Benchmarking California Board Diversity: Even if California's Law is Blocked, Gender Diversity Initiatives from Stockholders Will Impact Public Companies Across the United States

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STATUS UPDATE ON CALIFORNIA'S BOARD GENDER DIVERSITY MANDATE

On August 6, a group of three individual plaintiffs represented by Judicial Watch, Inc. filed suit in Los Angeles County Superior Court against California's Secretary of State seeking to block the provisions of SB 826, which was signed into law in September 2018 and provides that:

- By December 31, 2019, every publicly traded company on a major securities exchange (e.g. Nasdaq, NYSE) with its headquarters in California is required to have at least 1 female board director; and
- By December 31, 2021, a public company board with 5 board members will need at least 2 female members, and those boards with 6 or more members will need at least 3 female members.

As the Judicial Watch lawsuit notes, at the time of the law's enactment in September 2018, many commentators questioned its constitutionality and enforceability, irrespective of its public policy goal.

However, whether or not California's law stands, it likely only raises a question as to legally mandated timing to increase gender diversity on boards. But an equally important mandate for increased gender diversity is emerging through "private ordering" from other constituencies, including from large index and pension fund investors and proxy advisory firms.

Each of the 'Big 3' rules-based index investing fund families — BlackRock, Vanguard and State Street — are vocal. BlackRock expects at least two board members to be female and already is voting against the re-election of nominating committee members on companies where it sees shortfalls in board diversity. Vanguard has joined the '30% Club' (https://30percentclub.org). State Street formally has announced that beginning in 2020, it will vote against the entire nominating committee of any company without at least one female director — thus mirroring the first step in California's requirement.

And proxy advisors, whose policies remain controlling in the voting decisions of many institutional investors, are likewise adopting similar stances. ISS issued a new 2019 policy, which is effective in 2020, to vote against re-electing the nominating committee chairperson where no female is on the board. Glass Lewis issued an identical policy in 2017, which took effect already in 2019 and extends further in that Glass Lewis reserves the right to vote against the re-election of more than just the nominating committee chair. These efforts stand on their own and U.S. public company boards should be cognizant that irrespective of California's law, Judicial Watch's challenge thereto or their company's location, there are independent reasons to pay heed in earnest to increasing board gender diversity.

Against this background, we thought it would be useful to benchmark the data on where California public companies stand today on board gender diversity.

SAMPLE SIZE TO BENCHMARK BOARD GENDER DIVERSITY

For meaningful trends in board gender diversity, of the approximately 750 public companies in California, we looked in 2019 at 350 companies, with two criteria: (1) headquarters in California, and (2) over $750 million market capitalization, as follows:

122 companies between $750 million – $2 billion

93 companies between $2 billion – $5 billion

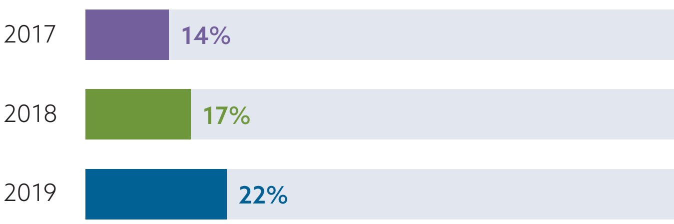
135 companies with over $5 billion

These 350 companies — representing just under half of the public companies in California — are the most material from an economic standpoint. Interesting to note, despite the contraction in the number of public companies in the United States — from approximately 8,100 in 1996 to 4,300 today — the population of public companies headquartered in California with above $750 million in market capitalization has grown in the past three years: from 294 in 2017 to 305 in 2018 to 350 in 2019. No doubt this is both because equity market values have continued appreciating in a bull market, and, relatedly, the IPO 'window' has reopened and numerous companies have gone public.

Increase in Public Companies in California Worth Over $750m

TRENDS IN BOARD GENDER DIVERSITY

The median percentage of female directors at the sample companies has increased.



Moreover, there is a striking continued difference in gender balance between smaller cap and large cap companies.

# of Female Directors	$750m–$2b (%)	$2b–$5b (%)	$5b+ (%)
0	11%	4%	3%
1	35%	39%	16%
2	35%	28%	45%
3	14%	22%	24%
4+	4%	8%	11%

Correlation of Number of Female Directors to Market Capitalization

- Smaller companies are more likely to have 0-2 female board members.
- Mid-size companies are more likely to have 1-3 female board members.
- Large cap companies have a definite bulge — 45 percent of such companies have 2 female board directors and 35 percent of such companies have 3 or more female board directors.

Over 10% of Companies Worth From $750m-$2b Still Do Not Have a Single Female Director

- The slope of companies with no female director clearly is correlated and goes down as market cap increases.
- 1 out of every 10 companies with market capitalization between $750m-$2b do not have any gender diversity in their boardrooms. However, that number still represents progress, as it is a roughly 50 percent drop from 2017 — when 1 in 5 companies in that value band did not have a single female board director.

Acceleration of Female Directors in Large Cap Companies

- Whereas 1 in 3 companies over $5 billion in value had 2 female directors in 2017, in 2019 that number is just shy of 1 in 2.
- The percentage of large cap companies with 3 female directors increased from 14 percent in 2017 to 24 percent in 2019 — and the percentage of such companies with more than 3 female directors ticked up slightly from 8 percent to 11 percent.

Mid-Size Companies Also Continue Acceleration of Adding Female Directors

- 7 percent had 3 female board members in 2017 and 22 percent have 3 female board members in 2019.
- The percentage of such companies with 0 female board members has precipitously dropped — from 1 in 5 companies in 2017 to under 5 percent in 2019.

# of Female Directors		$750m–$2b Market Capitalization	$2b–$5b Market Capitalization	$5b+ Market Capitalization
0	2017	20%	20%	7%
	2018	19%	12%	3%
	2019	11%	4%	3%
1	2017	47%	41%	38%
	2018	44%	45%	29%
	2019	35%	39%	16%
2	2017	25%	27%	33%
	2018	26%	30%	44%
	2019	35%	28%	45%
3	2017	5%	7%	14%
	2018	8%	8%	14%
	2019	14%	22%	24%
4+	2017	2%	5%	8%
	2018	3%	5%	10%
	2019	4%	8%	11%

In conclusion, there continues to be an unmistakable migration toward higher percentage of female board members among California's most significant public companies. We clearly would expect this trend to continue as the deadlines at the end of this year and then in 2021 for mandated board gender diversity continue to grow closer.

RAW DATA ON CALIFORNIA BOARD GENDER DIVERSITY

Companies w/ $750m-$2bn Market Cap						
# of Female Directors	2017		2018		2019	
	#	%	#	%	#	%
0	18	20%	19	19%	14	11%
1	43	47%	43	44%	43	35%
2	23	25%	25	26%	45	35%
3	5	5%	8	8%	24	14%
4+	2	2%	3	3%	11	4%
Total	**91**		**98**		**122**	

Companies w/ $2bn-$5bn Market Cap						
# of Female Directors	2017		2018		2019	
	#	%	#	%	#	%
0	17	20%	10	12%	4	4%
1	34	41%	38	45%	36	39%
2	22	27%	25	30%	26	28%
3	6	7%	7	8%	20	22%
4+	4	5%	4	5%	7	8%
Total	**83**		**84**		**93**	

Companies w/ >$5bn Market Cap						
# of Female Directors	2017		2018		2019	
	#	%	#	%	#	%
0	8	7%	4	3%	4	3%
1	46	38%	36	29%	22	16%
2	39	33%	54	44%	61	45%
3	17	14%	17	14%	33	24%
4+	10	8%	12	10%	15	11%
Total	**120**		**123**		**135**	