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Skadden Offers a Scorecard on Diversity in the Corporate Boardroom

By Jessie K. Liu, Susan Saltzstein, Lauren Aguiar and Tansy Woan July 14, 2021

Comment

The social and political disruptions of the past year have heightened the awareness of diversity challenges, including at public and private companies in the U.S. In particular, the representation of women and other diverse individuals in the boardroom is of continuing relevance. Last month, Deloitte and the Alliance for Board Diversity^[1] published a comprehensive report analyzing the current makeup of boards of directors at Fortune 500 and Fortune 100 companies.^[2] That report concluded that the composition of boards at the country's largest companies has not changed materially in the last several years. Against this backdrop, a number of states have passed – and others are in the process of passing – legislation that may result in further progress on this front.

On the one hand, the Deloitte/Alliance report notes modest improvement on several metrics. White women have seen the largest increase in representation, achieving a gain of 15% (34 board seats) in the Fortune 100 and 21% (209 board seats) in the Fortune 500. Women and minorities^[3] combined occupy 38% of Fortune 500 board seats and 42% of Fortune 100 seats. On the other hand, the report also highlights notable shortcomings. For instance, there has been no substantial increase in the representation of minority men on boards at Fortune 500 and Fortune 100 companies. In fact, black men lost one seat in the Fortune 100 and five seats in the Fortune 500 in the last year. Minority women still represent the smallest percentage of boardroom seats at both the Fortune 100 and Fortune 500 level. Interestingly, the report also observes that more than 36% of diverse board seats overlap, meaning they are held by individuals who serve on *multiple* Fortune 500 boards.

In an attempt to address the issue, a number of states have passed, or are in the midst of passing, laws that aim to effect change in one of three ways: (1) mandating board diversity; (2) encouraging board diversity; or (3) requiring disclosure of board diversity information. In fact, California and Washington State have enacted statutes that require a certain number of board seats be held by women or underrepresented groups. Other states, such as Maryland and Illinois, require companies to disclose the demographic composition of their boards.

As of June 2020, New York State now requires that any for-profit corporation authorized to do business in that state disclose the number of directors on its board and how many of those directors are women.^[4] This law is particularly notable for its broad scope in applying to *any* for-profit corporation, in contrast to legislation in other states that applies only to companies listed on a public exchange. Another interesting example can be found in California, which recently mandated that all publicly listed companies headquartered in the state appoint at least one director from an underrepresented background to their board by the end of 2021.^[5] This expands on earlier legislation enacted by California in 2018, which required all public companies headquartered in the state to have at least one female board member by the end of 2019 with increases in subsequent years.^[6] Failure to comply with either California statute carries a \$100,000 penalty to the company for the first violation and a \$300,000 penalty for each additional violation. California already has faced several lawsuits challenging its 2018 statute. For example, in *Meland v. Padilla*, a shareholder filed a suit against California's Secretary of State challenging California Senate Bill No. 826 ("SB 826")^[7]. The U.S. District Court for the Eastern District of California held that the shareholder plaintiff lacked standing to bring suit. On June 21, 2021, the U.S. Court of Appeals for the Ninth Circuit reversed the trial court, finding that the plaintiff plausibly alleged that the statute requires or encourages him to discriminate based on sex, which was sufficient to establish standing and raise a Fourteenth Amendment challenge.^[8]

While California and Washington are currently the only states with mandatory diversity requirements, nearly all of the bills introduced in state legislatures in 2021 have followed that approach – including Connecticut, Hawaii, Massachusetts, Michigan, New Jersey, and Oregon. Illinois and Maryland require only disclosure of boardroom demographics, but do not mandate any level of board diversity. Colorado and Pennsylvania have non-binding diversity requirements, urging companies to act on their own;^[9] Ohio has introduced similar legislation.^[10]

In addition to state legislatures, stock exchanges and large proxy advisory firms have clarified their expectations relating to boardroom diversity. NASDAQ, in conjunction with the Securities and Exchange Commission, has proposed its own standards to encourage greater board diversity and transparency surrounding board diversity. The NASDAQ proposal, citing more than two dozen studies explaining the tangible benefits of diverse boardrooms, would require NASDAQ-listed companies to meet board composition requirements or publicly explain why they have failed to do so. Beginning in the 2021 proxy season, Glass Lewis's company reports will include an assessment of company proxy statement disclosures relating to board diversity. These assessments will help inform its rating of a company's governance. As of January 2021, Institutional Shareholder Services (ISS) began identifying companies in either the Russell 3000 or S&P 1500 that lack board-level ethnic and racial diversity. ISS has publicly stated that beginning in February 2022, it will recommend voting against the reelection of any chair of a nominating committee, or other directors on a case-by-case basis, in situations where there is no diverse member on the board.^[11]

Shareholders also have taken matters into their own hands. Since July 2020, shareholder derivative suits have been filed against at least twelve publicly traded companies alleging lack of board diversity and other sufficient diversity initiatives, seeking a wide range of relief that varies anywhere from replacing current non-diverse directors with diverse directors to the disgorgement of directors' fees to the creation of billion dollar funds to hire minority employees.^[12] In light of this movement to exert pressure on companies to increase board diversity, companies should continue to monitor these developments, particularly by the legislatures of states in which they are incorporated or conduct business.

State	Requirement	Scope of Entities Affected	Status
California ^[13]	Mandatory Diversity	Public companies headquartered in the state (applies to companies domiciled somewhere else with an HQ in the state)	<i>Enacted September 2018 (for women) & September 2020 (for minorities)</i>
Colorado ^[14]	Non-Binding: urging boardroom diversity	Public companies headquartered in the state	<i>Enacted March 2017</i>
Connecticut ^[15]	Considering Mandatory Diversity	Public companies headquartered in the state	<i>Introduced January 2021</i>
Hawaii ^[16]	Considering Mandatory Diversity	Public companies headquartered in the state	<i>Introduced January 2021</i>
Illinois ^[17]	Mandatory Disclosure	Public companies headquartered in the state	<i>Enacted August 2019</i>
Maryland ^[18]	Mandatory Disclosure	Business entities (profit or non-profit) with corporate headquarters in the state	<i>Enacted October 2019</i>
Massachusetts ^[19]	Considering Mandatory Diversity	Public companies headquartered in the state	<i>Introduced January 2019</i>
Michigan ^[20]	Considering Mandatory Diversity	Public companies headquartered in the state	<i>Introduced February 2019</i>
New Jersey ^[21]	Considering Mandatory Diversity	Public companies headquartered in the state	<i>Introduced February 2019</i>
New York ^[22]	Mandatory Disclosure	Public and private for-profit business corporations authorized to do business in the state (not just publicly listed companies)	<i>Enacted March 2019</i>
Ohio ^[23]	Considering Non-Binding: urging boardroom diversity	Public and private companies "doing business" in the state	<i>Introduced September 2019</i>
Oregon ^[24]	Considering Mandatory Diversity	Public companies headquartered in the state	<i>Introduced</i>
Pennsylvania ^[25]	Non-Binding: urging boardroom diversity	Public companies headquartered in the state	<i>Enacted April 2017</i>
Washington ^[26]	Mandatory Diversity	Public companies headquartered in the state	<i>Enacted</i>

ENDNOTES

[1] The Alliance for Board Diversity is a collaboration of four organizations: Catalyst; the Executive Leadership Council; the Hispanic Association on Corporate Responsibility; and Leadership Education for Asian Pacifics. Its mission is to enhance shareholder value in Fortune 500 companies by promoting inclusion of women and minorities on corporate boards.

[2] Deloitte & All. for Bd. Diversity, *Missing Pieces Report: The Board Diversity Census of Women and Minorities on Fortune 500 Boards* (6th ed., June 8, 2021).

[3] The report defines “minorities” as Asian/Pacific Islander, Hispanic/Latino(a) and African American/Black individuals.

[4] N.Y. Bus. Corp. Law § 408.

[5] Cal. Corp. Code § 301.4.

[6] Cal. Corp. Code § 301.3.

[7] SB 826 became Cal. Corp. Code § 301.3 when signed into law in 2018.

[8] *Meland v. WEBER*, No. 20-15762, 2021 WL 2521615 (9th Cir. June 21, 2021).

[9] The proposed legislation in Pennsylvania provides that the House of Representatives encourage equitable and diverse gender representation on corporate boards and urge that by 2021 every publicly held corporation headquartered in the state have a minimum number of women on their board, based on the board’s size.

[10] The proposed legislation in Ohio encourages all private and public companies and institutions doing business in the state to commit to increase the gender diversity on their boards of directors and in senior management positions and to set and publish goals by which to measure progress.

[11] For more on this topic, See Brian V. Breheny et al., Skadden, Arps, Slate, Meagher & Flom LLP, *ISS and Glass Lewis Release Updated Proxy Voting Guidelines* (Dec. 7, 2020), <https://www.skadden.com/insights/publications/2020/12/iss-and-glass-lewis-release>. or more on this topic, See <https://www.skadden.com/insights/publications/2020/12/iss-and-glass-lewis-release>.

[12] For more on this issue, See Jessie K. Liu, Susan L. Saltzstein & Tansy Woan, Skadden, Arps, Slate, Meagher & Flom LLP, *Shareholder Suits Demand More Progress on Diversity* (Apr. 13, 2021), <https://www.skadden.com/insights/publications/2021/04/the-informed-board/shareholder-suits-demand-more-progress>; Raquel Fox, Skadden, Arps, Slate, Meagher & Flom LLP, *The Search for Board Diversity: Practical Tips, Statistics on Progress* (Apr. 13, 2021), <https://www.skadden.com/insights/publications/2021/04/the-informed-board/the-search-for-board-diversity>.

[13] Cal. Corp. Code § 301.3; Cal. Corp. Code § 301.4.

[14] H.R.J. Res. 17-1017, 71st Gen. Assemb., 1st Reg. Sess. (Colo. 2017) (enacted).

[15] H.R. 6211, Gen. Assemb., 2021 Reg. Sess. (Conn. 2021).

[16] S. 193, 31st Leg., Reg. Sess. (Haw. 2021).

[17] H.R. 3394, 101st Gen. Assemb., Reg. Sess. (Ill. 2019) (enacted).

[18] H.D. 1116, 440th Gen. Assemb., Reg. Sess. (Md. 2019) (enacted).

[19] S. 1879, 191st Gen. Ct. (Mass. 2019).

[20] S. 115, 100th Leg., Reg. Sess. (Mich. 2019).

[21] S. 3469, 218th Leg., 2nd Ann. Sess. (N.J. 2019).

[22] N.Y. Bus. Corp. Law § 408.

[23] H.R. Con. Res. 13, 133rd Gen. Assemb., Reg. Sess. (Ohio 2019).

[24] H.R. 3110, 81st Legis. Assemb., Reg. Sess. (Or. 2021).

[25] H.R. 114, Gen. Assemb., 2019 Reg. Sess. (Pa. 2019) (enacted).

[26] Wash. Rev. Code § 23B.08.120.

This post comes to us from Skadden, Arps, Slate, Meagher & Flom LLP. It is based on the firm’s memorandum, “Diversity in the Corporate Boardroom: A Current Scorecard.” Eryn Hughes, a summer associate at the firm, contributed to the memorandum.