

#### **XIV. *Gender Diversity on Corporate Boards of Directors***

##### **A. Introduction**

In September 2018, California became the first state in the union to pass a law, Senate Bill 826 (SB 826), with an explicit gender quota for boards of directors.<sup>1</sup> SB 826 requires both domestic and international corporations with headquarters in California to have at least one female on their board of directors by the end of 2019 and to reach a higher threshold by 2021.<sup>2</sup> A 2014 study on institutional factors impacting gender quotas on boards of directors found that only ten countries had a law that required a certain percentage of female directors with an additional fifteen countries with a “comply or explain” approach to female directors.<sup>3</sup> That same study found women occupied only 10.3% of board directorships in sixty-seven countries, with some of the highest percentages of female directors in countries with a gender quota law.<sup>4</sup>

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<sup>1</sup> Gary Shorter, Corporate Governance: Board Diversity, HEINONLINE (May 21, 2019), <https://heinonline.org/HOL/P?h=hein.crs/govzur0001&i=2> (“On September 30, 2018, then-California Governor Jerry Brown signed SB 826 into law, making the state the first to enact board diversity quotas.”).

<sup>2</sup> S. B. 826, 2018 Assemb. Reg. Sess., § 301.3(b) (Cal. 2018) [hereinafter “S.B. 826”] (“No later than the close of the 2021 calendar year, a publically held domestic or foreign corporation whose principal executive offices, according to the corporation’s SEC 10-K form, are located in California shall comply with the following: (1) If its number of directors is six or more, the corporation shall have a minimum of three female directors. (2) If its number of directors is five, the corporation shall have a minimum of two female directors. (3) If its number of directors is four or fewer, the corporation shall have a minimum of one female director.”).

<sup>3</sup> Siri Terjesen, Ruth V. Aguilera, & Ruth Lorenz, *Legislating a Woman’s Seat on the Board: Institutional Factors Driving Gender Quotas for Boards of Directors*, 50 J. OF BUS. ETHICS 2 (2014), [https://www.researchgate.net/publication/271922150\\_Legislating\\_a\\_Woman’s\\_Seat\\_on\\_the\\_Board\\_Institutional\\_Factors\\_Driving\\_Gender\\_Quotas\\_for\\_Boards\\_of\\_Directors](https://www.researchgate.net/publication/271922150_Legislating_a_Woman’s_Seat_on_the_Board_Institutional_Factors_Driving_Gender_Quotas_for_Boards_of_Directors) (identifying ten countries with laws requiring 33%–50% female representation on a board of directors). The ten countries identified in the study include countries where gender diversity is not required for publicly traded companies but is required for state-owned entities.

<sup>4</sup> *Id.* at 3. Although only Norway had actually met (and exceeded) its quota of female directors, while other countries, such as Iceland and France, are in the top ten countries but had not met their 40% quota.

Traditionally, directors are elected to boards by shareholders.<sup>5</sup> Boards are important in setting the tone at the top; therefore, as fiduciaries of their companies, they are often responsible for the culture and business objectives of their respective companies, as well as supporting their company's senior management.<sup>6</sup> Boards review a variety of critical information about a company, from financial reports to executive compensation packages to choosing their fellow board members.<sup>7</sup> Thus, the composition of the board is often of critical importance to a corporation. Certain shareholders have been more vocal than others in the last ten years about gender diversity on corporate boards in the United States. Some large asset managers (such as BlackRock and State Street) as well as some of the largest pension funds (such as CalPERS and CalSTRS) have put pressure on companies through their proxy voting strategies, frequently withholding votes or voting against companies with no gender diversity on their boards.<sup>8</sup>

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<sup>5</sup> Shorter, *supra* note 1 (“A public company’s board of directors is a group of individuals who have been elected to be the company’s fiduciaries on behalf of its shareholders.”).

<sup>6</sup> *Id.* (“Along with company executives . . . the board helps set the tone for the corporation.”).

<sup>7</sup> *Id.* (“Key board committees include the compensation committee (responsible for setting pay packages for key executives), the nominating and governance committee (responsible for ensuring that there are quality candidates running for the board), and the audit committee (responsible for overseeing financial reporting).”).

<sup>8</sup> *Id.* (“During the last decade or so, large companies have felt increased pressure from pension funds (such as CalPERS and CalSTRS) and large asset managers (such as State Street and Blackrock) to adopt more gender diverse boards.”); Arthur Kohn, Elizabeth Bieber, & Maria Maldonado, *Companies Could Face Pressures Over Board Competition*, LAW360 (Aug. 13, 2018, 3:44 PM), <https://www-law360-com.ezproxy.bu.edu/articles/1069401/companies-could-face-pressure-over-board-composition> (“Over the last few years, boards have come under mounting pressure to focus on board composition and refreshment, including length of tenure, individual and aggregate skills mix and diversity.”); Warren de Wied, Philip Richter, & Gail Weinstein, *The Road Ahead for Shareholder Activism After ‘Record Year,’* LAW360 (Jan. 25, 2019, 4:10 PM), <https://www-law360-com.ezproxy.bu.edu/articles/1122349/the-road-ahead-for-shareholder-activism-after-record-year-> (“Moreover, the pervasiveness of activism has driven critical transformations in the mindset and actions of corporate boards, management teams and institutional investors.”). For instance, BlackRock Inc. requires a minimum of two female directors and may vote against members of the board who do not meet that

California has recently taken a stand in support of greater gender diversity on corporate boards of directors.<sup>9</sup> This article will explore SB 826's beginnings, its European predecessors, studies on the effect of gender diversity on corporate boards, the constitutional challenges this new law faces, and the possible future of the law. SB 826 is just one additional step in a growing trend of encouraging gender diversity.

### **B. Brief History**

In 2013, Senator Hannah-Beth Jackson authored Senate Concurrent Resolution No. 62 (SCR 62), the predecessor to SB 826.<sup>10</sup> SCR 62, similar to SB 826, recommended that companies in California have at least 20–40% female representation on their board of directors by 2016.<sup>11</sup> As an advisory note, it largely failed. By 2016, fewer than 20% of corporations headquartered in California voluntarily complied with SRC 62.<sup>12</sup>

While it may seem that SB 826 is a novel piece of legislation that flows from its 2013 predecessor, the emphasis on diversity—specifically gender diversity—has a much longer history. Sixteen years ago, in 2003, Norway became the first country in the world to mandate a gender quota on boards of directors, requiring a 40% female director representation.<sup>13</sup> Norway's example was later followed by

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criteria. State Street will vote against members of the board if corporations do not have at least one woman. CalSTRS and CalPERS have no specific number requirement but may withhold their votes as well.

<sup>9</sup> See S.B. 826, *supra* note 2.

<sup>10</sup> *Id.* (identifying Senator Hannah-Beth Jackson as author).

<sup>11</sup> *Id.* (“In September 2013, Senate Concurrent Resolution 62 urged that by December 31, 2016, all public companies in California increase the number of women on their boards of directors ranging from one to three, depending upon the size of their boards.”).

<sup>12</sup> CALIFORNIA SENATE RULES COMMITTEE, SB 826: UNFINISHED BUSINESS (2018) (“As of the cut-off date of December 31, 2016, fewer than 20% of the companies headquartered in California had the number of women directors called for in the resolution.”).

<sup>13</sup> Shorter, *supra* note 1 (“A precedent for the practice began in 2003 when Norway first required that its corporate boards be composed of at least 40% female directors”).

other countries in the European Union (EU) such as Spain, Iceland, France, Italy, and Belgium.<sup>14</sup>

In the United States, the push for diversity on boards began as early as 2009, when the Securities and Exchange Commission (SEC) began requiring corporations to disclose “whether, and if so how, the nominating committee (or the board) considers diversity in identifying nominees for director [and] [i]f the nominating committee (or the board) has a policy with regard to the consideration of diversity in identifying director nominees.”<sup>15</sup> However, it seems that this disclosure requirement lacked any teeth in advancing diversity concerns. Multiple reports criticized its utility,<sup>16</sup> and the SEC published revised guidance in 2019, stating that it expected “the company’s discussion required by [the disclosure regulation] would include, but not necessarily be limited to, identifying those characteristics and how they were considered.”<sup>17</sup>

SB 826 has occurred at a time of heightened scrutiny of the lack of corporate diversity and may well engender a shift towards more states adopting a strict gender quota, similar to how Norway kicked off the same movement in the EU.<sup>18</sup>

### C. Relevance to Current Financial Conditions

Part of the supporting argument for passage of SB 826 emphasized statistics and recent studies showing the dearth of women on boards of directors.<sup>19</sup> For example, California “is the 5<sup>th</sup> largest economy in the world” and yet “one-fourth of California’s public companies” do not have a single women director.<sup>20</sup> Senator Jackson emphasized the importance of having female directors by noting that

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<sup>14</sup> Terjesen et al., *supra* note 3 at Table 1. Spain, Iceland, and France have 40% quotas like Norway. Italy and Belgium have 33% quotas.

<sup>15</sup> Shorter, *supra* note 1.

<sup>16</sup> *Id.* (highlighting that SEC officials themselves, the investor community, and a GAO report were unsatisfied because “many firms do not include factors such as gender, race, or ethnicity in how they define diversity.”).

<sup>17</sup> *Id.*

<sup>18</sup> *Id.* (“As of early April 2019, two states, new Jersey and Massachusetts, were reportedly considering bills along the lines of the California statute.”)

<sup>19</sup> Jackson, *supra* note 12, at 3 (“The author notes that, in California, only 15.5% of board seats are held by women, relative to 16.5% of board seats held by women in Russell 3000 companies and 19.8% of board seats held by women in Fortune 1000 firms.”).

<sup>20</sup> *Id.* at 5.

“achiev[ing] gender equity in the workplace . . . need[s] to occur at the top of the corporate structure.”<sup>21</sup> But the need for women on corporate boards is much greater than that. The 2020 Women on Boards, a non-profit organization dedicated to achieving 20% female representation on boards of directors by 2020, states that “[b]oard diversity is not a social issue, it is a strategic imperative.”<sup>22</sup> Gender diversity as a strategic imperative has been the focus of a number of recent studies on financial institutions, which seem to echo its importance to company performance.<sup>23</sup>

In 2012, the Credit Suisse Research Institute published a study examining female leadership and corporate performance.<sup>24</sup> Studying the 2011 MSCI AC World index, the Credit Suisse Research Institute concluded that “in a like-for-like comparison, companies with at least one woman on the board would have outperformed in terms of share price performance, those with no women on the board over the course of the past six years.”<sup>25</sup> This finding is largely consistent with a study examining 612 European banks across twenty EU countries and the gender composition on the banks’ boards of directors.<sup>26</sup> The EU banks

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<sup>21</sup> S. HANNAH-BETH JACKSON, CORPORATIONS: BOARDS OF DIRECTORS, S. Jud. Comm. Reg Sess. 3 (Cal. 2017–2018).

<sup>22</sup> Betsy Berkhemer-Credaire & Stephanie Sonnabend, 2020 WOMEN ON BOARDS GENDER DIVERSITY INDEX, 2020wob.com/sites/default/files/2020\_WOB\_GDI\_Report\_2018\_FINAL.pdf (last visited Oct. 28, 2019).

<sup>23</sup> See Mary Curtis, Christine Schmid & Marion Struber, *Gender Diversity and Corporate Performance*, CREDIT SUISSE RESEARCH INSTITUTE (Aug. 2012), [https://www.calstrs.com/sites/main/files/file-attachments/csri\\_gender\\_diversity\\_and\\_corporate\\_performance.pdf](https://www.calstrs.com/sites/main/files/file-attachments/csri_gender_diversity_and_corporate_performance.pdf); Ruth Mateos de Cabo, Ricardo Gimeno & Maria J. Nieto, *Gender Diversity on European Banks’ Boards of Directors*, 109 J. OF BUS. ETHICS 145, 147 (2012) (“Existing studies on ethical aspects argue that this underrepresentation of certain groups raises ethical considerations that derive from an imperative to enfranchise those constituencies historically excluded from positions of economic power.”); Ann L. Owen & Judit Temesvary, *Gender Diversity on Bank Board of Directors and Performance*, FEDS NOTES (Feb. 12, 2019), <https://www.federalreserve.gov/econres/notes/feds-notes/gender-diversity-on-bank-board-of-directors-and-performance-20190212.htm> (“Overall, we find that banks with more gender diversity on their board perform better once the composition of these boards reaches a critical level of gender diversity, corresponding to a board female share of around 1317 percent.”).

<sup>24</sup> See Curtis, *supra* note 23.

<sup>25</sup> *Id.* at 6, 12 (finding a 26% outperformance of all companies over 6 years).

<sup>26</sup> Cabo, *supra* note 23, at 1 (hypothesizing that growth-oriented banks are more likely to have women on their boards).

study also supports the notion that placing women on boards of directors is a strategic imperative.<sup>27</sup> One of its conclusions is that “banks that have a growth orientation are more prone to include women on their board, since they may be seen as providers of diverse external resources.”<sup>28</sup> Additionally, previous studies on women in management found women on boards “improve the board’s monitoring role in protecting shareholder interests by better top management control.”<sup>29</sup> Thus, the inclusion of female board members may not be solely an issue of business ethics but also a strategic benefit to banks focused on growth.

However, the Federal Reserve Bank (the “Fed”) recently published a study looking at ninety U.S. banks’ performance and gender diversity on their boards that runs slightly counter to the EU banks’ study.<sup>30</sup> The Fed recognized a lack of studies on gender diversity on boards of directors and its effect on the banking industry.<sup>31</sup> Quoting a study from 2015, the Fed’s study notes that while women are more than 50% of the workforce in S&P 500 finance companies, they represent only 18.7% of those same company boards, and only 2.1% of the CEOs were women.<sup>32</sup> Even though certain empirical results from this study suggest that gender diversity on a board of directors negatively affects a bank’s performance, the Fed’s ultimate conclusion was that a strategic benefit of more women on boards depends largely on the existing traits and characteristics of the bank.<sup>33</sup>

SB 826 requires, at a minimum, one female board member by the end of 2019.<sup>34</sup> Interestingly, the Fed study found that for the ninety

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<sup>27</sup> *Id.* at 3 (“Existing studies on ethical aspects argue that this underrepresentation of certain groups raises ethical considerations that derive from an imperative to enfranchise those constituencies historically excluded from positions of economic power.”).

<sup>28</sup> *Id.*

<sup>29</sup> *Id.* at 3 (“This is because women have higher expectations regarding their responsibilities as directors . . .”).

<sup>30</sup> See Owen & Temesvary, *supra* note 23.

<sup>31</sup> Owen, *supra* note 23 (“Many papers have studied the effects of boards’ gender composition on firm performance and a few have studied it in the banking industry specifically, showing mixed results.”).

<sup>32</sup> *Id.* (“While women made up 54.3 percent of the workforce at S&P 500 finance companies in 2014, only 18.7 percent of S&P 500 finance company boards and only 2.1 percent of CEOs were women.”).

<sup>33</sup> *Id.* (“[W]e propose the resolution to these conflicting findings is that the impact of greater gender diversity depends on bank and board traits.”).

<sup>34</sup> See S.B. 826, *supra* note 2.

banks it surveyed, adding the first female to a board of directors does not affect performance.<sup>35</sup> In fact, if the bank is considered “well-capitalized” with a “very low level of board gender diversity,” then the addition of a female to its board “has a negative effect on performance.”<sup>36</sup> This negative effect only disappears once there is a significant increase in gender diversity, implying that there may be a diversity threshold before seeing performance benefits.<sup>37</sup> This suggests that the short-term effects of SB 826 may not be readily apparent, but that its 2021 requirement of gender parity on boards may result in better performance, at least for well-capitalized banks.

While studies on financial institutions may show varying benefits to a bank’s financial performance, studies cited in support of SB 826 purposefully excluded financial institutions “because they are subject to specific regulations and [have] fundamentally different investment approaches than nonfinancial institutions.”<sup>38</sup> Looking broadly at publicly-traded, non-financial companies in the United States, a study examining corporate risk taking given a corporation’s board diversity found that diverse boards “are more effective in monitoring corporate investment activities than homogenous boards.”<sup>39</sup> Additionally, other studies show that gender diversity specifically is associated with “better earnings quality,” “lower likelihood of financial restatement,” and “less aggressive acquisition strategies.”<sup>40</sup> This may be particularly relevant to California itself given that 761 publicly-traded companies are headquartered there, and the percentage of female directors on those company boards lags behind the national average.<sup>41</sup> For instance, in Fortune 1000 firms, women hold 19.8% of

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<sup>35</sup> *Id.* (“Given the size and composition of most boards, this result essentially means that adding more women to the board improves overall performance if there is already at least one woman on the board; adding the first woman to the board does not have this positive effect.”).

<sup>36</sup> *Id.*

<sup>37</sup> *Id.* (“Consistently, we find some evidence suggesting that increasing gender diversity beyond a threshold is associated with fewer regulatory enforcement actions.”).

<sup>38</sup> Maretto A. Harjoto, Indrarini Laksmana & Ya-wen Yang, *Board Diversity and Corporate Risk Taking* (Jan. 24, 2018), <https://ssrn.com/abstract=2412634>.

<sup>39</sup> *Id.* at 5.

<sup>40</sup> *Id.*

<sup>41</sup> Jackson, *supra* note 21, at 3 (“There are currently 761 publicly traded companies headquartered in California, including 510 traded on NASDAQ, 216 traded on the NYSE, and 35 on AMEX . . . Further, California’s public

the seats on boards; in Russell 3000 companies, that percentage is 16.5%; and in California, women hold only 15.5% of corporate board seats.<sup>42</sup> SB 826 may thus be relevant in addressing the disparity between California-headquartered corporations and other large corporations.

#### **D. Current Status of SB 826 and Regulations Affecting It**

On July 1, 2019, California's Secretary of State, Alex Padilla published an update on the status of corporations and their compliance with SB 826.<sup>43</sup> The report identified 537 publicly-held corporations whose primary place of business is in California.<sup>44</sup> Most notably missing from this list is Apple, although other corporate giants are included and non-compliant (such as Google, Facebook, Tesla, Netflix, and PayPal).<sup>45</sup> Several attorneys have criticized the lack of meaningful information due to a dataset that is riddled with errors.<sup>46</sup> The next

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corporations have fewer female directors than public corporations elsewhere in the United States.”).

<sup>42</sup> *Id.* (“The author notes that, in California, only 15.5% of board seats are held by women, relative to 16.5% of board seats held by women in Russell 3000 companies and 19.8% of board seats held by women in Fortune 1000 firms.”).

<sup>43</sup> Alex Padilla, *Women on Boards*, CA SEC’Y OF STATE, <https://www.sos.ca.gov/business-programs/women-boards/> [<https://perma.cc/K2UX-VC8Y>] (last visited Oct. 28, 2019) (“In 2018, Women on Boards (Senate Bill 826) was signed into law to advance equitable gender representation on California corporate boards.”).

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

<sup>46</sup> Cydney Posner, *California Secretary of State Publishes “Report” about SB 826, California’s New Board Gender Diversity Mandate*, COOLEY PUBCO (Jul. 11, 2019), <https://cooleypubco.com/2019/07/11/california-publishes-report-sb-826-updated/> (explaining the inaccuracies are largely from unreliable data sources, such as 10-Ks and form SI-PT which is the “California Statement” that public corporations must file annually in California); Keith Bishop, *Why The Mandated Report On Female Directors Fails To Provide Meaningful Information*, CAL. CORP. & SEC. LAW (July 3, 2019), <https://www.calcorporatelaw.com/why-the-mandated-report-on-female-directors-fails-to-provide-meaningful-information> (observing a lack of information about whether or not any corporations are actually in violation of the new law).



update is due in March 2020.<sup>47</sup> However it is unclear whether courts will uphold the new law given some of the challenges in enforcing SB 826. Early opponents and the Senate analysis of the bill itself highlighted potential conflicts with the Equal Protection Clause of the Fourteenth Amendment and the internal affairs doctrine.<sup>48</sup> California Governor Jerry Brown himself mentioned that there may be flaws “fatal to its ultimate implementation.”<sup>49</sup> Possible constitutional challenges would revolve around whether or not SB 826 would be able to withstand strict scrutiny.<sup>50</sup> Based on prior rulings in the state of California on constitutionality matters, gender is a “suspect classification subject to strict scrutiny review . . . [and] will be upheld as constitutional only if it furthers a compelling state interest through the least restrictive means available.”<sup>51</sup> Professor Joseph A. Grundfest of Stanford University Law School’s Rock Center of Corporate Governance published a working paper before passage of the bill in which he pushed for an alternative to a mandatory gender quota given the hurdles in showing specific discriminatory behavior in California against women.<sup>52</sup> Professor Grundfest also emphasizes that the internal affairs doctrine narrows SB 826’s scope, applying only to corporations

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<sup>47</sup> Posner, *supra* note 46 (“An updated report will be published on March 1, 2020.”).

<sup>48</sup> Jackson, *supra* note 12, at 5 (“California court rulings on the constitutionality of laws that require differential treatment based on gender have identified gender as a suspect classification subject to strict scrutiny review.”).

<sup>49</sup> Dave Simpson, Calif. Board Diversity Law Is Illegal, Conservative Group Says, LAW360 (Aug. 9, 2019, 6:52 PM), <https://www-law360-com.ezproxy.bu.edu/articles/1186831/calif-board-diversity-law-is-illegal-conservative-group-says> ([I]n signing the bill, Brown wrote that ‘serious legal concerns have been raised’ about the legislation. ‘I don’t minimize the potential flaws that indeed may prove fatal to its ultimate implementation.’”).

<sup>50</sup> Jackson, *supra* note 12, at 5 (“California court rulings on the constitutionality of laws that require differential treatment based on gender have identified gender as a suspect classification subject to strict scrutiny review.”).

<sup>51</sup> *Id.*

<sup>52</sup> Joseph A. Grundfest, *Mandating Gender Diversity in the Corporate Boardroom: The Inevitable Failure of California’s SB 826* (Stanford Law School and the Rock Center for Corp. Governance, Working Paper No. 232, 2018) (“California can use its significant capital market influence to induce major institutional investors to mount more aggressive activist campaigns that can rapidly and materially increase boardroom diversity.”).

that are both incorporated and headquartered within the state of California rather than only headquartered.<sup>53</sup>

However, California's long-arm statute codified in California Corporations Code Section 2115 may successfully counter the internal affairs doctrine.<sup>54</sup> Conflicts between the laws of the state of incorporation and California law are not unfamiliar to California.<sup>55</sup> In fact, Section 2115 explicitly states that some of its provisions apply to corporations "to the exclusion of the law of the jurisdiction in which the foreign corporation is incorporated."<sup>56</sup> Courts have ruled both against the application of California law and for it,<sup>57</sup> and it is not quite clear cut whether a court would rule in favor of upholding SB 826 or not. In a recent case, *Boschetti v. Pacific Bay Investments Inc.*,<sup>58</sup> the Court re-iterates the presence of a narrow exception to the internal affairs doctrine which was elucidated in *Lidow v. Superior Court*: a "vital statewide interest."<sup>59</sup> *Boschetti* ruled in favor of the laws of the states of incorporation because the issue at hand involved preventing the dissolution of out-of-state incorporated limited liability companies and limited partnerships, and dissolution is a "quintessential internal

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<sup>53</sup> *Id.* at 2 ("Considering the 117 corporations in the Russell 3000 that are headquartered in California and that have no women directors, the internal affairs doctrine would cause SB 826 to likely apply to only about 12 of those corporations.").

<sup>54</sup> Jackson, *supra* note 21 ("Although the US Supreme Court has taken a broad view of the internal affairs doctrine, stating that only one State should have the authority to regulate a corporation's internal affairs because otherwise a corporation could be faced with conflicting demands, California Corporations Code Section 2115 applies a full laundry list of California statutes to out-of-state corporations, notwithstanding the law applicable within their state of incorporation. In other words, the internal affairs doctrine does not overrule applicability of Section 2115 to out-of-state corporations.").

<sup>55</sup> PRACTICAL LAW CORPORATE & SECURITIES, SECTION 2115: CALIFORNIA'S CORPORATE LONG-ARM STATUTE (2019), Westlaw Practical Law ("A coalition of businesses represented by the California Chamber of Commerce has opposed the law based on possible violations of the US Constitution, California Constitution, California's civil rights law, and the 'internal affairs' doctrine.").

<sup>56</sup> Cal. Corp. Code § 2115(b).

<sup>57</sup> Westlaw Practical Law, *supra* note 55.

<sup>58</sup> 244 Cal. Rptr. 3d 480 (2019).

<sup>59</sup> *Id.* at 487 (2019) (quoting *Lidow v. Superior Court*, 141 Cal. Rptr. 3d 729, 736 (2012)) ("[C]ourts are less apt to apply the internal affairs doctrine when vital statewide interests are at stake.").

governance issue” rather than a material state interest.<sup>60</sup> Here, the appointment of a member of the board of directors may be a vital internal governance issue, but it may also be an issue that is vital to California’s interests. After all, courts do not “blindly apply” the internal affairs doctrine and prefer to examine the particular facts of each case before deciding whether the laws of the state of incorporation apply over California’s laws.<sup>61</sup> There is no clear answer to whether SB 826 can withstand an internal affairs challenge.

Two recent lawsuits against Secretary Padilla further emphasizes the uneven footing of SB 826.<sup>62</sup> The first lawsuit concerns Robin Crest and others—represented by the conservative legal group Judicial Watch—who allege that enforcing SB 826 violates California’s constitution because its express gender classification does not meet strict scrutiny, and therefore any taxpayers’ money used to enforce SB 826 is an illegal use of taxpayers’ money.<sup>63</sup> The second lawsuit concerns Creighton Meland—represented by libertarian legal group Pacific Legal Foundation—who alleges that enforcing SB 826 violates the Equal Protection Clause of the Fourteenth Amendment.<sup>64</sup> Meland is a

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<sup>60</sup> *Id.* at 486 (quoting *Colaco v. Cavotec SA*, 236 Cal. Rptr. 3d 542, 562 (2018)).

<sup>61</sup> *Colaco v. Cavotec SA*, 236 Cal. Rptr. 3d 542, 559 (2018) (upholding trial court’s application of California state law over Delaware law because plaintiff failed to show that Delaware had a substantial material interest over California).

<sup>62</sup> Simpson, *supra* note 49 (“The complaint, filed on behalf of three California taxpayers Tuesday, argues that SB 826, which was signed by former Gov. Jerry Brown in September, will require the state to spend hundreds of thousands of dollars to enforce, and that such expenditures render it illegal under the state constitution.”); Associated Press, *California Sued Again for Requiring Women on Corporate Boards*, L.A. TIMES (Nov. 13, 2019 1:25 PM) <https://www.latimes.com/business/story/2019-11-13/california-sued-for-requiring-women-corporate-boards> (“The Pacific Legal Foundation provided the Associated Press with the lawsuit it filed in federal court Wednesday, arguing that the law violates the equal protection clause of the U.S. Constitution.”).

<sup>63</sup> Complaint for Declaratory and Injunctive Relief at 19, *Crest et al. v. Padilla*, No. 19STCV27561 (Cal. Super. Ct. 2019), <https://www.judicialwatch.org/wp-content/uploads/2019/08/Crest-et-al-v-Padilla-Women-on-Boards-complaint-27561> [<https://perma.cc/LQZ3-AKWA>] (“Specifically, Plaintiffs contend that any expenditure of taxpayer funds or taxpayer-financed resources on SB 826 is illegal under the California Constitution.”).

<sup>64</sup> Complaint for Declaratory and Injunctive Relief at 31, *Meland, Jr. vs. Padilla*, 2:19CV02288 (E.D. Cal. 2019), <https://pacificlegal.org/wp-content/>

shareholder of a company headquartered in California which currently has an all-male board of directors,<sup>65</sup> and the complaint contends that SB 826's gender quota is not "an important government interest" and that the law is "not closely tailored to that interest" to survive an Equal Protection Clause challenge.<sup>66</sup> *Crest v. Padilla* has no current hearing dates with latest movement being a Notice of Continuance filed by the plaintiffs in response to the state's demurrer.<sup>67</sup> *Meland v. Padilla* has a Motion to Dismiss hearing set for March 24, 2020.<sup>68</sup> The existence of SB 826 may very well be threatened.

### E. General Trends and Expected Future Developments

In order to meet the 2021 mandate of SB 826, corporations in California will need to act fast. Board Governance Research LLC's CEO, Annalisa Barrett, has conducted extensive research on female statistics on corporate boards of directors in California.<sup>69</sup> At the time of the report published in 2018, Ms. Barrett estimated 1,060 board seats must be filled by women by 2021.<sup>70</sup> In other words, 177 companies must add one woman, 254 companies must add two women, and 125

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uploads/2019/11/Creighton-Meland-v.-Alex-Padilla-Secretary-of-State-of-California-Complaint.pdf\_ [https://perma.cc/4K7C-8CJU] ("Plaintiff contends that the Woman Quota is a sex-based classification that violates the Fourteenth Amendment to the United States Constitution. Defendant disputes that the quota, or that enforcing the quota, is unconstitutional.").

<sup>65</sup> *Id.* at 4, 17, & 21. ("[Meland, Jr.] is a shareholder of OSI, System, Inc. . . . [which] is headquartered in Hawthorne, California. . . . OSI currently has an all-male board.").

<sup>66</sup> *Id.* at 36 & 39.

<sup>67</sup> *Robin Crest et al. vs. Alex Padilla*, DOCKET ALARM, [https://www.docketalarm.com/cases/California\\_State\\_Los\\_Angeles\\_County\\_Superior\\_Court/19S\\_TCV27561/ROBIN\\_CREST\\_ET\\_AL\\_VS\\_ALEX\\_PADILLA/](https://www.docketalarm.com/cases/California_State_Los_Angeles_County_Superior_Court/19S_TCV27561/ROBIN_CREST_ET_AL_VS_ALEX_PADILLA/) [https://perma.cc/GQ4U-QKRM] (last visited Jan. 13, 2020).

<sup>68</sup> *Meland v. Padilla*, PACERMONITOR, [https://www.pacermonitor.com/public/case/30951577/Meland\\_v\\_Padilla](https://www.pacermonitor.com/public/case/30951577/Meland_v_Padilla) (last visited Jan. 13, 2020).

<sup>69</sup> Annalisa Barrett, *Women of Boards of Public Companies Headquartered in California 2018 Report*, BOARD GOVERNANCE RES. 13 (2018), <https://static1.squarespace.com/static/56e8489162cd944a6424f542/t/5c71e90c652dea4b797a5b14/1550969114360/2018+WOB+Final+Hi+Res.pdf> ("Ms. Barrett served as the subject matter expert for the sponsors and authors of California Senate Bill 826").

<sup>70</sup> *Id.* at 4.

companies must add three women by December 31, 2021, in order to comply with SB 826.<sup>71</sup> With so many vacant seats to fill, it is no surprise that one of the main concerns related to the future of SB 826 is whether corporations will be able to have a pool of qualified women from which they could choose in order to fill seats on boards of directors.<sup>72</sup> However, this does not seem likely to develop into a large issue, especially considering the availability and network of existing organizations such as Women Corporate Directors, 2020 Women on Boards, and DirectWomen.<sup>73</sup> In the event that SB 826 is struck down, Professor Grundfest identified shareholder activism as a more viable solution to tackling diversity.<sup>74</sup> Indeed, many institutional investors, as mentioned earlier, have already taken a strong stand in their voting guidelines against companies who do not make progress in terms of diversity on their boards of directors.<sup>75</sup>

Despite the current legal challenge against SB 826, there does seem to be increasing emphasis on gender diversity. A partner at Sullivan & Cromwell LLP wrote an advisory draft to boards of directors and/or senior management of public companies.<sup>76</sup> The drafted memorandum is not limited to corporations in California.<sup>77</sup> Rather, it is

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<sup>71</sup> *Id.*

<sup>72</sup> Jackson, *supra* note 12, at 3 (“Furthermore, are we confident that corporations will be able to identify a sufficient pool of qualified female directors to comply with the provisions of this bill?”).

<sup>73</sup> Trevor Norwitz, Sabastian V. Niles & Jenny Lin, *Corporate Board Diversity Requirements Expand: Guidance for Corporations*, LEXIS PRACTICE ADVISOR (last visited Sept. 1, 2019), <https://www.lexisnexis.com/lexis-practice-advisor/the-journal/b/lpa/posts/corporate-board-diversity-requirements-expand-guidance-for-corporations> (identifying key organizations with access to large, female talent pools that can be tapped to fill board seats).

<sup>74</sup> Grundfest, *supra* note 52, at 8 (“Similar, if not superior, results can be obtained through shareholder activism designed to increase boardroom diversity.”).

<sup>75</sup> de Wied, *supra* note 8 (“Also of note, institutional investors BlackRock, State Street, CalPERS and CalSTERS all have added board diversity to their voting policies (and California has adopted a first-of-its-kind law requiring a minimum number of female directors on the boards of corporations incorporated or headquartered in the state).”).

<sup>76</sup> Frank J. Aquila, Memorandum to Board: Gender Diversity in the Boardroom, WESTLAW PRAC. LAW CORP. & SEC., <https://us.practicallaw.thomson-reuters.com/w-020-5531?view=hidealldraftingnotes> (last visited Oct. 28, 2019).

<sup>77</sup> *Id.*

meant as guidance to inform which current trends should “guide the Board’s discussions when considering gender diversity in the boardroom.”<sup>78</sup> The memorandum urges boards to monitor legislative development both in the corporation’s state of incorporation and the “main jurisdictions in which the Company operates” as it notes that there may be increased legislative efforts to promote gender diversity in our current “electrifying political environment of the upcoming presidential elections.”<sup>79</sup> Previously, only Colorado, Illinois, Massachusetts, and Pennsylvania had voluntary thresholds of gender diversity on corporate boards.<sup>80</sup> However, following in the footsteps of SB 826, Illinois,<sup>81</sup> Maryland,<sup>82</sup> and New York<sup>83</sup> have recently enacted similar legislation. Additionally, efforts to increase gender diversity are also currently underway through pending quota legislation in Massachusetts,<sup>84</sup> Michigan,<sup>85</sup> New Jersey,<sup>86</sup> Pennsylvania,<sup>87</sup> and Washington.<sup>88</sup>

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<sup>78</sup> *Id.* at 2.

<sup>79</sup> *Id.* at 8.

<sup>80</sup> *Id.* (“Colorado, Illinois, Massachusetts, and Pennsylvania, have passed non-binding resolutions to encourage companies doing business in their states to increase board gender diversity.”).

<sup>81</sup> H.B. 3394, 101st Gen. Assemb., Reg. Sess. (Ill. 2019), Pub. Act 101-0589. Earlier versions of H.B. 3394 had mandatory diversity quotas, however the final bill signed by the Governor focuses more on reporting requirements for corporations with principal executive offices located in Illinois.

<sup>82</sup> H.B. 1116, 2019 Leg., Reg. Sess. (Md. 2019); S.B. 0911, 2019 Leg., Reg. Sess. (Md. 2019). Similar to Illinois, these concurrent bills focus on reporting requirements by “requiring a certain entity submitting an annual report . . . to include information relating to the number of female members of the board.”

<sup>83</sup> S.B. S04278, 2019 Assemb., Reg. Sess. 2019-2020 (N.Y. 2019). A little different from other bills, S04278 requires New York’s state department to conduct a study on women on corporate boards for corporations “authorized to do business in New York state.”

<sup>84</sup> S.B. 1879, 191st Gen. Court, Current Sess., § 57(b) (Mass. 2019) (introducing a specific quota for close of 2023 of “(1) If its number of directors is 6 or more, the corporation shall have a minimum of 3 female directors. (2) If its number of directors is 5 or fewer, the corporation shall have a minimum of 2 female directors.”).

<sup>85</sup> S.B. 0115, 2019 Leg., Reg. Sess., § 505(a)(2) (Mich. 2019) (introducing a specific quota beginning January 1, 2023 of “(a) If its number of directors is 6 or more, the corporation must have at least 3 female directors. (b) If its number of directors is 5, the corporation must have at least 2 female directors. (c) If its number of directors is 4 or fewer, the corporation must have at least 1 female director.”).

Should SB 826 withstand its challenges, California, in particular, seems to be the best candidate for such a rule. California is home to 15% of the companies on the Russell 3000 Index, and progress in that state alone could be significant in leveling gender parity on boards.<sup>89</sup>

## F. Conclusion

Despite the passing of the December 31, 2019 deadline for corporations headquartered in California to have at least one female on their board of directors, the future of the law is as unclear as it was when Governor Brown signed it. Even if empirical studies have not jointly reached a definitive conclusion that gender diversity on boards of directors positively affects corporate performance, they have all recognized the importance of gender diversity in our current society. Reaching a more gender-balanced corporate board may satisfy both a strategic imperative for companies as well as a social imperative. U.S. financial institutions should still strongly consider adding more females to their board ranks.

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<sup>86</sup> S.B. 3469, 218th Leg., Reg. Sess. 2018–2019 (N.J. 2018) (introducing a specific quota for close of 2021 of “(1) a corporation with six or more directors shall have a minimum of three female directors; (2) a corporation with five directors shall have a minimum of two female directors; or (3) a corporation with four or fewer directors shall have a minimum of one female director.”).

<sup>87</sup> H. Res. 114, 2019 Leg., Reg. Sess. 2019–2020 (Pa. 2019) (encouraging “equitable and diverse gender representation on corporate boards and urge that by 2021 every publicly held corporation in this Commonwealth with nine or more director seats have a minimum of three women on its board, every publicly held corporation with five to eight director seats have a minimum of two women on its board and every publicly held corporation with fewer than five director seats have at least one woman on its board”).

<sup>88</sup> S.B. 5142, 2019 Leg., Reg. Session (Wash. 2019) (requiring corporations to have at least one female director by close of 2020).

<sup>89</sup> Jackson, *supra* note 12, at 3 (“There are currently 761 publicly traded companies headquartered in California, including 510 traded on NASDAQ, 216 traded on the NYSE, and 35 on AMEX.”).

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