U.S. State and Federal Initiatives to Increase Diversity on Corporate Boards

By Annalisa Barrett
Clinical Professor of Finance, University of San Diego
CEO & Founder, Board Governance Research
Senior Advisor, ValueEdge Advisors

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Introduction

Numerous studies have found that diversity among the members of the board of directors of publicly-traded companies can lead to improved corporate performance. For this reason, investors across the U.S. have been calling on companies to improve the diversity of their corporation boards. Similarly, elected officials at both the state and federal level have taken action to address the issue. While many are hesitant to put rules in place which prevent company leaders from deciding how to best address the issue, others feel that a "quota" approach to board diversity is the best way to effect change. This article summarizes the approaches currently being taken at the state and federal level to address board diversity.

State Initiatives

California Takes the Lead

California was the first state to pass a resolution calling on boards of publicly-traded companies based in the state to increase the level of gender diversity among the members of their boards of directors by passing Senate Concurrent Resolution No. 62 in 2013. The non-binding resolution encouraged companies based in California to have a specified number of female directors—from one to three women directors—depending on the size of the board, within the following three years. Although the resolution was not binding, it achieved at least three goals: 1) encouraging discussion regarding board diversity among corporate directors and other leaders; 2) supporting institutional investors' initiatives targeting companies lacking board diversity; and 3) setting an example for other state legislatures to call on companies based in their states to improve board diversity.

As of December 31, 2016, which was the end of the three-year time frame specified in the first California resolution, approximately 20% of the companies included in the Russell 3000 Index and headquartered in California were in compliance with the targeted number of female directors. Despite the continued low numbers of female directors serving on California company boards, the supporters of the resolution feel that it partially served its purpose in that it raised awareness regarding the need for improved gender diversity on the boards of companies based in the state.

Other States Take Action

This notion is bolstered by the fact that several other states around the country have followed California's lead and passed non-binding resolutions calling on companies in their states to improve gender diversity on the boards of companies based in their states. The following states are among those that have taken legislative action:

- In Illinois, HR0439 was adopted in May 2015; more information can be found here.

- In Massachusetts, Resolution S.1007 was adopted in October 2015; more information can be found here.

- In Colorado, House Joint Resolution 17-1017 was passed in March 2017; more information can be found here.

- In Pennsylvania House Resolution 273 was adopted in April 2017; more information can be found here.

Federal Initiatives

Studies and Legislation

A report by the U.S. Government Accountability Office published in December 2015, found that, assuming women join boards in equal proportion to men, this number will likely not reach 50 percent – gender parity – before the year 2054. In 2016, a bill called "Gender Diversity in Corporate Leadership Act of 2016" was introduced in the House of Representatives called on the Securities Exchange Commission (SEC) to, among other things, "establish a Gender Diversity Advisory Group to study and make recommendations on strategies to increase gender diversity among the members of the board of directors of issuers." This bill was re-introduced as H.R. 1611 in March 2017.

Federal Rules regarding Corporate Disclosure

While some efforts to encourage companies to increase diversity among corporate directors are underway, others are focused on improving the disclosure regarding the current level of board diversity. Historically, those advocating change have had success by requesting enhanced disclosure to push companies to take action. This is likely due to the notion that, as Justice Louis D. Brandies once said, "sunshine is the best disinfectant." Also, when companies have to provide information in their regulatory filings regarding an issue, it often necessitates a review of the company's practices prior to documenting that practice to share with the investing public.

Currently, companies are required to provide a short biography of their current and nominated directors in their proxy statements, which are filed with the SEC and therefore available to the public at www.sec.gov. However, these biographies most often do not include much information regarding aspects of diversity each director brings to the board. Of course, titles and pronouns allow an external observer to determine the gender of the director and director ages are provided, but information regarding the ethnic and racial background is not discernable. Likewise, membership in other groups which might provide diverse perspectives in boardroom deliberations are often not discernable from the information currently provided.

Most recently, a group of 29 members of the U.S. House of Representatives, led by Congressman Gregory W. Meeks, a senior member of the House Financial Services Committee, signed a letter to the new Chair of the SEC, Jay Clayton, requesting that the commission require enhanced disclosure regarding board diversity from the companies which are required to file with the SEC. This letter requests that companies be required to provide details regarding the "race, gender, and ethnicity of each board member/nominee." The previous SEC Chair, Mary Jo White, had indicated more than once that she was interested in pursuing such enhancements to the required disclosures. In a speech in June 2016, she said that her staff would be proposing rule changes to require companies "to include in their proxy statements more meaningful board diversity disclosures on their board members and nominees where that information is voluntarily self-reported by directors." However, Chair White stepped down before this proposal moved forward. The letter from the Representatives indicates that there is support among current federal legislators to call on the current SEC Chair to move forward on this issue.

Conclusion

Taken together, the federal and state initiatives addressing diversity on corporate boards should serve as a strong signal that institutional investors are not alone in their desires for more diversity in corporate boardrooms. Directors and other company leaders should take notice and act preemptively to improve the diversity of their boards and discuss this diversity in their regulatory filing.