

Illinois General Assembly Passes Bill to Require Annual Reporting of Board Diversity Information

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Bill intended to provide data to support future policy changes to address underrepresentation of women and minorities on public company boards.

On Saturday, June 1, 2019, The Illinois General Assembly passed a bill (the “Diversity Disclosure Bill”) requiring most publicly held companies organized or headquartered in Illinois to include detailed demographic diversity information in their annual reports required to be filed with the Illinois Secretary of State. The Diversity Disclosure Bill is expected to be signed by Governor J.B. Pritzker.

As enacted, the Diversity Disclosure Bill differs significantly from both the original bill (HB 3394) as passed by the House on March 29, 2019 and a proposed amendment considered by the Senate. Unlike the earlier versions of the bill, the Diversity Disclosure Bill *does not mandate* the inclusion of women or minorities on public company boards or impose a fine for failure to achieve a specified diversity target. The Diversity Disclosure Bill requires only that subject companies *report* diversity-related information to the Secretary of State.

The earlier versions of the bill were patterned after the California statute adopted last year requiring publicly held companies organized or based in California to include women on their boards of directors. The California statute also levies fines against noncompliant companies. In our view, the absence of a mandate and potential for fines in the Diversity Disclosure Bill avoids the serious constitutional questions as to the validity of the California statute. We note, however, that the Diversity Disclosure Bill expressly states that it is the intent of the General Assembly to gather more data and study the underrepresentation of women and minorities in positions of corporate authority so that effective policy changes may be implemented in the future. Accordingly, future legislation mandating board diversity along the lines of the California statute remains a possibility.

The Diversity Disclosure Bill also calls for the University of Illinois System to publicly report on the

demographic characteristics of directors and officers¹ of subject companies and to publish individual ratings of companies based on their reported information. The Diversity Disclosure Bill's requirement of individual ratings based on both gender and minority diversity are a step ahead of proxy advisory firms such as ISS and Glass Lewis which currently only track, and make voting recommendations based on, gender diversity.² The Diversity Disclosure Bill could lead the way for broader diversity tracking and voting guidelines by proxy advisory firms in the future.

What companies are subject to the Diversity Disclosure Bill?

The Diversity Disclosure Bill applies to “publicly held”³ domestic corporations (those organized under Illinois law) and foreign corporations (those organized under the laws of another jurisdiction but qualified to transact business in Illinois). The substantive “demographic reporting obligations” under the Diversity Disclosure Bill apply *only* to those corporations which have their principal executive offices located in the State of Illinois.⁴ The mandated disclosures are to be included in the Annual Report required to be filed with the Secretary of State by Illinois Business Corporation Act Section 14.05, which applies to domestic corporations and foreign corporations authorized to transact business in the State of Illinois. The Diversity Disclosure Bill, by its express terms, applies only to corporations and not to limited liability companies, limited partnerships, trusts or other legal entities. As a result, certain publicly held entities with their principal executive offices in Illinois, including closed-end investment companies, effectively are not subject to the Diversity Disclosure Bill. Section 14.05 also does not apply to Illinois incorporated homestead associations, building and loan associations, banks and insurance companies.

What additional information is required to be included in the Annual Report?

Publicly held domestic and foreign corporations that have their principal executive offices located in Illinois must disclose the information set forth below. It is worth noting that the Diversity Disclosure Bill directs the Secretary of State to make such information available to the public online as it is received.

- (i) Data on specific qualifications, skills and experience that the corporation considers for its board of directors, nominees for the board of directors, and executive officers
- (ii) The self-identified gender of each member of its board of directors
- (iii) Whether each member of its board of directors self-identifies as a minority person and, if so, which race or ethnicity to which the member belongs
- (iv) A description of the corporation's process for identifying and evaluating nominees for the board of directors, including whether and, if so, how demographic diversity is considered⁵
- (v) A description of the corporation's process for identifying and appointing executive officers, including whether and, if so, how demographic diversity is considered
- (vi) A description of the corporation's policies and practices for promoting diversity, equity and inclusion among its board of directors and executive officers

What classifications of people are covered by the Diversity Disclosure Bill?

The Diversity Disclosure Bill requires disclosures about females and minority persons. “Female” is defined as a person who is a citizen or lawful permanent resident of the United States and who self-identifies as a woman, without regard to the individual's designated sex at birth. “Minority person” is defined as a person who is a citizen or lawful permanent resident of the United States and who is any of the following races or ethnicities: American Indian or Alaska Native; Asian; Black or African

American; Hispanic or Latino; or Native Hawaiian or other Pacific Islander.⁶ Interestingly, in order to be reported as a female or minority person, a director must be a citizen or lawful permanent resident⁷ of the United States.

When must the information be provided?

The Diversity Disclosure Bill will be effective as of the date of enactment. Because the bill requires that the demographic diversity information be included in annual reports no later than January 1, 2021, subject companies should be prepared to include the required information in their annual reports to be filed with the Illinois Secretary of State in 2020. The Diversity Disclosure Bill is silent as to the date with respect to which the information will be disclosed. Absent guidance from the Secretary of State, companies should consider stating in their annual reports the specific date with respect to which the information is reported.

What should subject companies do now?

Companies subject to the demographic disclosure obligations will want to review their existing diversity policies as well as their proxy statement disclosures in response to Regulation S-K, Item 407(c)(2). These SEC-required disclosures address, among other things, the minimum qualifications, qualities and skills the nominating committee (or board) considers necessary for directors, as well as information regarding whether the nominating committee (or board) considers diversity in identifying nominees for director and other disclosures related to any board diversity policy. These existing disclosures can form the basis for some of the disclosures required by the Diversity Disclosure Bill, and subject companies will want to harmonize their SEC and Illinois-mandated disclosures in this regard.

Subject companies will also want to update their D&O questionnaires to gather some of the needed information. For example, companies should include questions regarding whether the responding director is a citizen or lawful permanent resident of the United States and self-identifies as a female and/or a minority person. The definition of each ethnic and racial minority identified in the statute will need to be included in the definitions section of the D&O questionnaire.

It is expected that the Illinois Secretary of State will update the Form BCA 14.05 Annual Reports for domestic corporations ([here](#)) and for foreign corporations ([here](#)), which updates should provide more clarity as to the date as to which the required information must be provided.

¹ While the University of Illinois System is charged with publicly reporting on the demographic characteristics of directors and officers, subject companies will only be required to disclose such information relating to their directors.

² Starting in 2019, Glass Lewis's general policy has been to recommend voting against nominating committee chairs at companies with no female directors unless the company is outside of the Russell 3000 index or the board has provided a sufficient rationale for not having any female directors.

ISS has announced a similar policy to take effect in 2020.

³ As used in the Board Diversity Disclosure Bill, "publicly held" means having outstanding shares listed on a "major" United States stock exchange. Certainly, this would include corporations with shares listed on the NYSE and Nasdaq, but it is not clear whether the term "publicly held" would include

corporations with shares listed on other U.S. stock exchanges.

⁴ All domestic and foreign corporations will have to disclose whether or not they are "publicly held" and have their principal executive office in Illinois. Public companies identify their principal executive office on their Forms 10-K, 10-Q and 8-K filings with the SEC.

5 The detailed “demographic reporting obligations” do not extend to executive officers.

6 Racial and ethnic identities are as specified and defined in the statute.

7 Per the Department of Homeland Security website, lawful permanent residents, also known as “green card” holders, are “non-citizens who are lawfully authorized to live permanently within the United States.”

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National Law Review, Volume IX, Number 156

Source URL: <https://natlawreview.com/article/illinois-general-assembly-passes-bill-to-require-annual-reporting-board-diversity>