

## CALIFORNIA STATE LAW REQUIRING DIVERSITY ON COMPANY BOARDS FOUND UNCONSTITUTIONAL

On May 13, 2022, in [\*Crest, et. al. v. Padilla\*](#), the Superior Court of the State of California for the County of Los Angeles held that [S.B. 826](#), later codified as [§301.3](#) of the California Corporations Code, violated the equal protection clause of the California constitution on its face. This decision comes on the heels of an April 2022 ruling in which [§301.4](#), a similar law, was also [found unconstitutional](#) on equal protection grounds.

§301.3 requires, among other things, that publicly held companies located within the state have:

- three or more female directors for boards with six or more members;
- two or more female directors for boards with five members; and
- at least one female director for boards with four or fewer members.

Penalties for non-compliance with §301.3 include fines of \$100,000 for the first violation and \$300,000 for subsequent violations. Other states, including Colorado, Illinois, Maryland, New York, Pennsylvania, and Washington, followed California's lead and enacted legislation, albeit less expansive, requiring or encouraging some form of board diversity. Moreover, some proxy advisors such as [Glass Lewis](#),<sup>1</sup> generally recommend that shareholders vote in line with companies' applicable state laws regarding board diversity.

In finding [S.B. 826](#) unconstitutional, the California court reasoned that the State of California failed to meet the strict scrutiny test and did not present a "compelling state interest" for the law's treatment of similarly situated individuals based on gender. While the court acknowledged that remediation of discrimination may constitute a compelling state interest, such remedies cannot be founded upon "[g]eneralized, non-specific allegations of discrimination." Further, the court was not convinced that S.B. 826 furthered a compelling state interest by increasing gender diversity on public company boards. The court scrutinized the State of

<sup>1</sup> However, other proxy advisors, such as ISS, do not make similar recommendations and, instead, recommend voting in line with their own, individual gender diversity policies.

California's lack of reliable evidence that S.B. 826's gender classification was necessary to "boost California's economy, improve opportunities for women in the workplace, or protect California taxpayers, public employees, pensions, and retirees." Lastly, the court found that the State of California failed to consider, or demonstrate the absence of, gender-neutral alternatives to remedy discrimination against women by companies in the selection of board members.

While it's unclear whether the State of California will appeal the ruling, other board diversity mandates face similar [legal challenges](#), including [Nasdaq Rule 5605\(f\)](#), which requires that Nasdaq-listed companies have at least one female board member and one board member who identifies as an underrepresented minority or LGBTQ+ or, alternatively, disclose the reasons why the company lacks sufficient board diversity by the later of August 6, 2025 or when the company files its proxy statement for its annual meeting in 2026.

## CONTACTS

**Andrew Epstein**  
Partner

**T** +1 212 878 8332  
**E** andrew.epstein  
@cliffordchance.com

**Kathleen Werner**  
Partner

**T** +1 212 878 8526  
**E** kathleen.werner  
@cliffordchance.com

**Jed Tift**  
Associate

**T** +1 212 880 5695  
**E** jed.tift  
@cliffordchance.com

### GLOBAL CAPITAL MARKETS CONTACTS – AMERICAS

**Jay Bernstein**  
Senior Counsel

**T** +1 212 878 8527  
**E** jay.bernstein  
@cliffordchance.com

**Cliff Cone**  
Partner

**T** +1 212 878 3180  
**E** clifford.cone  
@cliffordchance.com

**Jacob Farquharson**  
Partner

**T** +1 212 878 3302  
**E** jacob.farquharson  
@cliffordchance.com

**Patrick Jackson**  
Partner

**T** +55 11 3019 6017  
**E** patrick.jackson  
@cliffordchance.com

**Jefferey LeMaster**  
Partner

**T** +1 212 878 3206  
**E** jefferey.lemaster  
@cliffordchance.com

**Jason Myers**  
Partner

**T** +1 212 878 8324  
**E** jason.myers  
@cliffordchance.com

**Jonathan Zonis**  
Partner

**T** +1 212 878 3250  
**E** jonathan.zonis  
@cliffordchance.com

**Jason Parsont**  
Counsel

**T** +1 212 878 8213  
**E** jason.parsont  
@cliffordchance.com

**Matt Worden**  
Counsel

**T** +1 212 878 4970  
**E** matt.worden  
@cliffordchance.com

**Rebecca Hoskins**  
Professional Support  
Lawyer

**T** +1 212 878 3118  
**E** rebecca.hoskins  
@cliffordchance.com

**Hank Michael**  
Strategic Advisory  
Lawyer

**T** +1 212 878 8225  
**E** hank.michael  
@cliffordchance.com

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## ASIA-PACIFIC

**Liu Fang**  
Partner

**T** +852 2825 8919  
**E** fang.liu  
@cliffordchance.com

**Johannes Juette**  
Partner

**T** +65 6410 2293  
**E** johannes.juette  
@cliffordchance.com

**Jean Thio**  
Partner

**T** +65 6506 1956  
**E** jean.thio  
@cliffordchance.com

**Alan Yeung**  
Partner

**T** +852 2826 3520  
**E** alan.yeung  
@cliffordchance.com

**Terrence Moloney**  
Counsel

**T** +61 2 8922 8559  
**E** terrence.moloney  
@cliffordchance.com

## EUROPE

**Alex Bafi**  
Partner

**T** +33 1 4405 5267  
**E** alex.bafi  
@cliffordchance.com

**John Connolly**  
Partner

**T** +44 207006 2096  
**E** john.connolly  
@cliffordchance.com

**Michael Dakin**  
Partner

**T** +44 207006 2856  
**E** michael.dakin  
@cliffordchance.com

**George Hacket**  
Partner

**T** +49 69 7199 3103  
**E** george.hacket  
@cliffordchance.com

**Andrew Kelly**  
Partner

**T** +44 207006 8552  
**E** andrew.kelly  
@cliffordchance.com

**Olivier Plessis**  
Counsel

**T** +33 1 4405 5487  
**E** olivier.plessis  
@cliffordchance.com

**Laura Scaglioni**  
Counsel

**T** +39 02 8063 4254  
**E** laura.scaglioni  
@cliffordchance.com