

# California Court Rules State's Racial/Ethnic Board Diversity Mandate Unconstitutional

Insights

April 4, 2022

*In September 2018, California became the first state to mandate gender diversity for boards of directors of public companies, requiring those headquartered in California (irrespective of their state of incorporation) to have at least one woman on their board by the end of 2019 and, depending on the company's size, two or three women by the end of 2021 (SB 826). A similar measure followed in September 2020, which required California-headquartered public companies to have at least one director from an "underrepresented community" (defined as "an individual who self-identifies as Black, African American, Hispanic, Latino, Asian, Pacific Islander, Native American, Native Hawaiian or Alaska Native, or who self-identifies as gay, lesbian, bisexual or transgender") by the end of 2021 and, depending on the company's size, up to three such directors by the end of 2022 (AB 979). Companies may increase the size of their board to comply with the mandates, and a single director may satisfy both requirements. Noncompliant companies face potential fines of up to \$300,000 per violation, although the California Secretary of State has yet to propose or adopt implementing regulations and has not imposed any penalties on noncompliant companies to date.*

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On April 1, 2022, in the first decision to be handed down in several state and federal lawsuits underway challenging California's gender and racial board diversity mandates, Judge Terry Green of Los Angeles County Superior Court declared the state's board diversity mandate for "underrepresented communities" (racial/ethnic/LGBT) unconstitutional. The judge did not explain the reasoning for his decision, and it is currently unclear whether the state will appeal the ruling.

The lawsuit was filed by Judicial Watch, a nonprofit conservative advocacy group, on behalf of three California taxpayers to prevent California from enforcing AB 979, which Judicial Watch argued violated the equal protection clause of the California Constitution because it mandated quotas. In a hearing last month on both parties' summary judgment motions, Judge Green expressed skepticism toward the law, saying it appeared to call for racial quotas and describing it as "a bit arbitrary" as to which minority groups are included in the law and which are not. The state argued the law does not establish quotas because it allows boards to add new seats to accommodate the law's requirements. Late on Friday, the court granted Judicial Watch's motion for summary judgment, holding that any expenditure of taxpayer funds or taxpayer-financed resources on the statute is illegal under the California Constitution.

### **No Decision on California's Gender Board Diversity Law**

Judicial Watch filed a similar lawsuit in Los Angeles County Superior Court challenging California's board gender diversity mandate. A six-week bench trial before a different judge of that court recently concluded, although the judge has yet to make a ruling.

### **Federal Court Challenges to California Laws**

Challenges against both board diversity statutes are also pending in the U.S. District Court for the Eastern District of California, a federal court in the Ninth Circuit, arguing that the California mandates violate the federal equal protection clause and anti-discrimination statutes.

### **Federal Court Challenge to Nasdaq Rules**

Another federal case is pending in the Fifth Circuit against Nasdaq's board diversity listing rules, effective this year, that require most listed companies, after a transition period, to have at least two "diverse" directors, or explain why they do not, and to publish diversity data about their boards. The lawsuit argues that the SEC's approval of Nasdaq's rules violated the equal protection clause of the U.S. Constitution and federal anti-discrimination laws. The petitioner has filed its opening brief, but it is unclear whether a decision will be handed down this year.

### **More Information**

More information about California's board diversity requirements and related resources, including the March 2022 report documenting the status of California-

headquartered public companies' compliance with the mandates, is available on the Secretary of State's website [here](#).

More information about Nasdaq's board diversity and disclosure listing rules can be found in our previously published client alert [here](#).

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