



## Boardroom Diversity Push Gains Steam

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As investors are exerting increased pressure on companies to address diversity in the boardroom, states may begin to address the issue through legislation. Recently, on September 30, 2018, Governor Jerry Brown signed SB826 into law, making California the first state in the nation to mandate gender diversity for the boards of public corporations. SB826 requires each corporation traded on a major US stock exchange and headquartered in California to have at least one female on their board of directors by the end of 2019. By July 2021, a minimum of two women must be on boards with five members and a minimum of three women on boards with six or more members. Companies that fail to comply with the law will face steep fines of \$100,000 for the first violation, and \$300,000 for every subsequent violation.

SB826 is the newest development in the rising trend of promoting increased gender equality and diversity representation in corporate boardrooms. Studies show that a more gender balanced boardroom can not only be good for a company's morale and overall atmosphere, but also its bottom line. A recent study by McKinsey & Company illustrated that companies having strong female representation at board or top-management levels also have higher levels of profitability, productivity, innovation, governance, performance and workforce engagement.<sup>1</sup>

Institutional investors and asset management companies such as CalPERS, CalSTRS, BlackRock, State Street Global Advisors and Vanguard are pushing for increased boardroom diversity. BlackRock's February 2018 Proxy Voting Guidelines illustrate its emphasis on gender diversity in boardrooms by mandating that companies elect at least two women directors on their boards.<sup>2</sup> Blackrock has contacted to every Russell 1000 company with fewer than two women on its board requesting a detailed explanation of its board diversification efforts.<sup>3</sup> Likewise, State Street actively engages various companies and board leadership, advocating for boardroom diversity. Of the 700 companies State Street recently engaged and targeted for having no female directors, more than 20% have since added at least one female director to their boards.<sup>4</sup> Further, State Street has launched a gender diversity campaign, "Fearless Girl," which encourages companies to have strong female presence on their boards and in senior management roles.<sup>5</sup>

Similarly, city and state governments have passed initiatives to incentivize boardroom diversity. The Boardroom Accountability Project 2.0, promoted by the New York City Comptroller, is an initiative focusing investors on board diversity.<sup>6</sup> It requires targeted companies to disclose the race, gender, and skill sets of their board members. By increasing transparency, the project attempts to combat the persistently pervasive lack of boardroom diversity. Other similar resolutions pushing for

<sup>1</sup> McKinsey & Company published its Diversity Matters report on February 2, 2015, <https://www.mckinsey.com/~media/mckinsey/business%20functions/organization/our%20insights/why%20diversity%20matters/diversity%20matters.ashx>.

<sup>2</sup> Blackrock's February 2018 Proxy Voting Guidelines can be found here: <https://www.blackrock.com/corporate/literature/fact-sheet/blk-responsible-investment-guidelines-us.pdf>.

<sup>3</sup> <https://www.bloomberg.com/news/articles/2018-02-02/blackrock-asks-companies-to-explain-dearth-of-women-on-boards>.

<sup>4</sup> See State Street's 2017 Stewardship Report, which can be found here: <https://www.ssga.com/investment-topics/environmental-social-governance/2018/07/annual-stewardship-report-2017.pdf>.

<sup>5</sup> [https://www.ssga.com/investment-topics/general-investing/2018/04/drive\\_change\\_gender\\_diversity.pdf](https://www.ssga.com/investment-topics/general-investing/2018/04/drive_change_gender_diversity.pdf).

<sup>6</sup> <https://comptroller.nyc.gov/services/financial-matters/boardroom-accountability-project/boardroom-accountability-project-2-0/>.

boardroom diversity have been passed in Pennsylvania, Massachusetts, Illinois, and Colorado.<sup>7</sup>

However, despite these efforts, studies by the US Government Accountability Office and Equilar GDI estimate that it would take 40 to 50 years for women to represent 50% of the boards of public companies.<sup>8</sup> Even as of 2017, California's 445 companies in the Russell 3000 with a total of 3,645 corporate directors only included 565 women.<sup>9</sup> These studies frequently cite the requirements established by certain regulating entities as being too general to be conducive of instrumental change. The Securities and Exchange Commission (SEC), for example, only requires the disclosure of whether, and if, a corporation's nominating committee considers diversity in identifying potential directors and how such policies are implemented and assessed.<sup>10</sup> Further, the SEC does not categorize "diversity" but instead allows the corporations to define the term as they seem fit. Such a broad policy allows companies to categorize "diversity" as including differing viewpoints, experiences, and perspectives. Such broad definitions fail to specifically include race, gender, ethnicity, or national origin, and do not promote the shift to institutional inclusion and equality promoted by certain prominent institutional investors and the State of California.

California's new legislative initiative resembles similar mandates adopted by several European nations.<sup>11</sup> Based on SB 826's requirements, at least 377 Russell 3000 companies will have to add at least one female director by December 2019. Of those, 175 companies would have to add two women to their boards, and 66 companies would have to add three women to their boards by December 2021. While many applaud the intention behind California's new law and agree that there are too few women at the boardroom table, they simultaneously argue the law is unconstitutional. The opposition, consisting of more than 30 businesses and supported by the California Chamber of Commerce, argues the law violates the common law internal affairs doctrine, the Fourteenth Amendment's equal protection clause, and Article 1 of the California State Constitution.

While the effectiveness and constitutionality of the California law is still unclear, the trend for increased boardroom diversity continues to grow. Companies can take the first step in achieving gender diversity in their own boardrooms. To help ensure a plentiful pool of qualified female candidates, companies should start developing women for board member roles earlier on in their careers. If women are not given the opportunity to serve in leadership executive roles, they will never achieve the necessary qualifications for board roles. Second, companies should re-evaluate their stringent director specifications, as many women who are qualified to serve in these roles do not always meet such narrow requirements. Lastly, companies should explore unconventional sources to find qualified women, such as accounting firms, the National Finance Center Database and the military. California's law is an admirable first step for increasing gender diversity in the boardroom. However, legislative mandates aside, companies must use internal measures to educate existing board members regarding the value of diversity and the need to re-examine company-wide diversity policies and procedures that govern board composition. An increasing number of investors are demanding boardroom equality and studies continue to show the positive impact and benefits of such policies on a company's profitability, productivity and innovation.

<sup>7</sup> The General Assembly of Pennsylvania, House Resolution No. 273, Session of 2017, April 2017; The 190th General Court of the Commonwealth of Massachusetts, Resolution S.1007, 2015; Illinois General Assembly, House Resolution 0439, 99th General Assembly, 2015; Colorado General Assembly, HJR 17-1017, 2017.

<sup>8</sup> <https://www.equilar.com/blogs/361-boards-will-reach-gender-parity-by-2048.html>.

<sup>9</sup> <https://www.linkedin.com/pulse/women-business-continue-fight-seat-board-tables-sb-826-bennyhoff/>.

<sup>10</sup> See the required disclosures in Item 407(c)(2)(vi) of Regulation S-K.

<sup>11</sup> "Norway in 2003 mandated 40% seats be held by women, followed by France and other European countries. Germany is the most recent (2015) and largest economy to mandate that 30% of corporate board seats be held by women."

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