

The Push For Corporate Board Diversity Requires Your Attention, Regardless of Legal Challenges

Labor & Employment Law Update

By Beverly Alfon on April 19, 2022

Board diversity requirements have hit the headlines again due to a recent ruling by a California Superior Court judge who struck down a 2020 California law (AB 979) that required companies headquartered in California to have from one to three board members who self-identify as a member of an “underrepresented community,” which includes Asian, Black, Latino, Native American, and Pacific Islander individuals, as well as those who are gay, lesbian, bisexual or transgender. It allowed the Secretary of State to fine companies who did not comply. The court found for the plaintiff, who argued that without a compelling state interest, the law imposes quotas based on race and ethnicity, and therefore violates the California Constitution’s Equal Protection Clause.

A similar legal challenge has been brought against California’s 2018 law (SB 826) which requires publicly listed corporations headquartered in California to have at least one woman on each board by the end of 2019, and then depending on board size, up to three female directors by the end of 2021. A trial has been held on the matter in Los Angeles Superior Court, but the court has not yet issued a ruling.

Massachusetts, Michigan, New Jersey, and Oregon are currently considering legislation that would impose board diversity quotas.

Other states have enacted laws that encourage board diversity – but do not include a mandated quota like the California laws. For example:

- In Illinois, a publicly listed corporation with its principal executive office in Illinois must include board diversity data in its annual reports and their policies and practices for promoting diversity, equity and inclusion among the board of directors and executive officers, and that information is made available to the public.
- New York has a board diversity disclosure law that requires both public *and privately held* domestic and foreign corporations authorized to do business in New York, to report the number of women directors on their board, along

with the total number of directors.

- In Maryland, tax-exempt, non-stock domestic corporations with operating budgets of more than \$5 million and domestic stock corporations with total sales of \$5 million or more must include in their state annual reports the number of female board members as well as the total number of board members.
- Washington state law requires specific diverse board representation. The law generally applies to public companies incorporated in Washington and requires that these companies either have a “gender-diverse board” (at least 25% of directors self-identify as women) or provide shareholders with a “board diversity discussion and analysis” as to why not. Notably, it does not carry any fiscal penalties like the California law.

Colorado passed a resolution encouraging “equitable and diverse gender representation on corporate boards.” The resolution urges public corporations in Colorado with nine or more directors to have at least three women; with five to eight directors, two women; and with fewer than five directors, at least one woman on the board. Similarly, Pennsylvania passed a resolution that calls upon public and private companies to allocate at least 30% of the board seats for women. However, neither resolutions are legally enforceable.

Outside of legislative arenas, other efforts to increase board diversity have been in motion. For example, the Securities and Exchange Commission has approved a rule by Nasdaq that will require companies listed on its exchange to disclose the ethnic and gender makeup of their boards and have at least two “diverse” members or explain why they do not. Similar policies have been issued by other investment firms and agencies, including Goldman Sachs, Institutional Shareholder Services, Inc. (ISS), Glass Lewis, and State Street Global Advisors. Notably, the SEC’s approval of the Nasdaq rule is being challenged in federal court, but for now remains in effect.

Bottom line: Regardless of the various legal challenges to mandated board diversity requirements, organizations should anticipate that efforts to encourage diversification at board and similar top-leadership levels will continue in one form or another, through investors or legislation. If your company seeks to increase diversity for your boards and other top-level positions, obtain legal counsel for structuring board searches in a manner that avoids violation of state or federal anti-discrimination laws, while also complying with applicable diversity laws and policies. Consideration should also be given to how diversity goals are included in director recruitment policies and procedures and corporate governance guidelines.

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