of DEI factors, goals, or mandates in federal employment or contracting.
- **Aggressive enforcement and new legal tools**: The U.S. Department of Justice has announced that it will use the False Claims Act (FCA) — a statute allowing for treble damages and uncapped civil penalties — to pursue claims against recipients of federal funds who "falsely certify" compliance with federal civil rights laws, including those related to DEI. This is a significant expansion because, unlike most civil rights laws, the FCA exposes organizations to much larger financial risks.
- **Certification requirements and whistleblower risks**: Federal contractors and grantees must now certify that they do not operate "illegal" DEI programs. This opens the door for both government enforcement and whistleblower lawsuits, which can lead to costly investigations and litigation.
- **Targeted investigations and public scrutiny**: Attorney General Pam Bondi has been directed to identify and investigate private sector companies with "egregious and discriminatory" DEI programs, signaling that large corporations and nonprofits are in the crosshairs for regulatory action and potential litigation.
- **Broader definition of "illegal" DEI**: The administration has not clearly defined what constitutes "illegal" DEI, but the government is taking a broad view, targeting anything that could be construed as a preference, quota or goal based on protected characteristics. Even aspirational diversity targets, certain training programs or affinity groups are now under scrutiny.

How broadly is DEI defined?

The definition of DEI currently under federal scrutiny is notably broad. While DEI is often primarily associated with race and gender, recent policy changes and enforcement actions have targeted a wider range of programs. The federal government's approach now encompasses any initiative that could be seen as giving preference based on any protected characteristic, including disability, veteran status, income level, and age. This means that programs designed to support people with disabilities, veterans, older workers, or individuals from low-income backgrounds — such as job training, healthcare access, or educational benefits — could also come under review if they are perceived as offering preferential treatment.

No federal law stops an employer from having the goal of achieving a diverse, equitable and inclusive workplace, but it does limit how it can be achieved. Any DEI program that appears to give preferential treatment based on a protected category — whether through hiring, promotions, training, or even aspirational goals — can now expose a company to significant legal and financial risk. The overarching message from federal regulators is that if a company's DEI program even appears to give preferential treatment based on race, gender, or other protected traits, it could be vulnerable to investigation, litigation, and substantial penalties.

Who is most impacted by federal DEI changes?

The most immediate and significant impact of recent federal DEI policy changes has been felt by companies that contract with the federal government or apply for federal grants and funding. This includes not only large corporations but also nonprofits and small businesses that rely on set-aside programs, such as 8(a), Women-Owned Small Business (WOSB), Service-Disabled Veteran-Owned Small Business (SDVOSB) and HUBZone contracting. These entities face heightened scrutiny, as federal agencies are now required to identify, review, and report all contracts connected to DEI initiatives, and they may restructure, cancel, or reallocate federal contracting opportunities as a result.

The challenge is particularly acute for employers who must balance compliance with more expansive California requirements while simultaneously ensuring their practices do not jeopardize eligibility for federal contracts or funding.

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How does this intersect with California's legal protections?

Meanwhile, California isn't following the federal retreat. The state's **Fair Employment and Housing Act (FEHA)**, **Equal Pay Act**, and **diversity reporting requirements** are all still in force, and regulators have doubled down on the idea that proactive, bias-reducing policies are not just legal but expected. That means employers must balance federal caution with state-level mandates, all while keeping an eye on new developments.

Key changes include:

- **FEHA and state anti-discrimination protections remain strong**: FEHA continues to prohibit discrimination in California based on a wide range of protected characteristics. In 2025, these protections have expanded to cover discrimination based on a combination of protected traits, such as being both Hispanic and female. FEHA also mandates antidiscrimination training and robust workplace protections, regardless of federal rollbacks.
- **Equal pay and transparency laws**: California's Equal Pay Act and updated wage **reporting** and **transparency rules** require employers to disclose pay ranges in job postings and maintain pay equity records.
- **Diversity reporting requirements**: The state's diversity reporting laws under **Senate Bill 54** for venture capital and certain other sectors remain in effect, with new amendments clarifying reporting obligations and enforcement, not eliminating them. The law doesn't mandate quotas or diversity targets; it only requires reporting demographic information. Covered entities should prepare for compliance by spring 2026 — though this reflects a one-year delay from the original timelines, and future changes are possible.

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Compliance strategies for law firms and employers

For in-house counsel, the goal is to thread a fine needle: stay legally compliant without abandoning the spirit of inclusion. There is still a clear path forward, but it requires nuance, legal fluency, and a thoughtful shift in strategy.

Here's how the most proactive legal departments are adapting:

1. Audit with precision

Start with a top-to-bottom review of the company's DEI programs. Look not only at hiring practices but also at internal communications, performance metrics, mentorship initiatives, and leadership training. Ask: Could any of these be misconstrued as race- or gender-based preferences? If so, reframe the approach, shifting emphasis to equal opportunity, inclusive culture, and a fair process.

2. Open the door for all

Affinity groups and mentorship programs don't have to end, but they do need to be structured around shared experiences, rather than identity alone. For example, a mentoring circle for first-generation professionals or early-career employees is lawful and impactful, especially when open to all who self-identify with the experience.

3. Move from outcome to process

Swap out representation "targets" for process metrics: Are job opportunities reaching a broad range of candidates? Are interviews being conducted consistently? Are performance reviews documented and criteria-based? Standardizing procedures will help mitigate bias without triggering unnecessary legal risks.

4. Calibrate the message

Words matter, and federal scrutiny can hinge on perception as much as intent. That means reviewing your public-facing DEI statements, website language, and internal policy documents. Favor terms such as inclusive hiring practices, equity in opportunity, and bias prevention training over language that could be construed as prioritizing any demographic trait.

5. Train, but don't preach

When conducting DEI or other anti-discrimination training, avoid messaging that could be viewed as coercive or ideological. Instead, focus on fostering awareness of unconscious bias, ensuring lawful hiring practices, and promoting respectful workplace behaviors. Ground training in the law, not politics.

6. Document everything

This is no time for informal policies. As federal scrutiny ramps up, documentation can become your strongest shield. Keep clear records of why initiatives were implemented, how they comply with California and federal law, and how decisions were made. Ensure a compliance trail is maintained for every DEI-related effort.

Focus on bias removal, not box-checking

The regulatory landscape may be shifting, but the business case for diversity hasn't changed. That's especially true for California, where innovation, creativity, and global markets hinge on a workforce with a broad range of perspectives — and where employers are still expected to take meaningful steps toward fairness and inclusion. The challenge now is to advance those goals without crossing legal lines.

That means shifting the focus away from demographic targets and toward building structures that reduce bias in practical, measurable ways. Rather than framing efforts around representation for its own sake, companies should focus on ensuring that hiring, promotion, and evaluation processes are consistent, defensible, and genuinely open to all qualified candidates.

Programs aimed at mentorship, retention, or engagement can continue, but they must be designed thoughtfully, with clear eligibility criteria and inclusive access. Demographic data can still inform internal analysis, but it must be handled with care, kept voluntary and anonymized, and used to identify potential barriers, rather than driving decision-making.

Legal departments play a critical role in this new environment. The most effective in-house counsel will help their organizations stay compliant while still fostering the kind of workplace culture that attracts and retains top talent. That doesn't mean walking away from DEI. It means making it legally sound, strategically focused and built to last.

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