



## **CALIFORNIA'S NEW GENDER MANDATE FOR CORPORATE BOARDS**

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Publicly held corporations that are headquartered in California should take note of a new law imposing gender representation requirements on corporate boards. Under SB 826, which was signed into law in 2018 and is among several bills reflective of the #MeToo movement, any publicly held corporation whose principal executive offices are located in California is required to have at least one female on its board of directors by the end of 2019. By the close of calendar year 2021, the law increases the required minimum number of female directors to two if the corporation has five directors, and three female directors if the corporation has six or more directors. The law, which adds section 301.3 to the Corporations Code, defines a publicly held corporation as one with outstanding shares listed on a major United States stock exchange. The gender diversity requirement applies to any public company that is headquartered in California,

regardless of the state in which it was incorporated. Whether a company's executive offices are in California would be determined by its SEC 10-K form.

The law expressly authorizes the Secretary of State to impose significant monetary fines for violations. A corporation would be subject to a fine of at least \$100,000 for every director's seat that was not held by a female director during at least a portion of the calendar year. Companies that fail to file board member information in a timely manner with the Secretary of State also would be subject to a \$100,000 fine. The Secretary of State is also required to publish overtime statistics on its website regarding corporate compliance with the new law, including publishing the number of corporations that complied with the law during at least one point during the preceding calendar year.

California is the first state to pass such a requirement. In a press release by one of the bill's authors that accompanied its passage, Senator Hannah Beth Jackson (D-Santa Barbara) noted that gender diversity on corporate boards is associated with increased profitability, performance, governance, innovation and opportunity. Numerous studies have concluded that publicly held companies that have female board directors perform better on a number of metrics, such as average return on equity and price-to-book value. Despite these advantages, however, as of June 2017, among the 446 publicly traded companies included in the Russell 3000 index and headquartered in California, female directors held only 15.5 percent of board seats. The Legislature also noted in passing the law that 26 percent of the Russell 3000 companies based in California had no women directors serving on their boards, and that smaller companies in the State were much more likely to lack female directors. Those facts stand in stark contrast to a number of European countries, such as Germany and Norway, that have mandated gender diversity on corporate boards.

When signing the bill into law, Governor Jerry Brown expressly noted that there had been "numerous objections to this bill" and that "serious legal concerns" had been raised. Opponents contend that the law violates the California Constitution and equal protection clause of the United States Constitution, which subject laws involving gender classifications to heightened levels of judicial scrutiny. Another potential issue is whether the law violates the internal affairs doctrine, by requiring corporations that are headquartered in California, but that are incorporated elsewhere, to abide by these requirements.

Despite these potential difficulties, Governor Brown still signed the law because, as he stated in a letter accompanying its signing, “it’s high time corporate boards include the people who constitute more than half the ‘persons’ in America.” Investors, stakeholders and members of the public have similarly demanded the inclusion of more women on corporate boards.

Public companies in California should consider taking immediate steps to ensure that they comply with the requirements imposed by SB 826, including ensuring that they have the minimum number of female directors by December 31, 2019, and leaving themselves sufficient time to obtain the requisite board approvals and votes. Companies will also need to continue to spend time and effort toward board development, including keeping an eye on potential candidates who may be needed in the future to maintain the requisite board composition, particularly since temporary periods of noncompliance can result in significant penalties under the new law.

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