SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–90574; File No. SR–NASDAQ–2020–081]

Self-Regulatory Organizations; The Nasdaq Stock Market LLC; Notice of Filing of Proposed Rule Change To Adopt Listing Rules Related to Board Diversity

December 4, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on December 1, 2020, The Nasdaq Stock Market LLC (''Nasdaq'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to adopt listing rules related to board diversity, as described in more detail below:

(i) To adopt Rule 5605(f) (Diverse Board Representation), which would require Nasdaq-listed companies, subject to certain exceptions, (A) to have at least one director who self-identifies as a female, and (B) to have at least one director who self-identifies as Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, two or more races or ethnicities, or as LGBTQ+, or (C) to explain why the company does not have at least two directors on its board who self-identify in the categories listed above;

(ii) to adopt Rule 5606 (Board Diversity Disclosure), which would require Nasdaq-listed companies, subject to certain exceptions, to provide statistical information in a proposed uniform format on the company's board of directors related to a director's self-identified gender, race, and self-identification as LGBTQ+; and

(iii) to update Rule 5615 and IM–5615–3 (Foreign Private Issuers) and Rule 5810(c) (Types of Deficiencies and Notifications) to incorporate references to proposed Rule 5605(f) and Rule 5606; and

(iv) to make certain other non-substantive conforming changes.

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

The text of the proposed rule change is available on the Exchange's website at *https://listingcenter.nasdaq.com/rulebook/nasdaq/rules,* at the principal office of the Exchange, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

I. The Diversity Imperative for Corporate Boards

Over the past year, the social justice movement has brought heightened attention to the commitment of public companies to diversity and inclusion. Controversies arising from corporate culture and human capital management challenges, as well as technology-driven changes to the business landscape, already underscored the need for enhanced board diversity—diversity in the boardroom is good corporate governance. The benefits to stakeholders of increased diversity are becoming more apparent and include an increased variety of fresh perspectives, improved decision making and oversight, and strengthened internal controls. Nasdaq believes that the heightened focus on corporate board diversity by companies,[3] investors,[4] corporate governance organizations,[5] and legislators[6] demonstrates that investor confidence is enhanced when boardrooms are comprised of more than one demographic group. Nasdaq has also observed recent calls from SEC commissioners[7] and investors[8] for

[3] *See* Deloitte and the Society for Corporate Governance, *Board Practices Quarterly: Diversity, equity, and inclusion* (Sept. 2020), available at: *https://www2.deloitte.com/us/en/pages/center-for-board-effectiveness/articles/diversity-equity-and-inclusion.html* (finding, in a survey of over 200 companies, that ''most companies and/or their boards have taken, or intend to take, actions in response to recent events surrounding racial inequality and inequity; 71% of public companies and 65% of private companies answered this question affirmatively'').

[4] *See* ISS Governance, *2020 Global Benchmark Policy Survey, Summary of Results* 6 (Sept. 24, 2020), available at: *https://www.issgovernance.com/wp-content/uploads/publications/2020-iss-policy-survey-results-report-1.pdf* (finding that ''a significant majority of investors (61 percent) indicated that boards should aim to reflect the company's customer base and the broader societies in which they operate by including directors drawn from racial and ethnic minority groups'').

[5] *See* International Corporate Governance Network, *ICGN Guidance on Diversity on Boards* 5 (2016), available at: *https://www.icgn.org/sites/default/files/ICGN%20Guidance%20on%20Diversity%20on%20Boards%20-%20Final.pdf* (''The ICGN believes that diversity is a core attribute of a well-functioning board which supports greater long-term value for shareholders and companies.'').

[6] *See, e.g.,* John J. Cannon et al., Sherman & Sterling LLP, *Washington State Becomes Next to Mandate Gender Diversity on Boards* (May 28, 2020), available at: *https://www.shearman.com/perspectives/2020/05/washington-state-becomes-next-to-mandate-gender-diversity-on-boards;* Cal. S.B. 826 (Sept. 30, 2018); Cal. A.B. 979 (Sept. 30, 2020) (California legislation requiring companies headquartered in the state to have at least one director who self-identifies as a Female and one from an Underrepresented Community).

[7] *See* Commissioner Allison Herren Lee, *Regulation S–K and ESG Disclosures: An Unsustainable Silence* (Aug. 26, 2020), available at: *https://www.sec.gov/news/public-statement/lee-regulation-s-k-2020-08-26#_ftnref15* (''There is ever-growing recognition of the importance of diversity from all types of investors . . . [a]nd large numbers of commenters on this [SEC] rule proposal emphasized the need for specific diversity disclosure requirements.''); *see also* Commissioner Caroline Crenshaw, *Statement on the ''Modernization'' of Regulation S–K Items 101, 103, and 105* (August 26, 2020), available at: *https://www.sec.gov/news/public-statement/crenshaw-statement-modernization-regulation-s-k* (''As Commissioner Lee noted in her statement, the final [SEC] rule is also silent on diversity, an issue that is extremely important to investors and to the national conversation. The failure to grapple with these issues is, quite simply, a failure to modernize.''); Mary Jo White, *Keynote Address, International Corporate Governance Network Annual Conference: Focusing the Lens of Disclosure to Set the Path Forward on Board Diversity, Non-GAAP, and Sustainability* (June 27, 2016), available at: *https://www.sec.gov/news/speech/chair-white-icgn-speech.html* (''Companies' disclosures on board diversity in reporting under our current requirements have generally been vague and have changed little since the rule was adopted . . . Our lens of board diversity disclosure needs to be re-focused in order to better serve and inform investors.'').

[8] *See* Vanguard, *Investment Stewardship 2019 Annual Report* (2019), available at: *https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/2019_investment_stewardship_annual_report.pdf* (''We want companies to disclose the diversity makeup of their boards on dimensions such as gender, age, race, ethnicity, and national origin, at least on an aggregate basis.''); *see also* State Street Global Advisors, *Diversity Strategy, Goals & Disclosure: Our Expectations for Public Companies* (Aug. 27, 2020) *https://www.ssga.com/us/en/individual/etfs/insights/diversity-strategy-goals-disclosure-our-expectations-for-public-companies* (announcing expectation that State Street's portfolio companies (including US companies ''and, to the greatest extent possible, non-US companies'') provide board level ''[d]iversity characteristics, including racial and ethnic makeup, of the board of directors'').

companies to provide more transparency regarding board diversity.

Nasdaq conducted an internal study of the current state of board diversity among Nasdaq-listed companies based on public disclosures, and found that while some companies already have made laudable progress in diversifying their boardrooms, the national market system and the public interest would best be served by an additional regulatory impetus for companies to embrace meaningful and multi-dimensional diversification of their boards. It also found that current reporting of board diversity data was not provided in a consistent manner or on a sufficiently widespread basis. As such, investors are not able to readily compare board diversity statistics across companies.

Accordingly, Nasdaq is proposing to require each of its listed companies, subject to certain exceptions, to: (i) Provide statistical information regarding diversity among the members of the company's board of directors under proposed Rule 5606; and (ii) have, or explain why it does not have, at least two ''*Diverse*'' *directors on its board under proposed rule 5605(f)(2).* ''Diverse'' means a director who self-identifies as: (i) Female, (ii) an Underrepresented Minority, or (iii) LGBTQ+. Each listed company must have, or explain why it does not have, at least one Female director and at least one director who is either an Underrepresented Minority or LGBTQ+. Foreign Issuers (including Foreign Private Issuers) and Smaller Reporting Companies, by contrast, have more flexibility and may satisfy the requirement by having two Female directors. ''Female'' means an individual who self-identifies her gender as a woman, without regard to the individual's designated sex at birth. ''Underrepresented Minority'' means, consistent with the categories reported to the Equal Employment Opportunity Commission (''EEOC'') through the Employer Information Report EEO–1 Form (''EEO–1 Report''), an individual who self-identifies as one or more of the following: Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, or Two or More Races or Ethnicities. ''LGBTQ+'' means an individual who self-identifies as any of the following: Lesbian, gay, bisexual, transgender or a member of the queer community.

Under proposed Rule 5606, Nasdaq proposes to provide each company with one calendar year from the date that the Commission approves this proposal (the ''*Approval Date*''*) to comply with the requirement for statistical information regarding diversity.* Under proposed Rule 5605(f)(2), no later than two calendar years after the Approval Date, each company must have, or explain why it does not have, one Diverse director. Further, each company must have, or explain why it does not have, two Diverse directors no later than: (i) Four calendar years after the Approval Date for companies listed on the Nasdaq Global Select or Global Market tiers; or (ii) five calendar years after the Approval Date for companies listed on the Nasdaq Capital Market tier.

Nasdaq undertook extensive research and analysis and has concluded that the proposal will fulfill the objectives of the Act in that it is designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, to prevent fraudulent and manipulative acts and practices, and to protect investors and the public interest. In addition to conducting its own internal analysis as described above, Nasdaq reviewed a substantial body of third-party research and interviewed leaders representing a broad spectrum of market participants and other stakeholders to:

- Determine whether empirical evidence demonstrates an association between board diversity, shareholder value, investor protection and board decision-making;
- understand investors' interest in, and impediments to obtaining, information regarding the state of board diversity at public companies;
- review the current state of board diversity and disclosure, both among Nasdaq-listed companies and more broadly within the U.S.;
- gain a better understanding of the causes of underrepresentation on boards;
- obtain the views of leaders representing public companies, investment banks, corporate governance organizations, investors, regulators and civil rights groups on the value of more diverse corporate boards, and on various approaches to encouraging more diversity on corporate boards; and
- evaluate the success of approaches taken by exchanges, regulators, and governments in both the U.S. and foreign jurisdictions to remedy underrepresentation on boards.

While gender diversity has improved among U.S. company boards in recent years, the pace of change has been gradual, and the U.S. still lags behind other jurisdictions that have imposed requirements related to board diversity. Moreover, progress toward bringing underrepresented racial and ethnic groups into the boardroom has been even slower. Nasdaq is unable to provide definitive estimates regarding the number of listed companies that will be affected by the proposal due to the inconsistent disclosures and definitions of diversity across companies and the extremely limited disclosure of race and ethnicity information—an information gap the proposed rule addresses. Based on the limited information that is available, Nasdaq believes a supermajority of listed companies have made notable strides to improve gender diversity in the boardroom and have at least one woman on the board. Nasdaq also believes that listed companies are diligently working to add directors with other diverse attributes, although consistent with other studies of U.S. companies, Nasdaq believes the pace of progress, in this regard, is happening more gradually. While studies suggest that current candidate selection processes may result in diverse candidates being overlooked, Nasdaq also believes that the lack of reliable and consistent data creates a barrier to measuring and improving diversity in the boardroom.

Nasdaq reviewed dozens of empirical studies and found that an extensive body of academic research demonstrates that diverse boards are positively associated with improved corporate governance and financial performance. For example, as discussed in detail below in *Section II, Academic Research: The Relationship between Diversity and Shareholder Value, Investor Protection and Decision Making,* studies have found that companies with gender-diverse boards or audit committees are associated with: More transparent public disclosures and less information asymmetry; better reporting discipline by management; a lower likelihood of manipulated earnings through earnings management; an increased likelihood of voluntarily disclosing forward-looking information; a lower likelihood of receiving audit qualifications due to errors, non-compliance or omission of information; and a lower likelihood of securities fraud. In addition, studies found that having at least one woman on the board is associated with a lower likelihood of material weaknesses in internal control over financial reporting and a lower likelihood of material financial restatements. Studies also identified positive relationships between board diversity and commonly used financial metrics, including higher returns on invested capital, returns on equity, earnings per share, earnings before interest and taxation margin, asset valuation multiples and credit ratings.

Nasdaq believes there are additional compelling reasons to support the diversification of company boards beyond a link to improved corporate governance and financial performance:

• Investors are calling in greater numbers for diversification of boardrooms. Vanguard, State Street Advisors, BlackRock, and the NYC Comptroller's Office include board diversity expectations in their engagement and proxy voting guidelines.[9] The heightened investor focus on corporate diversity and inclusion efforts demonstrates that investor confidence is undermined when a company's boardroom is homogenous and when transparency about such efforts is lacking. Investors frequently lack access to information about corporate board diversity that could be material to their decision making, and they might divest from companies that fail to take into consideration the demographics of their corporate stakeholders when they refresh their boards. Nasdaq explores these investor sentiments in *Section III, Current State of Board Diversity and Causes of Underrepresentation on Boards.*

• Nasdaq believes, consistent with SEC disclosure requirements in other contexts,[10] that management's vision on key issues impacting the company should be communicated with investors in a clear and straightforward manner. Indeed, transparency is the bedrock of federal securities laws regarding disclosure, and this sentiment is reflected in the broad-based support for uniform disclosure requirements regarding board diversity that Nasdaq observed during the course of its outreach to the industry. In addition, organizational leaders representing every category of corporate stakeholders Nasdaq spoke with (including business, investor, governance, regulatory and civil rights communities) were overwhelmingly in favor of diversifying boardrooms. Nasdaq summarizes the findings of its stakeholder outreach in *Section IV, Stakeholder Perspectives.*

• Legislators at the federal and state level increasingly are taking action to encourage or mandate corporations to diversify their boards and improve diversity disclosures. Congress currently is considering legislation requiring each SEC-registered company to provide board diversity statistics and disclose whether it has a board diversity policy. To date, eleven states have passed or proposed legislation related to board diversity.[11] SEC regulations require companies to disclose whether diversity is considered when identifying director nominees and, if so, how. Nasdaq explores various state and federal initiatives in *Section V, U.S. Regulatory Framework and Section VI, Nasdaq Proposal.*

In considering the merits and shaping the substance of the proposed listing rule, Nasdaq also sought and received valuable input from corporate stakeholders. During those discussions, Nasdaq found consensus across every constituency in the inherent value of board diversity. Business leaders also expressed concern that companies—and particularly smaller companies—would prefer an approach that allows flexibility to comply in a manner that fits their unique circumstances and stakeholders. Nasdaq recognizes that the operations, size, and current board composition of each Nasdaq-listed company are unique, and Nasdaq therefore endeavored to provide a regulatory impetus to enhance board diversity that balances the need for flexibility with each company's particular circumstances.

The Exchange also considered the experience of its parent company, Nasdaq, Inc., as a public company.[12] In 2002, Nasdaq, Inc. met the milestone of welcoming its first woman, Mary Jo White, who later served as SEC Chair, to its board of directors. In her own words, ''I was the first and only woman to serve on the board when I started, but, happily, I was joined by another woman during my tenure . . . And then there were two. Not enough, but better than one.'' [13] In 2019, Nasdaq, Inc. also welcomed its first Black director. As a Charter Pledge Partner of The Board Challenge, Nasdaq supports The Board Challenge's goal of ''true and full representation on all boards of directors.'' [14]

As a self-regulatory organization, Nasdaq also is cognizant of its role in advancing diversity within the financial industry, as outlined in the Commission's diversity standards issued pursuant to Section 342 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (''Standards'').[15] Authored jointly by the Commission and five other financial regulators, the Standards seek to provide a framework for exchanges and financial services organizations ''to create and strengthen

[9] Vanguard announced in 2020 it would begin asking companies about the race and ethnicity of directors. *See* Vanguard, *Investment Stewardship 2020 Annual Report* (2020), available at: *https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/2020_investment_stewardship_annual_report.pdf.* Starting in 2020, State Street Global Advisors will vote against the entire nominating committee of companies that do not have at least one woman on their boards and have not addressed questions on gender diversity within the last three years. *See* State Street Global Advisors, *Summary of Material Changes to State Street Global Advisors' 2020 Proxy Voting and Engagement Guidelines* (2020), available at: *https://www.ssga.com/library-content/pdfs/global/proxy-voting-and-engagement-guidelines.pdf.* Beginning in 2018, BlackRock stated in proxy voting guidelines they ''would normally expect to see at least 2 women directors on every board.'' *See* BlackRock Investment Stewardship, *Corporate governance and proxy voting guidelines for U.S. securities* (Jan. 2020), available at: *https://www.blackrock.com/corporate/literature/fact-sheet/blk-responsible-investment-guidelines-us.pdf.* The NYC Comptroller's Office in 2019 asked companies to adopt policies to ensure women and people of color are on the initial list for every open board seat. *See* Scott M. Stringer, *Remarks at the Bureau of Asset Management 'Emerging Managers and MWBE Managers Conference* (Oct. 11, 2019), available at: *https://comptroller.nyc.gov/wp-content/uploads/2019/10/10.11.19-SMS-BAM-remarks_distro.pdf.*

[10] *See* Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations, 68 FR 75,056 (Dec. 29, 2003) (''We believe that management's most important responsibilities include communicating with investors in a clear and straightforward manner. MD&A is a critical component of that communication. The Commission has long sought through its rules, enforcement actions and interpretive processes to elicit MD&A that not only meets technical disclosure requirements but generally is informative and transparent.''); *see also* Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information, Release No. 33–10890 (Nov. 19, 2020) (citing the 2003 MD&A Interpretative Release and stating that the purpose of the MD&A section is to enable investors to see a company ''through the eyes of management'').

[11] *See* Michael Hatcher and Weldon Latham, *States are Leading the Charge to Corporate Boards: Diversify!,* Harv. L. Sch. Forum on Corp. Governance (May 12, 2020), available at: *https://corpgov.law.harvard.edu/2020/05/12/states-are-leading-the-charge-to-corporate-boards-diversify/.*

[12] While the Exchange recognizes that it is only one part of an ecosystem in which multiple stakeholders are advocating for board diversity, that part is meaningful: The United Nations Sustainable Stock Exchanges Initiative, of which Nasdaq, Inc., is an official supporter, recognized that ''[s]tock exchanges are uniquely positioned to influence their market in a way few other actors can.'' *See* United Nations Sustainable Stock Exchanges Initiative, *How Stock Exchanges Can Advance Gender Equality* 2 (2017), available at: *https://sseinitiative.org/wp-content/uploads/2019/12/How-stock-exchanges-can-advance-gender-equality.pdf.*

[13] *See* Mary Jo White, Completing the Journey: Women as Directors of Public Companies (Sept. 16, 2014), available at: *https://www.sec.gov/news/speech/2014-spch091614-mjw#.VBiLMhaaXDo.*

[14] *See* The Board Challenge, *https://theboardchallenge.org/. See also* Nasdaq, Inc., *Notice of 2020 Annual Meeting of Shareholders and Proxy Statement* 52 (Mar. 31, 2020), available at: *https://ir.nasdaq.com/static-files/ce5519d4-3a0b-48ac-8441-5376ccbad4e5* (Nasdaq, Inc. believes that ''[d]iverse backgrounds lead to diverse perspectives. We are committed to ensuring diverse backgrounds are represented on our board and throughout our organization to further the success of our business and best serve the diverse communities in which we operate.'').

[15] *See* Final Interagency Policy Statement Establishing Joint Standards for Assessing the Diversity Policies and Practices of Entities Regulated by the Agencies, 80 FR 33,016 (June 10, 2015).

[their] diversity policies and practices.'' Through these voluntary Standards, the Commission and other regulators ''encourage each entity to use the[ ] Standards in a manner appropriate to its unique characteristics.'' [16] To that end, the proposed rule leverages the Exchange's unique ability to influence corporate governance in furtherance of the goal of Section 342, which is to address the lack of diversity in the financial services industry.[17] Finally, while the Exchange recognizes the importance of maximizing shareholder value, its role as a listing venue is to establish and enforce substantive standards that promote investor protection. As a self-regulatory organization, the Exchange must demonstrate to the Commission that any proposed rule is consistent with Section 6(b) of the Act because, among other things, it is designed to protect investors, promote the public interest, prevent fraudulent and manipulative acts and practices, and remove impediments to the mechanism of a free and open market. The Exchange must also balance promoting capital formation, efficiency, and competition, among other things, alongside enhancing investor confidence.

With these objectives in mind, Nasdaq believes that a listing rule designed to enhance transparency related to board diversity will increase consistency and comparability of information across Nasdaq-listed companies, thereby increasing transparency and decreasing information collection costs. Nasdaq further believes that a listing rule designed to encourage listed companies to increase diverse representation on their boards will result in improved corporate governance, thus strengthening the integrity of the market, enhancing capital formation, efficiency, and competition, and building investor confidence. To the extent a company chooses not to meet the diversity objectives of Rule 5605(f)(2), Nasdaq believes that the proposal will provide investors with additional transparency through disclosure explaining the company's reasons for not doing so. For example, the company may choose to disclose that it does not meet the diversity objectives of Rule 5605(f)(2) because it is subject to an alternative standard under state or foreign laws and has chosen to meet that standard instead, or has a board philosophy regarding diversity that differs from the diversity objectives set forth in Rule 5605(f)(2). Nasdaq believes that such disclosure will improve the quality of information available to investors who rely on this information to make informed investment and voting decisions, thereby promoting capital formation and efficiency.

Nasdaq observed that studies suggest that certain groups may be underrepresented on boards because the traditional director nomination process is limited by directors looking within their own social networks for candidates with previous C-suite experience.[18] Leaders from across the spectrum of stakeholders with whom Nasdaq spoke reinforced the notion that if companies recruit by skill set and expertise rather than title, they will find there is more than enough diverse talent to satisfy demand. In order to assist companies that strive to meet the diversity objectives of Rule 5605(f)(2), Nasdaq is proposing to provide listed companies that have not yet met its diversity objectives with free access to a network of board-ready diverse candidates and a tool to support board evaluation, benchmarking and refreshment. Nasdaq is contemporaneously submitting a rule filing to the Commission regarding the provision of such services. Nasdaq also plans to publish FAQs on its Listing Center to provide guidance to companies on the application of the proposed rules, and to establish a dedicated mailbox for companies and their counsel to email additional questions to Nasdaq regarding the application of the proposed rule. Nasdaq believes that these services will help to ease the compliance burden on companies whether they choose to meet the listing rule's diversity objectives or provide an explanation for not doing so.

II. Academic Research: The Relationship Between Diversity and Shareholder Value, Investor Protection and Decision Making

A company's board of directors plays a critical role in formulating company strategy; appointing, advising and overseeing management; and protecting investors. Nasdaq has recognized the importance of varied perspectives on boards since 2003, when the Exchange adopted a listing rule intended to enhance investor confidence by requiring listed companies, subject to certain exceptions and cure periods, to have a majority independent board.[19] Accompanying the rule are interpretive materials recognizing that independent directors ''play an important role in assuring investor confidence. Through the exercise of independent judgment, they act on behalf of investors to *maximize shareholder value* in the Companies they oversee and guard against conflicts of interest.'' [20]

a. Diversity and Shareholder Value

There is a significant body of research suggesting a positive association between diversity and shareholder value.[21] In the words of SEC Commissioner Allison Herren Lee: ''to the extent one seeks economic support for diversity and inclusion (instead of requiring economic support for the lack of diversity and exclusion), the evidence is in.'' [22]

The Carlyle Group (2020) found that its portfolio companies with two or more diverse directors had average earnings growth of 12.3% over the previous three years, compared to 0.5% among portfolio companies with no diverse directors, where diverse directors were defined as female, Black, Hispanic or Asian.[23] ''After controlling for industry, fund, and vintage year, companies with diverse boards generate earnings growth that's five times faster, on average, with each diverse board member associated with a 5% increase in annualized earnings growth.'' [24]

Several other studies also found a positive association between diverse boards and company performance. FCLTGlobal (2019) found that ''the most diverse boards (top 20 percent) added 3.3 percentage points to [return on invested capital], as compared to their least diverse peers (bottom 20 percent).'' [25] McKinsey (2015) found

[16] *Id.* at 33,023.

[17] 156 Cong. Rec. H5233–61 (June 30, 2010).

[18] *See infra* Section III.

[19] *See* Nasdaq Stock Market Rulebook, Rules 5605(b), 5615(a), and 5605(b)(1)(A).

[20] *Id.,* IM–5605–1 (emphasis added).

[21] Some companies recently have expressed the belief that a company must consider the impact of its activities on a broader group of stakeholders beyond shareholders. *See* Business Roundtable, *Statement on the Purpose of a Corporation* (Aug. 19, 2019), available at: *https://s3.amazonaws.com/brt.org/BRT-StatementonthePurposeofaCorporationOctober2020.pdf.* Commentators articulated this view as early as 1932. *See* E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?,* 45 Harv. L. Rev. 1145, 1153 (1932).

[22] *See* Commissioner Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (September 22, 2020), available at: *https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.*

[23] *See* Jason M. Thomas and Megan Starr, The Carlyle Group, *Global Insights: From Impact Investing to Investing for Impact* 5 (Feb. 24, 2020), available at: *https://www.carlyle.com/sites/default/files2020-02/From%20Impact%20Investing%20to%20Investing%20for%20Impact_022420.pdf* (analyzing Carlyle U.S. portfolio company data, February 2020).

[24] *Id.*

[25] *See* FCLTGlobal, *The Long-term Habits of a Highly Effective Corporate Board* 11 (March 2019), available at: *https://www.fcltglobal.org/wp-content/uploads/long-term-habits-of-highly-effective-*

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that ''companies in the top quartile for racial/ethnic diversity were 35 percent more likely to have financial returns above their national industry median.'' [26] Carter, Simkins and Simpson (2003) found among Fortune 1000 companies ''statistically significant positive relationships between the presence of women or minorities on the board and firm value.'' [27] Bernile, Bhagwat and Yonker (2017) found that greater diversity on boards—including gender, ethnicity, educational background, age, financial expertise and board experience—is associated with increased operating performance, higher asset valuation multiples, lower stock return volatility, reduced financial leverage, increased dividend payouts to shareholders, higher investment in R&D and better innovation.[28] The authors observed that ''[t]his is in line with the results in Carter, Simkins, and Simpson (2003), which show a positive association between local demographic diversity and firm value.'' [29]

Several studies have found a positive association between gender diversity and financial performance. Credit Suisse (2014) found companies with at least one woman on the board had an average sector-adjusted return on equity (''ROE'') of 12.2%, compared to 10.1% for companies with no female directors, and average sector-adjusted ROEs of 14.1% and 11.2%, respectively, for the previous nine years.[30] MSCI (2016) found that U.S. companies with at least three women on the board in 2011 experienced median gains in ROE of 10% and earnings per share (''EPS'') of 37% over a five year period, whereas companies that had no female directors in 2011 showed median changes of −1% in ROE and −8% in EPS over the same five-year period.[31] Catalyst (2011) found that the ROE of Fortune 500 companies with at least three women on the board (in at least four of five years) was 46% higher than companies with no women on the board, and return on sales and return on invested capital was 84% and 60% higher, respectively.[32]

Credit Suisse (2016) found an association between LGBTQ+ diversity and stock performance, finding that a basket of 270 companies ''supporting and embracing LGBT employees'' outperformed the MSCI ACWI index by an average of 3.0% per year over the past 6 years.[33] Further, ''[a]gainst a custom basket of companies in North America, Europe and Australia, the LGBT 270 has outperformed by 140 bps annually.'' [34] Nasdaq acknowledges that this study focused on LGBTQ+ employees as opposed to directors, and that there is a lack of published research on the issue of LGBTQ+ representation on boards. However, Out Leadership (2019) suggests that the relationship between board gender diversity and corporate performance may extend to LGBTQ+ diversity:

> While the precise reason for the positive correlation between gender diversity and better corporate performance is unknown, many of the reasons that gender diversity is considered beneficial are also applicable to LGBT+ diversity. LGBT+ diversity in the boardroom may create a dynamic that enables better decisionmaking, and it brings to the boardroom the perspective of a community that is a critical component of the company's consumer population and organizational talent.[35]

McKinsey (2020) found ''a positive, statistically significant correlation between company financial outperformance and [board] diversity, on the dimensions of both gender and ethnicity,'' with companies in the top quartile for board gender diversity ''28 percent more likely than their peers to outperform financially,'' and a statistically significant correlation between board gender diversity and outperformance on earnings before interest and taxation margin.[36] Moody's (2019) found that greater board gender diversity is associated with higher credit ratings, with women accounting for an average of 28% of board seats at Aaa-rated companies but less than 5% of board seats at Ca-rated companies.[37]

While the overwhelming majority of studies on the association between economic performance and board diversity, including gender diversity, present a compelling case that board diversity is positively associated with financial performance, the results of some other studies on gender diversity are mixed. For example, Pletzer et al. (2015) found that board gender diversity alone has a ''small and non-significant'' relationship with a company's financial performance.[38] Post and Byron (2014) found a ''near zero'' relationship with a company's market performance, but a positive relationship with a company's

corporate-boards.pdf (analyzing 2017 MSCI ACWI constituents from 2010 to 2017 using Bloomberg data).

[26] *See* Vivian Hunt et al., McKinsey & Company, *Diversity Matters* (February 2, 2015), available at: *https://www.mckinsey.com/~/media/mckinsey/business%20functions/organization/our%20insights/why%20diversity%20matters/diversity%20matters.pdf* (analyzing 366 public companies in the United Kingdom, Canada, the United States, and Latin America in industries for the years 2010 to 2013, using the ethnic and racial categories African ancestry, European ancestry, Near Eastern, East Asian, South Asian, Latino, Native American, and other).

[27] *See* David A. Carter et al., *Corporate Governance, Board Diversity, and Firm Value.* 38(1) Fin. Rev. 33 (analyzing 638 Fortune 1000 firms in 1997, measuring firm value by Tobin's Q, with board diversity defined as the percentage of women, African Americans, Asians and Hispanics on the board of directors).

[28] *See* Gennaro Bernile et al., *Board Diversity, Firm Risk, and Corporate Policies* (March 6, 2017), available at: *https://ssrn.com/abstract=2733394* (analyzing 21,572 firm-year observations across non-financial, non-utility firms for the years 1996 to 2014, based on the ExecuComp, RiskMetrics, Compustat and CRSP databases).

[29] *Id.* at 32.

[30] *See* Credit Suisse, *The CS Gender 3000: Women in Senior Management* 16 (Sept. 2014), available at: *https://www.credit-suisse.com/media/assets/corporate/docs/about-us/research/publications/the-cs-gender-3000-women-in-senior-management.pdf* (analyzing 3,000 companies across 40 countries from the period from 2005 to 2013).

[31] *See* Meggin Thwing Eastman et al., MSCI, *The tipping point: Women on boards and financial performance* 3 (December 2016), available at: *https://www.msci.com/documents/10199/fd1f8228-cc07-4789-acee-3f9ed97ee8bb* (analyzing of U.S. companies that were constituents of the MSCI World Index for the entire period from July 1, 2011 to June 30, 2016).

[32] *See* Harvey M. Wagner, Catalyst, *The Bottom Line: Corporate Performance and Women's Representation on Boards (2004–2008)* (March 1, 2011), available at: *https://www.catalyst.org/research/the-bottom-line-corporate-performance-and-womens-representation-on-boards-2004-2008/* (analyzing gender diversity data from Catalyst's annual Fortune 500 Census of Women Board Directors report series for the years 2005 to 2009, and corresponding financial data from S&P's Compustat database for the years 2004 to 2008).

[33] *See* Credit Suisse ESG Research, *LGBT: The value of diversity* 1 (April 15, 2016), available at: *https://research-doc.credit-suisse.com/docView?language=ENG&source=emfromsendlink&format=PDF&document_id=807075590&extdocid=807075590_1_eng_pdf&serialid=evu4wXNcHexx7kusNLaZQphUkT9naxi1PvptZQvPjr1k%3d.*

[34] *Id.*

[35] *See* Quorum, *Out Leadership's LGBT+ Board Diversity and Disclosure Guidelines* 3 (2019), available at: *https://outleadership.com/content/uploads/2019/01/OL-LGBT-Board-Diversity-Guidelines.pdf.*

[36] *See* McKinsey & Company, *Diversity wins: How inclusion matters* 13 (May 2020), available at: *https://www.mckinsey.com/~/media/McKinsey/Featured%20Insights/Diversity%20and%20Inclusion/Diversity%20wins%20How%20inclusion%20matters/Diversity-wins-How-inclusion-matters-vF.pdf* (analyzing 1,039 companies across 15 countries for the period from December 2018 to November 2019).

[37] *See* Moody's Investors Service, *Gender diversity is correlated with higher ratings, but mandates pose short-term risk* 2 (Sept. 11, 2019), available at: *https://www.moodys.com/research/Moodys-Corporate-board-gender-diversity-associated-with-higher-credit-ratingsPBC_1193768* (analyzing 1,109 publicly traded North American companies rated by Moody's).

[38] *See* Jan Luca Pletzer et al., *Does Gender Matter? Female Representation on Corporate Boards and Firm Financial Performance—A Meta-Analysis* 1, PLOS One (June 18, 2015); *see also* Alice H. Eagly (2016), *When Passionate Advocates Meet Research on Diversity, Does the Honest Broker Stand a Chance?,* 72 J. Social Issues 199 (2016), available at *https://doi.org/10.1111/josi.12163* (concluding that the ''research findings are mixed, and repeated meta-analyses have yielded average correlational findings that are null or extremely small'' with respect to board gender diversity and company performance).

accounting returns.[39] Carter, D'Souza, Simkins and Simpson (2010) found that ''[w]hen Tobin's Q is used as the measure of financial performance, we find no relationship to gender diversity or ethnic minority diversity, neither positive nor negative.'' [40] A study conducted by Campbell and Minguez-Vera (2007) ''suggests, at a minimum, that increased gender diversity can be achieved without destroying shareholder value.'' [41] Adams and Ferreira (2009) found that ''gender diversity has beneficial effects in companies with weak shareholder rights, where additional board monitoring could enhance firm value, but detrimental effects in companies with strong shareholder rights.'' [42] Carter et al. (2010) [43] and the U.S. Government Accountability Office (''GAO'') (2015) [44] concluded that the mixed nature of various academic studies may be due to differences in methodologies, data samples and time periods.

While there are studies drawing different conclusions, Nasdaq believes that there is a compelling body of credible research on the association between economic performance and board diversity. At a minimum, Nasdaq believes that the academic studies support the conclusion that board diversity does not have adverse effects on company financial performance. This is not the first time Nasdaq has considered whether, on balance, various studies finding mixed results related to board composition and company performance are a sufficient rationale to propose a listing rule. For example, in 2003, notwithstanding the varying findings of studies at the time regarding the relationship between company performance and board independence,[45] Nasdaq adopted listing rules requiring a majority independent board that were ''intended to enhance investor confidence in the companies that list on Nasdaq.'' [46] In its Approval Order, the SEC stated that ''[t]he Commission has long encouraged exchanges to adopt and strengthen their corporate governance listing standards in order to, among other things, enhance investor confidence in the securities markets.'' [47]

Along the same lines, even without clear consensus among studies related to board diversity and company performance, the heightened focus on corporate board diversity by investors demonstrates that investor confidence is undermined when data on board diversity is not readily available and when companies do not explain the reasons for the apparent absence of diversity on their boards. Therefore, Nasdaq believes that the proposal will enhance investor confidence that all listed companies are considering diversity in the context of selecting directors, either by including at least two Diverse directors on their boards or by explaining their rationale for not meeting that objective. Further, Nasdaq believes that the proposal is consistent with the Act because it will not negatively impact capital formation, competition or efficiency among its public companies, and will promote investor protection and the public interest.[48]

b. Diversity and Investor Protection

There is substantial evidence that board diversity enhances the quality of a company's financial reporting, internal controls, public disclosures and management oversight. In reaching this conclusion, Nasdaq evaluated the results of more than a dozen studies spanning more than two decades that found a positive association between gender diversity and important investor protections, and the assertions by some academics that such findings may extend to other forms of diversity, including racial and ethnic diversity. The findings of the studies reviewed by Nasdaq are summarized below.

Adams and Ferreira (2009) found that women are ''more likely to sit on'' the audit committee,[49] and a subsequent study by Srinidhi, Gul and Tsui (2011) found that companies with women on the audit committee are associated with ''higher earnings quality'' and ''better reporting discipline by managers,'' [50] leading the authors to conclude that ''including female directors on the board and the audit committee are plausible ways of improving the firm's reporting discipline and increasing

[39] *See* Corinne Post and Kris Byron, *Women on Boards and Firm Financial Performance: A Meta-Analysis* 1 (2014). In 2016, the same authors, based on a review of the results for 87 studies, ''found that board gender diversity is weakly but significantly positively correlated with [corporate social responsibility],'' although they noted that ''a significant correlational relationship does not prove causality.'' *See* Corinne Post and Kris Byron, *Women on Boards of Directors and Corporate Social Performance: A Meta-Analysis,* 24(4) Corp. Governance: An Int'l Rev. 428 (July 2016), available at *http://dx.doi.org/10.1111/corg.12165.*

[40] *See* David A. Carter et al., *The Gender and Ethnic Diversity of US Boards and Board Committees and Firm Financial Performance,* 18(5) Corp. Governance 396, 410 (2010) (analysis of 541 S&P 500 companies for the years 1998–2002).

[41] *See* Kevin Campbell and Antonio Minguez-Vera, *Gender Diversity in the Boardroom and Firm Financial Performance,* 83(3) J. Bus. Ethics 13 (Feb. 2008) (analyzing 68 non-financial companies listed on the continuous market in Madrid during the period from January 1995 to December 2000, measuring firm value by an approximation of Tobin's Q defined as the sum of the market value of stock and the book value of debt divided by the book value of total assets).

[42] *See* Renee B. Adams and Daniel Ferreira, *Women in the boardroom and their impact on governance and performance,* 94 J. Fin. Econ. 291 (2009) (analyzing 1,939 S&P 500, S&P MidCaps, and S&P SmallCap companies for the period 1996 to 2003, measuring company performance by a proxy for Tobin's Q (the ratio of market value to book value) and return on assets).

[43] *See* Carter et al., *supra* note 40, at 400 (observing that the different ''statistical methods, data, and time periods investigated vary greatly so that the results are not easily comparable.'').

[44] *See* United States Government Accountability Office, Report to the Ranking Member, Subcommittee on Capital Markets and Government Sponsored Enterprises, Committee on Financial Services, House of Representatives, *Corporate Boards: Strategies to Address Representation of Women Include Federal Disclosure Requirements* 5 (Dec. 2015) (the ''GAO Report''), available at: *https://www.gao.gov/assets/680/674008.pdf* (''Some research has found that gender diverse boards may have a positive impact on a company's financial performance, but other research has not. These mixed results depend, in part, on differences in how financial performance was defined and what methodologies were used'').

[45] *See, e.g.,* Benjamin E. Hermalin and Michael S. Weisbach, *The Effects of Board Composition and Direct Incentives on Firm Performance,* 20 Fin. Mgmt. 101, 111 (1991) (finding that ''there appears to be no relation between board composition and performance''); Sanjai Bhagat and Bernard Black, *The Uncertain Relationship Between Board Composition and Firm Performance,* 54(3) Bus. Law. 921, 950 (1999) (''At the very least, there is no convincing evidence that increasing board independence, relative to the norms that currently prevail among large American firms, will improve firm performance. And there is some evidence suggesting the opposite—that firms with supermajority-independent boards perform worse than other firms, and that firms with more inside than independent directors perform about as well as firms with majority- (but not supermajority-) independent boards.'').

[46] *See* Order Approving Proposed Rule Changes, 68 FR 64,154, 64,161 (Nov. 12, 2003) (approving SR–NASD–2002–77, SR–NASD–2002–80, SR–NASD–2002–138, SR–NASD–2002–139, and SR–NASD–2002–141).

[47] *Id.* at 64,176.

[48] *See also* Lee, *supra* note 22 (''I could never quite buy in to the view that some 40 percent of the population in our country (if we're talking about minorities) or over half the country (if we're talking about women) must rationalize their inclusion in corporate boardrooms and elsewhere in economic terms instead of the reverse. How can one possibly justify—in economic terms—the systematic exclusion of a major portion of our talent base from the corporate pool?'').

[49] *See* Adams and Ferreira, *supra* note 42, at 292.

[50] *See* Bin Srinidhi et al., *Female Directors and Earnings Quality,* 28(5) Contemporary Accounting Research 1610, 1612–16 (Winter 2011) (analyzing 3,132 firm years during the period from 2001 to 2007 based on S&P COMPUSTAT, Corporate Library's Board Analyst, and IRRC databases; ''choos[ing] the accruals quality as the metric that best reflects the ability of current earnings to reflect future cash flows'' (noting that it ''best predicts the incidence and magnitude of fraud relative to other commonly used measures of earnings quality'') and analyzing surprise earnings results that exceeded previous earnings or analyst forecasts, because ''managers of firms whose unmanaged earnings fall marginally below the benchmarks have [an] incentive to manage earnings upwards so as to meet or beat previous earnings'').

investor confidence in financial statements.'' [51]

A study conducted in 2016 by Pucheta-Martínez et al. concluded that gender diversity on the audit committee ''improves the quality of financial information.'' [52] They found that ''the percentage of females on [audit committees] reduces the probability of [audit] qualifications due to errors, non-compliance or the omission of information,'' [53] and found a positive association between gender diverse audit committees and disclosing audit reports with uncertainties and scope limitations. This suggests that gender diverse audit committees ''ensure that managers do not seek to pressure auditors into issuing a clean opinion instead of a qualified opinion'' when any uncertainties or scope limitations are identified.[54]

More recently, a study by Gull in 2018 found that the presence of female audit committee members with business expertise is associated with a lower magnitude of earnings management,[55] and a study conducted in 2019 by Bravo and Alcaide-Ruiz found a positive association between women on the audit committee with financial or accounting expertise and the voluntary disclosure of forward-looking information.[56] Bravo and Alcaide-Ruiz concluded that ''female [audit committee] members with financial expertise play an important role in influencing disclosure strategies that provide forward-looking information containing projections and financial data useful for investors.'' [57]

While the above studies demonstrate a positive association between gender diverse audit committees and the quality of a company's earnings, financial information and public disclosures, other studies found a positive association between board gender diversity and important investor protections regardless of whether or not women are on the audit committee.

Abbott, Parker & Persley (2012) found, within a sample of non-Fortune 1000 companies, ''a significant association between the presence of at least one woman on the board and a lower likelihood of [a material financial] restatement.'' [58] Their findings are consistent with a subsequent study by Wahid (2017), which concluded that ''gender-diverse boards commit fewer financial reporting mistakes and engage in less fraud.'' [59] Specifically, companies with female directors have ''fewer irregularity-type [financial] restatements, which tend to be indicative of financial manipulation.'' [60] Wahid suggested that the implications of her study extend beyond gender diversity:

> If you're going to introduce perspectives, those perspectives might be coming not just from male versus female. They could be coming from people of different ages, from different racial backgrounds . . . [and] [i]f we just focus on one, we could be essentially taking away from other dimensions of diversity and decreasing perspective.[61]

Cumming, Leung and Rui (2015) also examined the relationship between gender diversity and fraud, and found that the presence of women on boards is associated with a lower likelihood of securities fraud; indeed, they found ''strong evidence of a negative and diminishing effect of women on boards and the probability of being in our fraud sample.'' [62] The authors suggested that ''other forms of board diversity, including but not limited to gender diversity, may likewise reduce fraud.'' [63]

Chen, Eshleman and Soileau (2016) suggested that the relationship between gender diversity and higher earnings quality observed by Srinidhi, Gul and Tsui (2011) is ultimately driven by reduced weaknesses in internal control over financial reporting, noting that ''prior literature has established a negative relationship between internal control weaknesses and earnings quality.'' [64] The authors found that having at least one woman on the board (regardless of whether or not she is on the audit committee) ''may lead to [a] reduced likelihood of material weaknesses [in internal control over financial reporting].'' [65]

Board gender diversity also was found to be positively associated with more transparent public disclosures. Gul, Srinidhi & Ng (2011) concluded that ''gender diversity improves stock price informativeness by increasing voluntary public disclosures in large firms and increasing the incentives for private information collection in small firms.'' [66] Abad et al. (2017) concluded that companies with gender diverse boards are associated with lower levels of information asymmetry, suggesting that increasing board gender diversity is associated with ''reducing the risk of

[51] *Id.* at 1612.

[52] *See* Maria Consuelo Pucheta-Martínez et al., *Corporate governance, female directors and quality of financial information.* 25(4) Bus. Ethics: A European Rev. 363, 378 (2016) (analyzing a sample of non-financial companies listed on the Madrid Stock Exchange during 2004–2011).

[53] *Id.* at 363.

[54] *Id.* at 368.

[55] *See* Ammar Gull et al., *Beyond gender diversity: How specific attributes of female directors affect earnings management,* 50(3) British Acct. Rev. 255 (Sept. 2017), available at: *https://ideas.repec.org/a/eee/bracre/v50y2018i3p255-274.html* (analyzing 394 French companies belonging to the CAC All-Shares index listed on Euronext Paris from 2001 to 2010, prior to the implementation of France's gender mandate law that required women to comprise 20% of a company's board of directors by 2014 and 40% by 2016).

[56] *See* Francisco Bravo and Maria Dolores Alcaide-Ruiz, *The disclosure of financial forward-looking information,* 34(2) Gender in Mgmt. 140, 142–44 (2019) (analyzing companies included in the S&P 100 Index in 2016, ''focus[ing] on the disclosure of financial forward-looking information (which is likely to require financial expertise), such as earnings forecasts, expected revenues, anticipated cash flows or any other financial indicator'').

[57] *Id.* at 150.

[58] *See* Lawrence J. Abbott et al., *Female Board Presence and the Likelihood of Financial Restatement,* 26(4) Accounting Horizons 607, 626 (2012) (analyzing a sample of 278 pre-SOX annual financial restatements and 187 pre-SOX quarterly financial restatements of U.S. companies from January 1, 1997 through June 30, 2002 identified by the U.S. General Accounting Office restatement report 03–138 (which only included ''material misstatements of financial results''), and 75 post-SOX annual financial restatements from July 1, 2002, to September 30, 2005 identified by U.S. General Accounting Office restatement report 06–678 (which only included ''restatements that were being made to correct material misstatements of previously reported financial information''), consisting almost exclusively of non-Fortune 1000 companies).

[59] *See* Aida Sijamic Wahid, The *Effects and the Mechanisms of Board Gender Diversity: Evidence from Financial Manipulation,* J. Bus. Ethics (forthcoming) (Dec. 2017) Rotman School of Management Working Paper No. 2930132 at 1, available at: *https://ssrn.com/abstract=2930132* (analyzing 6,132 U.S. public companies during the period from 2000 to 2010, for a total of 38,273 firm-year observations).

[60] *Id.* at 23.

[61] *See* Barbara Shecter, *Diverse boards tied to fewer financial 'irregularities,' Canadian study finds.* Financial Post (Feb. 5, 2020), *https://business.financialpost.com/news/fp-street/diverse-boards-tied-to-fewer-financial-irregularities-canadian-study-finds* (last accessed Nov. 27, 2020).

[62] *See* Douglas J. Cumming et al., *Gender Diversity and Securities Fraud,* Academy of Management Journal 34 (forthcoming) (Feb. 2, 2015), available at *https://ssrn.com/abstract=2562399* (analyzing China Securities Regulatory Commission data from 2001 to 2010, including 742 companies with enforcement actions for fraud, and 742 non-fraudulent companies for a control group).

[63] *Id.* at 33.

[64] *See* Yu Chen et al., *Board Gender Diversity and Internal Control Weaknesses,* 33 Advances in Acct. 11 (2016) (analyzing a sample of 4267 firm-year observations during the period from 2004 to 2013, beginning ''the first year internal control weaknesses were required to be disclosed under section 404 of SOX'').

[65] *Id.* at 18.

[66] *See* Ferdinand A. Gul et al., *Does board gender diversity improve the informativeness of stock prices?,* 51(3) J. Acct. & Econ. 314 (April 2011) (analyzing 4,084 firm years during the period from 2002 to 2007, excluding companies in the utilities and financial industries, measuring public information disclosure using ''voluntary continuous disclosure of 'other' events in 8K reports'' and measuring stock price informativeness by ''idiosyncratic volatility,'' or volatility that cannot be explained to systematic factors and can be diversified away).

informed trading and enhancing stock liquidity.'' [67]

Other studies have found that diverse boards are better at overseeing management. Adams and Ferreira (2009) found ''direct evidence that more diverse boards are more likely to hold CEOs accountable for poor stock price performance; CEO turnover is more sensitive to stock return performance in firms with relatively more women on boards.'' [68] Lucas-Perez et al. (2014) found that board gender diversity is positively associated with linking executive compensation plans to company performance,[69] which may be an effective mechanism to deter opportunistic behavior by management and align their interests with shareholders.[70] A lack of diversity has been found to have the opposite effect. Westphal and Zajac (1995) found that ''increased demographic similarity between CEOs and the board is likely to result in more generous CEO compensation contracts.'' [71]

c. Diversity and Decision Making

Wahid (2017) suggests that ''at a minimum, gender diversity on corporate boards has a neutral effect on governance quality, and at best, it has positive consequences for boards' ability to monitor firm management.'' [72] Nasdaq reviewed studies suggesting that board diversity can indeed enhance a company's ability to monitor management by reducing ''groupthink'' and improving decision making.

In 2009, the Commission, in adopting rules requiring proxy disclosure describing whether a company considers diversity in identifying director nominees, recognized the impact of diversity on decision making and corporate governance:

> A board may determine, in connection with preparing its disclosure, that it is beneficial to disclose and follow a policy of seeking diversity. Such a policy may encourage boards to conduct broader director searches, evaluating a wider range of candidates and potentially improving board quality. To the extent that boards branch out from the set of candidates they would ordinarily consider, they may nominate directors who have fewer existing ties to the board or management and are, consequently, more independent. To the extent that a more independent board is desirable at a particular company, the resulting increase in board independence could potentially improve governance. In addition, in some companies a policy of increasing board diversity may also improve the board's decision making process by encouraging consideration of a broader range of views.[73]

Nasdaq agrees with the Commission's suggestion that board diversity improves board quality, governance and decision making. Nasdaq is concerned that boards lacking diversity can inadvertently suffer from ''groupthink,'' which is ''a dysfunctional mode of group decision making characterized by a reduction in independent critical thinking and a relentless striving for unanimity among members.'' [74] The catastrophic financial consequences of groupthink became evident in the 2008 global financial crisis, after which the IMF's Independent Evaluation Office concluded that ''[t]he IMF's ability to correctly identify the mounting risks [as the crisis developed] was hindered by a high degree of groupthink.'' [75]

Other studies suggest that increased diversity reduces groupthink and leads to robust dialogue and better decision making. Dallas (2002) observed that ''heterogeneous groups share conflicting opinions, knowledge, and perspectives that result in a more thorough consideration of a wide range of interpretations, alternatives, and consequences.'' [76] Bernile et al. (2017) found that ''diversity in the board of directors reduces stock return volatility, which is consistent with diverse backgrounds working as a governance mechanism, moderating decisions, and alleviating problems associated with 'groupthink.''' [77] Dhir (2015) concluded that gender diversity may ''promote cognitive diversity and constructive conflict in the boardroom.'' [78] After interviewing 23 directors about their experience with Norway's board gender mandate, he observed:

> First, many respondents contended that gender diversity promotes enhanced dialogue. Interviewees frequently spoke of their belief that heterogeneity has resulted in: (1) Higher quality boardroom discussions; (2) broader discussions that consider a wide range of angles or viewpoints; (3) deeper or more thorough discussions; (4) more frequent and lengthier discussions; (5) better informed discussions; (6) discussions that are more frequently brought inside the boardroom (as opposed to being held in spaces outside the boardroom, either exclusively or in addition to inside the boardroom); or (7) discussions in which items that directors previously took for granted are drawn out and addressed—where the implicit becomes explicit. Second, and intimately related, many interviewees indicated that diversification has led to (or has the potential to lead to) better decision making processes and/or final decisions.[79]

Investors also have emphasized the importance of diversity in decision making. A group of institutional investors charged with overseeing state investments and the retirement savings of public employees asserted that ''board members who possess a variety of viewpoints may raise different ideas and encourage a full airing of dissenting views. Such a broad pool of talent can be assembled when potential board candidates are not limited by gender, race, or ethnicity.'' [80]

Nasdaq believes that cognitive diversity is particularly important on boards because in their advisory role, especially related to corporate strategy, ''the 'output' that boards produce is entirely cognitive in nature.'' [81] While in 1999, Forbes and Milliken characterized boards as ''large, elite, and episodic decision making groups that face complex tasks pertaining to strategic-issue processing,'' [82] over the past two decades, their role has evolved; boards are now more active, frequent advisors on areas such as cybersecurity, social media, and environmental, social and governance (''ESG'') issues such as climate change and racial and gender

[67] *See* David Abad et al., *Does Gender Diversity on Corporate Boards Reduce Information Asymmetry in Equity Markets?* 20(3) BRQ Business Research Quarterly 192, 202 (July 2017) (analyzing 531 company-year observations from 2004 to 2009 of non-financial companies traded on the electronic trading platform of the Spanish Stock Exchange (SIBE)).

[68] *See* Adams and Ferreira, *supra* note 42, at 292.

[69] *See* Maria Encarnacion Lucas-Perez et al., *Women on the Board and Managers' Pay: Evidence from Spain,* 129 J. Bus. Ethics 285 (April 2014).

[70] *Id.*

[71] *See* James D. Westphal and Edward J. Zajac, *Who Shall Govern? CEO/Board Power, Demographic Similarity, and New Director Selection,* 40(1) Admin. Sci. Q. 60, 77 (March 1995).

[72] *See* Wahid, *supra* note 59, at 5.

[73] *See* Proxy Disclosure Enhancements, 74 FR 68,334, 68,355 (Dec. 23, 2009).

[74] *See* Daniel P. Forbes and Frances J. Milliken, *Cognition and Corporate Governance: Understanding Boards of Directors as Strategic Decision-Making Groups,* 24(3) Acad. Mgmt. Rev. 489, 496 (Jul. 1999).

[75] *See* International Monetary Fund, *IMF Performance in the Run-Up to the Financial and Economic Crisis* (August 2011), available at: *https://www.elibrary.imf.org/view/IMF017/11570-9781616350789/11570-9781616350789/ch04.xml?language=en&redirect=true* (''The evaluation found that incentives were not well aligned to foster the candid exchange of ideas that is needed for good surveillance—many staff reported concerns about the consequences of expressing views contrary to those of supervisors, [m]anagement, and country authorities.'').

[76] *See* Lynne L. Dallas, *Does Corporate Law Protect the Interests of Shareholders and Other Stakeholders?: The New Managerialism and Diversity on Corporate Boards of Directors,* 76 Tul. L. Rev. 1363, 1391 (June 2002).

[77] *See* Bernile et al., *supra* note 28, at 38.

[78] *See* Aaron A. Dhir, Challenging Boardroom Diversity: Corporate Law, Governance, and Diversity 150 (2015) (emphasis removed) (sample included 23 directors of Norwegian corporate boards, representing an aggregate of 95 board appointments at more than 70 corporations).

[79] *Id.* at 124 (emphasis removed).

[80] *See* Petition for Amendment of Proxy Rule (March 31, 2015), available at: *https://www.sec.gov/rules/petitions/2015/petn4-682.pdf.*

[81] *See* Forbes and Milliken, *supra* note 74, at 492.

[82] *Id.*

inequality. Nasdaq believes that boards comprised of directors from diverse backgrounds enhance investor confidence by ensuring that board deliberations include the perspectives of more than one demographic group, leading to more robust dialogue and better decision making.

III. Current State of Board Diversity and Causes of Underrepresentation on Boards

While the above studies suggest a positive association between board diversity, company performance, investor protections, and decision making, there is a noticeable lack of diversity among U.S. public companies. Nasdaq is a global organization and operates in many countries around the world that already have implemented diversity-focused directives. In fact, Nasdaq-listed companies in Europe already are subject to diversity requirements.[83] This first-hand experience provides Nasdaq with a unique perspective to incorporate global best practices into its proposal to advance diversity on U.S. corporate boards. Given that the U.S. ranks 53rd in board gender diversity, according to the World Economic Forum in its 2020 Global Gender Gap Report, Nasdaq believes advancing board diversity in the U.S. is a critical business and market imperative. This same report also found that ''American women still struggle to enter the very top business positions: only 21.7% of corporate managing board members are women.'' [84] As of 2019, women directors held 19% of Russell 3000 seats (up from 16% in 2018).[85] In comparison, women hold more than 30% of board seats in Norway, France, Sweden and Finland.[86] At the current pace, the U.S. GAO estimates that it could take up to 34 years for U.S. companies to achieve gender parity on their boards.[87]

Progress toward greater racial and ethnic diversity in U.S. company boardrooms has been even slower. Over the past ten years, the percentage of African American/Black directors at Fortune 500 companies has remained between 7 and 9%, while the percentage of women directors has grown from 16 to 23%.[88] In 2019, only 10% of board seats at Russell 3000 companies were held by racial minorities, reflecting an incremental increase from 8% in 2008.[89] Among Fortune 500 companies in 2018, there were fewer than 20 directors who publicly self-identified as LGBT+, and only nine companies reported considering sexual orientation and/or gender identity when identifying director nominees.[90]

Women and minority directors combined accounted for 34% of Fortune 500 board seats in 2018.[91] While women of color represent 18% of the U.S. population, they held only 4.6% of Fortune 500 board seats in 2018.[92] Male underrepresented minorities held 11.5% of board seats at Fortune 500 companies in 2018, compared to 66% of board seats held by Caucasian/White men. Overall in 2018, 83.9% of board seats among Fortune 500 companies were held by Caucasian/White individuals (who represent 60.1% of the U.S. population), 8.6% by African American/Black individuals (who represent 13% of the U.S. population), 3.8% by Hispanic/Latino(a) individuals (who represent 19% of the U.S. population) and 3.7% by Asian/Pacific Islander individuals (who represent 6% of the U.S. population).[93] In its analysis of Russell 3000 companies, 2020 Women on Boards concluded that ''larger companies do better with their diversity efforts than smaller companies.'' [94]

Based on the limited information that is available, Nasdaq believes a supermajority of listed companies have made notable strides to improve gender diversity in the boardroom and have at least one woman on the board. Nasdaq also believes that listed companies are diligently working to add directors with other diverse attributes, although consistent with other studies of U.S. companies, Nasdaq believes the pace of progress, in this regard, is happening more gradually. Thus, and for the reasons discussed in this Section II.A.1.III, Nasdaq has concluded that a regulatory approach to encouraging greater diversity and data transparency would be beneficial.

Nasdaq reviewed academic studies on the causes of underrepresentation on boards and the approaches taken by other jurisdictions to remedy underrepresentation. Those studies suggest that the traditional director candidate selection process may create barriers to considering qualified diverse candidates for board positions. Dhir (2015) explains that ''[t]he presence of unconscious bias in the board appointment process, coupled with closed social networks, generates a complex set of barriers for diverse directors; these are the 'phantoms' that prevent entry.'' [95] In 2011, the Davies Review found that ''informal networks influential in board appointments'' contribute to the underrepresentation of women in the boardrooms of U.K. listed companies.[96] In 2017, the Parker Review acknowledged that ''as is the case with gender, people of colour within the UK have historically not had the same opportunities as many mainstream candidates to develop the skills, networks and senior leadership experience desired in a FTSE Boardroom.'' [97] In 2020, the United Kingdom Financial Reporting Council commissioned a report to analyze barriers to LGBTQ+ inclusion and promotion in the workplace. Leaders who self-identified as LGBTQ+ expressed concerns about the current

[83] On Nasdaq's Nordic and Baltic exchanges, large companies must comply with EU Directive 2014/95/EU (the ''EU Directive''), as implemented by each member state, which requires companies to disclose a board diversity policy with measurable objectives (including gender), or explain why they do not have such a policy. On Nasdaq Vilnius, companies are also required to comply with the Nasdaq Corporate Governance Code for Listed Companies or explain why they do not, which requires companies to consider diversity and seek gender equality on the board. Similarly, on Nasdaq Copenhagen, companies are required to comply with the Danish Corporate Governance Recommendations or explain why they do not, which requires companies to adopt and disclose a diversity policy that considers gender, age and international experience. On Nasdaq Iceland, listed companies must have at least 40% women on their board (a government requirement) and comply with the EU Directive.

[84] *See* World Economic Forum, *Global Gender Gap Report 2020* 33 (2019), available at: *http://www3.weforum.org/docs/WEF_GGGR_2020.pdf.*

[85] *See* Kosmas Papadopoulos, ISS Analytics, *U.S. Board Diversity Trends in 2019* 4–5 (May 31, 2019), available at: *https://www.issgovernance.com/file/publications/ISS_US-Board-Diversity-Trends-2019.pdf.*

[86] *See* Deloitte, *Women in the Boardroom: A global perspective* (6th ed. 2019), available at: *https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Risk/gx-risk-women-in-the-boardroom-sixth-edition.pdf.*

[87] *See* GAO Report, *supra* note 44.

[88] *See* Russell Reynolds, *Ethnic & Gender Diversity on US Public Company Boards* 6 (September 8, 2020).

[89] *See* Papadopoulous, *supra* note 85, at 5.

[90] *See* Out Leadership, *supra* note 35.

[91] *See* Deloitte, *Missing Pieces Report: The 2018 Board Diversity Census of Women and Minorities on Fortune 500 Boards* 9 (2018), available at: *https://www2.deloitte.com/content/dam/Deloitte/us/Documents/center-for-board-effectiveness/us-cbe-missing-pieces-report-2018-board-diversity-census.pdf.*

[92] *See* Catalyst, *Too Few Women of Color on Boards: Statistics and Solutions* (Jan. 31, 2020), *https://www.catalyst.org/research/women-minorities-corporate-boards/.*

[93] *See* Deloitte, *Missing Pieces Report, supra* note 91; United States Census Bureau, *QuickFacts,* available at: *https://www.census.gov/quickfacts/fact/table/US/PST045219.*

[94] *See 2020 Women On Boards Gender Diversity Index* 4 (2019), available at: *https://2020wob.com/wp-content/uploads/2019/10/2020WOB_Gender_Diversity_Index_Report_Oct2019.pdf.*

[95] *See* Dhir, *supra* note 78, at 47.

[96] *See Women on Boards* 17 (Feb. 2011), available at: *https://ftsewomenleaders.com/wp-content/uploads/2015/08/women-on-boards-review.pdf.*

[97] *See* Sir John Parker, *A Report into the Ethnic Diversity of UK Boards* 38 (Oct. 12, 2017), available at: *https://assets.ey.com/content/dam/ey-sites/ey-com/en_uk/news/2020/02/ey-parker-review-2017-report-final.pdf.*

board nomination process, which includes ''relying on personal recommendations without transparent competition or due process [and] informal 'interviewing' outside the selection process.'' [98]

These concerns are not unique to the United Kingdom. The U.S. GAO (2015) found that women's representation on corporate boards may be hindered by directors' tendencies to ''rely on their personal networks to identify new board candidates.'' [99] Vell (2017) found that ''92% of board seats [of public U.S. and Canadian technology companies] are filled through networking, and women have less access to these networks.'' [100] Deloitte and the Society for Corporate Governance (2019) found that this is also common in other industries including media, communications, energy, consumer products, financial services and life sciences.[101] They observed that although 94% of companies surveyed were looking to increase diversity among their boards, 77% of those boards looked to referrals from current directors when identifying diverse director candidates, suggesting that ''networking is still key to board succession.'' [102] Dhir (2015), in a qualitative study of Norwegian directors, observed that ''[b]oard seats tend to be filled by directors engaging their networks, and the resulting appointees tend to be of the same socio-demographic background.'' [103]

Another contributing factor may be the traditional experience sought in director nominees. Rhode & Packel (2014) observed that:

> One of the most common reasons for the underrepresentation of women and minorities on corporate boards is their underrepresentation in the traditional pipeline to board service. The primary route to board directorship has long been through experience as a CEO of a public corporation. . . . Given the low representation of women and minorities in top executive positions, their talents are likely to be underutilized if selection criteria are not broadened.[104]

Hillman et al. (2002) found that while white male directors of public companies were more likely to have current or former experience as a CEO, senior manager or director, African-American and white women directors were more likely to have specialized expertise in law, finance, banking, public relations or marketing, or community influence from positions in politics, academia or clergy.[105] Dhir (2015) suggests that ''[c]onsidering persons from other, non-management pools, such as academia, legal and accounting practice, the not-for-profit sector and politics, may help create a broader pool of diverse candidates.'' [106] Directors surveyed by the U.S. GAO also ''suggested, for example, that boards recruit high performing women in other senior executive level positions, or look for qualified female candidates in academia or the nonprofit and government sectors. . . . [I]f boards were to expand their director searches beyond CEOs more women might be included in the candidate pool.'' [107]

Investors have begun calling for greater transparency surrounding ethnic diversity on company boards, and in the past several months as the U.S. has seen an uprising in the racial justice movement, there has been an increase in the number of African Americans appointed to Russell 3000 corporate boards.[108] In a five-month span, 130 directors appointed were African American, in comparison to the 38 African American directors who were appointed in the preceding five months.[109] Although tracking the acceleration in board diversity is feasible for some Russell 3000 companies, many of the companies do not disclose the racial makeup of the board, making it impossible to more broadly assess the impact of recent events on board diversity.

IV. Stakeholder Perspectives

To gain a better understanding of the current state of board diversity, benefits of diversity, causes of underrepresentation on boards and potential remedies to address underrepresentation, Nasdaq spoke with leaders representing a broad spectrum of market participants and other stakeholders. Nasdaq sought their perspectives to inform its analysis of whether the proposed rule changes would promote the public interest and protection of investors without unduly burdening competition or conflicting with existing securities laws. The group included representatives from the investor, regulatory, investment banking, venture capital and legal communities. Nasdaq also spoke with leaders of civil rights and corporate governance organizations, and organizations representing the interests of private and public companies, including Nasdaq-listed companies. Specifically, Nasdaq obtained their views on:

- The current state of board diversity in the U.S.;
- the inherent value of board diversity;
- increasing pressure from legislators and investors to improve diverse representation on boards and board diversity disclosure;
- whether a listing rule related to board diversity is in the public interest;
- how to define a ''diverse'' director; and
- the benefits and challenges of various approaches to improving board diversity disclosures and increasing diverse representation on boards, including mandates and disclosure-based models.

The discussions revealed strong support for disclosure requirements that would standardize the reporting of board diversity statistics. The majority of organizations also were in agreement that companies would benefit from a regulatory impetus to drive meaningful and systemic change in board diversity, and that a disclosure-based approach would be more palatable to the U.S. business community than a mandate. While many organizations recognized that mandates can accelerate the rate of change, they expressed that a disclosure-based approach is less controversial and would spur companies to take action and achieve the same results. Business leaders also

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[98] *See* Catriona Hay et al., The Financial Reporting Council, *Building more open business* 25 (2020), available at: *https://www.frc.org.uk/getattachment/19f3b216-bd45-4d46-af2f-f191f5bf4a07/The-Good-Side-x-Financial-Reporting-Council-1811-AMENDED.pdf.*

[99] *See* GAO Report, *supra* note 44, at 15.

[100] *See* Vell Executive Search, *Women Board Members in Tech Companies: Strategies for Building High Performing Diverse Boards* 6 (2017), available at: *https://www.vell.com/images/pdf/VELL%20Report%20Women%20Board%20Members%20on%20Tech%20Boards%202017%203%2029.pdf.*

[101] *See* Deloitte and the Society of Corporate Governance, *Board Practices Report: Common threads across boardrooms* 5 (2019), available at: *https://higherlogicdownload.s3.amazonaws.com/GOVERNANCEPROFESSIONALS/a8892c7c-6297-4149-b9fc-378577d0b150/UploadedImages/1202241_2018_Board_Practices_Report_FINAL.pdf.*

[102] *Id.* at 6.

[103] *See* Dhir, *supra* note 78, at 52.

[104] *See* Deborah Rhode and Amanda K. Packel, *Diversity on Corporate Boards: How Much Difference Does Difference Make?,* 39(2) Del. J. Corp. L. 377, 402–403 (2014); *see also* Dhir, *supra* note 78, at 39 (''[T]here is an apparent preference for either CEOs (whether current or retired) or senior management who have experience at the helm of a particular business stream or unit. . . . The fact that far fewer women than men have been CEOs has a potentially devastating effect on access to the boardroom, which in turn can have an effect on the number of women who rise to the level of CEO and to the executive suite.'').

[105] *See* Amy J. Hillman et al., *Women and Racial Minorities in the Boardroom: How Do Directors Differ?,* 28(6) J. Mgmt. 747, 749, 754 (2002).

[106] *See* Dhir, *supra* note 78, at 42.

[107] *See* GAO Report *supra* note 44, at 18.

[108] *See* Leslie P. Norton, *The Number of Black Board Members Surged After George Floyd's Death, Barron's,* Oct. 27, 2020, available at: *https://www.barrons.com/articles/after-george-floyds-death-the-number-of-black-board-members-surges-51603809011.*

[109] *Id.*

expressed concern that smaller companies would require flexibility and support to comply with any time-sensitive requirements to add diverse directors. Some stakeholders highlighted additional challenges that smaller companies, and companies in certain industries, may face finding diverse board members. Leaders from across the spectrum of stakeholders that Nasdaq surveyed reinforced the notion that if companies recruit by skill set and expertise rather than title, then they will find there is more than enough diverse talent to satisfy demand. Leaders from the legal community emphasized that any proposed rule that imposed additional burdens beyond, or is inconsistent with, existing securities laws—by, for example, requiring companies to adopt a diversity policy or include disclosure solely in their proxy statements—would present an additional burden and potentially more legal liability for listed companies.

V. U.S. Regulatory Framework

As detailed above, diversity has been the topic of a growing number of studies over the past decade and, in recent years, some investors have been increasingly advocating for greater diversity among directors of public companies.[110] Over the past year, the social justice movement has underscored the importance of having diverse perspectives and representation at all levels of decision-making, including on public company boards. In recent years, diversity has become increasingly important to the public, including institutional investors, pension funds and other stakeholders who believe that board diversity enhances board performance and is an important factor in the voting decisions of some investors.[111] Legislators increasingly are taking action to encourage corporations to diversify their boards and improve diversity disclosures.[112]

a. SEC Diversity Disclosure Requirements—Background

In 2009, the Commission sought comment on whether to amend Item 407(c)(2)(vi) of Regulation S–K to require disclosure of whether a nominating committee considers diversity when selecting a director for a position on the board.[113] The Commission received more than 130 comment letters on its proposal. According to a University of Dayton Law Review analysis of those comment letters, most were submitted by groups with a specific interest in diversity, or by institutional investors, including mutual funds, pension funds, and socially responsible investment funds.[114] Further, the analysis showed that 56 commenters addressed the issue of diversity disclosures, and only 5 of those 56 commenters did not favor such disclosure.[115] Twenty-seven of the 56 mentioned gender diversity, 18 mentioned racial diversity, and 13 mentioned ethnic diversity. However, neither the proposed rule nor the final rule defined diversity.[116]

Ten years after its adoption of board diversity disclosure rules, the Commission revisited the rules by establishing new Compliance and Disclosure Interpretations (''C&DI''). However, the Commission did not provide a definition of diversity, and therefore issuers currently are not required to disclose the race, ethnicity or gender of their directors or nominees.

Currently, Item 401(e)(1) of Regulation S–K requires a company to ''briefly discuss the specific experience, qualifications, attributes or skills that led to the conclusion that the person should serve as a director.'' [117] The C&DI clarifies that if a board considered a director's self-identified diversity characteristics (*e.g.,* race, gender, ethnicity, religion, nationality, disability, sexual orientation or cultural background) during the nomination process, and the individual consents to disclose those diverse characteristics, the Commission ''would expect that the company's discussion required by Item 401 would include, but not necessarily be limited to, identifying those characteristics and how they were considered.'' [118]

Rather than providing a specific definition of diversity, the C&DI provides a non-exhaustive list of examples of diverse characteristics that a company could consider for purposes of Item 401(e)(1), including ''race, gender, ethnicity, religion, nationality, disability, sexual orientation, or cultural background.'' [119] Additionally, the Commission stated that any description of a company's diversity policy would be expected to include ''a discussion of how the company considers the self-identified diversity attributes of nominees as well as any other qualifications its diversity policy takes into account, such as diverse work experiences, military service, or socio-economic or demographic characteristics.'' [120]

Item 407(c)(2)(vi) of Regulation S–K requires proxy disclosure regarding whether diversity is considered when identifying director nominees and, if so, how. In addition, if the board or nominations committee has adopted a diversity policy, the company must describe how the policy is implemented and its effectiveness is assessed.[121] When adopting Item 407(c)(2)(vi), the Commission explained:

We recognize that companies may define diversity in various ways, reflecting different perspectives. For instance, some companies may conceptualize diversity expansively to

[110] In 2009, when the Commission proposed enhancements to proxy disclosures, including addressing board diversity disclosures, the Commission received over 130 comment letters related to its proposal, including from corporations, pension funds, professional associations, trade unions, accounting firms, law firms, consultants, academics, individual investors and other interested parties. *See* Proxy Disclosure Enhancements, 74 FR at 68,335; *see also* David A. Katz and Laura McIntosh, *Raising the Stakes for Board Diversity,* Law.com (July 22, 2020), available at: *https://www.law.com/newyorklawjournal/2020/07/22/raising-the-stakes-for-board-diversity/?slreturn=20201017021522*; Office of the Illinois State Treasurer, *The Investment Case For Board Diversity: A Review of the Academic and Practitioner Research on the Value of Gender and Racial/Ethnic Board Diversity for Investors* 7 (Oct. 2020), available at: *https://illinoistreasurergovprod.blob.core.usgovcloudapi.net/twocms/media/doc/il%20treasurer%20white%20paper%20-%20the%20investment%20case%20for%20board%20diversity%20(oct%202020).pdf.*

[111] *See* Comments on Proposed Rule: Proxy Disclosure and Solicitation Enhancements, available at: *https://www.sec.gov/comments/s7-13-09/s71309.shtml. See also* CGLytics, *Diversity on the Board? Metrics Used by Fortune 100 Companies* (June 29, 2020), available at: *https://www.cglytics.com/diversity-on-the-board-metrics-of-fortune-100-companies/*; Office of the Illinois State Treasurer, *supra* note 110.

[112] For example, California requires companies headquartered in the state to have at least one director who self-identifies as a Female and one director from an Underrepresented Community. *See* Cal. S.B. 826 (Sept. 30, 2018); Cal. A.B. 979 (Sept. 30, 2020). Washington requires companies headquartered in the state to have at least 25% women on the board by 2022 or provide certain disclosures. *See* Wash. Subst. S.B. 6037 (June 11, 2020). At least eleven states have proposed diversity-related requirements. *See* Hatcher and Latham, *supra* note 11.

[113] *See* Proxy Disclosure and Solicitation Enhancements, 74 FR 35,076, 35,084 (July 17, 2009) (proposed rule).

[114] *See* Thomas Lee Hazen and Lissa Lamkin Broome, *Board Diversity and Proxy Disclosure,* 37:1 Univ. Dayton L. Review 41, 51, n. 82 (citing the comment letters).

[115] In the five comments that opposed diversity disclosure, three stated that diversity was an important value. *See* Comments on Proposed Rule, *supra* note 111; *see also* Hazen and Broome, *supra* note 114, at 54 n.88 (citing the 56 comment letters).

[116] *See* Hazen and Broome, *supra* note 114, at 53 n. 84–86.

[117] *See* 17 CFR 229.401(e)(1).

[118] *See* Securities and Exchange Commission, Regulation S–K Compliance & Disclosure Interpretations (Sept. 21, 2020), available at: *https://www.sec.gov/divisions/corpfin/guidance/regs-kinterp.htm.*

[119] *Id.*

[120] *Id.*

[121] *See* 17 CFR 229.407(c)(2)(vi).

include differences of viewpoint, professional experience, education, skill and other individual qualities and attributes that contribute to board heterogeneity, while others may focus on diversity concepts such as race, gender and national origin. We believe that for purposes of this disclosure requirement, companies should be allowed to define diversity in ways that they consider appropriate. As a result we have not defined diversity in the amendments.[122]

Moreover, Item 407(c)(2)(vi) does not require companies to adopt a formal policy and does not require them to explain why they have not. It also does not require public disclosure of board-level diversity statistics.

b. Complaints Surrounding Current Diversity Disclosure Requirements

Given the broad latitude afforded to companies by the Commission's rules related to board diversity and proxy disclosure, current reporting of board-level diversity statistics has been significantly unreliable and unusable to investors. This has been due to myriad data collection challenges, including the scarcity of reported information, the lack of uniformity in the information that is disclosed and inconsistencies in the definitions of diversity characteristics across companies.[123] The heightened national discourse around diversity and mounting grievances from investors surrounding transparency on board diversity prompted Nasdaq to examine the state of board diversity among its listed companies. While conducting that research, Nasdaq identified a number of key challenges, such as: (1) Inconsistent disclosure and definitions of diversity across companies; (2) limited data on diverse characteristics outside of gender; (3) inconsistent or no disclosure of a director's race, ethnicity, or other diversity attributes (*e.g.,* nationality); (4) difficult-to-extract data because statistics are often embedded in graphics; and (5) aggregation of information, making it difficult to separate gender from other categories of diversity. Investors and data analysts have raised similar criticisms.

As the Illinois Treasurer observed, the paucity of data on race and ethnicity creates barriers to investment analysis, due diligence and academic study.[124] For example, the scarcity of such data is an impediment to academics who want to study the performance impact of racially diverse boards.[125] Nasdaq is concerned that investors also face the many data collection challenges Nasdaq encountered, rendering current diversity disclosures unreliable, unusable, and insufficient to inform investment and voting decisions. Commissioner Allison Herren Lee expressed similar concerns, stating that the current SEC disclosure requirements have ''led to spotty information that is not standardized, not consistent period to period, not comparable across companies, and not necessarily reliable. . . . And the current state of disclosure reveals the shortcomings of a principles-based materiality regime in this area.'' [126]

Some stakeholders believe there is a correlation between companies that disclose the gender, racial and ethnic composition of their board and the number of diverse directors on those companies' boards.[127] Currently, the lack of reliable and consistent data makes it difficult to measure diversity in the boardroom, and a common set of standards for diversity definitions and disclosure format is greatly needed. At present, U.S. companies must navigate a complex patchwork of federal and state regulations and disclosure requirements. The limited disclosure currently provided voluntarily, which is primarily focused on gender (due in part to that data being the most readily available), fails to provide the full scope of a board's diverse characteristics.[128] It is difficult to improve what one cannot accurately measure. This lack of transparency is impacting investors who are increasingly basing public advocacy, proxy voting and direct shareholder-company engagement decisions on board diversity considerations.[129]

c. Support for Updating Diversity Disclosure Requirements

Nasdaq's surveys of investors and reviews of their disclosed policies and actions show that board diversity is a priority when assessing companies, and investors report, in some cases, relying on intuition when there is a lack of empirical, evidenced-based data. Furthermore, the continued growth of ESG investing raises the importance of quality data, given the data-driven nature of investment products such as diversity-specific indices and broader ESG funds.

Investors have a unique platform from which to engage and influence a company's position on important topics like diversity. Similarly, Nasdaq, like other self-regulatory organizations, is uniquely positioned to establish practices that will assist in carrying out Nasdaq's mandate to protect investors and remove impediments from the market. Various stakeholders, including Nasdaq, believe that clear and concise annual disclosure of board diversity information that disaggregates the data by race, ethnicity, gender identity and sexual orientation will provide the public, including key stakeholders, with a better sense of a company's approach to improving corporate diversity and the support needed to effectuate any changes. Required disclosures also would eliminate the number of shareholder proposals asking for these key metrics and the need for companies to respond to multiple investor requests for information.[130] Moreover, companies manage issues more closely and demonstrate greater progress when data is available.[131]

In 2015, nine large public pension funds who collectively supervised $1.12 trillion in assets at the time petitioned the Commission to require registrants to disclose information related to, among other things, the gender, racial, and ethnic diversity of the registrant's board nominees.[132] In 2017, Human Capital Management Coalition, which described itself as a group of institutional investors with $2.8 trillion in assets at the time, made a similar petition to the Commission.[133] More recently, in October 2020, the Illinois Treasurer spearheaded an initiative along with twenty other investor organizations, asking for all companies in the Russell

[122] *See* Proxy Disclosure Enhancements, 74 FR at 68,344.

[123] *See* Petition for Rulemaking (July 6, 2017), available at: *https://www.sec.gov/rules/petitions/2017/petn4-711.pdf.*

[124] *See* Press Release, *Illinois State Treasurer Frerichs Calls on Russell 3000 Companies to Disclose Diversity Data* (Oct. 28, 2020), available at *https://illinoistreasurer govprod.blob.core.usgovcloudapi.net/twocms/media/doc/october2020_russell3000.pdf.*

[125] *See* Office of Illinois State Treasurer, *supra* note 110, at 3–4.

[126] *See* Lee, *supra* note 22.

[127] *See* Proxy Disclosure Enhancements, 74 FR at 68,355 (''Although the[se] amendments are not intended to steer behavior, diversity policy disclosure may also induce beneficial changes in board composition. A board may determine, in connection with preparing its disclosure, that it is beneficial to disclose and follow a policy of seeking diversity.''); *see also* Office of Illinois State Treasurer, *supra* note 110, at 3.

[128] *See, e.g.,* CGLytics, *supra* note 111, at *https://www.cglytics.com/diversity-on-the-board-metrics-of-fortune-100-companies/;* Petition for Amendment of Proxy Rule, *supra* note 80; Office of Illinois State Treasurer, *supra* note 110.

[129] *See* Office of the Illinois State Treasurer, *Russell 3000 Board Diversity Disclosure Initiative, https://www.illinoistreasurer.gov/Financial_Institutions/Equity,_Diversity__Inclusion/Russell_3000_Board_Diversity_Disclosure_Initiative* (last accessed Nov. 25, 2020).

[130] *See* Petition for Rulemaking, *supra* note 123, at 2.

[131] *See, e.g.,* Gwen Le Berre, Parametric, *Investors Need Data to Make Diversity a Reality* (Aug. 24, 2020), *https://www.parametricportfolio.com/blog/investors-need-data-to-make-diversity-a-reality.*

[132] *See* Petition for Amendment of Proxy Rule, *supra* note 80.

[133] *See* Petition for Rulemaking, *supra* note 123.

3000 Index to disclose the composition of their board, including each board member's gender, race and ethnicity.[134]

The largest proxy advisory firms have aligned their voting policies to encourage increased board diversity disclosure. Institutional Shareholder Services (''ISS''), recently adopted a new voting policy under which it will identify boards of companies in the Russell 3000 or S&P 1500 that ''lack racial and ethnic diversity (or lack disclosure of such)'' in 2021 and, beginning in 2022, will recommend voting against the chair of the nominating committee of such companies. The stated goal of the policy is ''helping investors identify companies with which they may wish to engage and to foster dialogue between investors and companies on this topic.'' [135] In 2017, proxy advisory firm Glass Lewis announced a policy regarding board gender diversity that took effect in 2019. Glass Lewis generally recommends voting against the nominating committee chair of a board that has no female members, and when making such a recommendation, the firm closely examines the company's disclosure of its board diversity considerations and other relevant contextual factors.[136] On November 24, 2020, Glass Lewis announced the publication of its 2021 Proxy Voting Policy Guidelines, which expand its board gender diversity policy to vote against nominating chairs if there are fewer than two female directors, beginning in 2022.[137] Most notably, beginning with the 2021 proxy season, the company will include an assessment report of company proxy disclosures relating to board diversity, skills and the director nomination process for companies in the S&P 500 index. According to Glass Lewis, it ''will reflect how a company's proxy statement presents: (i) The board's current percentage of racial/ethnic diversity; (ii) whether the board's definition of diversity explicitly includes gender and/or race/ethnicity; (iii) whether the board has adopted a policy requiring women and minorities to be included in the initial pool of candidates when selecting new director nominees (aka 'Rooney Rule'); and (iv) board skills disclosure.'' [138]

Congress and members of the Commission also have weighed in on the importance of improving board transparency. In 2017, Representative Carolyn Maloney introduced the ''Gender Diversity in Corporate Leadership Act of 2017,'' which proposed requiring public companies to provide proxy disclosure regarding the gender diversity of the board of directors and nominees.[139] In November 2019, the U.S. House of Representatives, with bipartisan support, passed the ''Corporate Governance Through Diversity Act of 2019,'' which requires certain registrants annually to disclose the racial, ethnic, and gender composition of their boards and executive officers, as well as the veteran status of any of those directors and officers, in their proxy statements.[140] The bill also requires the disclosure of any policy, plan or strategy to promote racial, ethnic, and gender diversity among these groups. Legislators have proposed a companion bill in the U.S. Senate.[141]

The Council of Institutional Investors (''CII''), U.S. Chamber of Commerce,[142] National Urban League, Office of New York State Comptroller and the National Association for the Advancement of Colored People praised the House of Representatives' for passing the 2019 legislation. According to the U.S. Chamber of Commerce's members and associations, it has become increasingly important to see improvements in board diversity.[143] Additionally, CII's General Counsel stated that the proxy statement disclosure requirement in the legislation ''could contribute to enhancing U.S. public company board consideration of diversity.'' [144]

More recently, SEC Commissioners have called for greater transparency surrounding ethnic diversity on company boards. In a September 2020 speech titled ''Diversity Matters, Disclosure Works, and the SEC Can Do More'' given at the CII Fall Conference, Commissioner Lee advocated advancing corporate diversity and for various approaches by which the Commission could promote diversity, including among other things, strengthening the C&DI's guidance related to disclosure of board candidate diversity characteristics.[145] Commissioner Lee stated:

> [The SEC has] largely declined to require diversity-related disclosure. In 2009, we adopted a requirement for companies to disclose if and how diversity is considered as a factor in the process for considering candidates for board positions, including any policies related to the consideration of diversity. In 2018, we issued guidance encouraging the disclosure of self-identified characteristics of board candidates. While I appreciate these measures, given that women of color hold just 4.6% of Fortune 500 board seats and less than one percent of Fortune 500 CEOs are Black, it's time to consider how to get investors the diversity information they need to allocate their capital wisely.[146]

VI. Nasdaq Proposal

a. Overview of Disclosure Requirements

Disclosure of information material to an investor's voting and investment decision is the bedrock of federal securities laws. The Exchange's listing rules require companies to comply with federal securities laws, including the registration requirements under the Securities Act of 1933. Once listed, companies are obligated to solicit proxies and file all annual and periodic reports with the Commission under the Act at the prescribed times.[147] In discharging its obligation to protect investors, Nasdaq monitors listed companies for compliance with those disclosure obligations, and the failure to do so results in a notice of deficiency or delisting.

Nasdaq believes it is well within the Exchange's delegated regulatory authority to propose listing rules designed to enhance transparency so long as they do not conflict with existing federal securities laws. For example, Nasdaq requires listed companies to publicly disclose compensation or other payments by third parties to a company's directors or

[134] *See* Press Release, *supra* note 124.

[135] *See* ISS Governance, *ISS Announces 2021 Benchmark Policy Updates* (November 12, 2020), available at: *https://www.issgovernance.com/iss-announces-2021-benchmark-policy-updates/*.

[136] *See* Glass Lewis, *2019 Policy Guideline Updates* (Oct. 24, 2018), available at: *https://www.glasslewis.com/2019-policy-guideline-updates-united-states-canada-shareholder-initiatives-israel/*.

[137] *See* Glass Lewis, *2021 Proxy Paper Guidelines: An Overview of the Glass Lewis Approach to Proxy Advice—United States* (2020), available at: *https://www.glasslewis.com/wp-content/uploads/2020/11/US-Voting-Guidelines-GL.pdf?hsCtaTracking=7c712e31-24fb-4a3a-b396-9e8568fa0685%7C86255695-f1f4-47cb-8dc0-e919a9a5cf5b*.

[138] *Id.*

[139] Gender Diversity in Corporate Leadership Act of 2017, H.R. 1611, 115th Cong. (2017).

[140] Improving Corporate Governance Through Diversity Act of 2019, H.R. 5084, 116th Cong. (2019).

[141] Improving Corporate Governance Through Diversity Act of 2019, S. 360, 116th Cong. (2019).

[142] *See* Letter from Various U.S. Chamber of Commerce Associations and Members to Chairman Mike Crapo and Ranking Member Sherrod Brown, U.S. House Committee on Banking, Housing, and Urban Affairs (July 27, 2020), available at: *https://www.uschamber.com/sites/default/files/200727_coalition_h.r._5084_senatesmallbusiness.pdf*.

[143] *Id.*

[144] *See* Joe Mont, *SEC, Congress seek better diversity disclosures,* Compliance Week (Feb. 20, 2019), *https://www.complianceweek.com/sec-congress-seek-better-diversity-disclosures/24802.article*.

[145] *See* Lee, *supra* note 22.

[146] *Id.* Commissioner Crenshaw also expressed disappointment with the Commission's silence on diversity. *See* Crenshaw, *supra* note 7.

[147] *See* Nasdaq Stock Market Rulebook, Rules 5250(c) and (d).

nominees, notwithstanding that such disclosure is not required by federal securities laws. In approving that proposed rule, the Commission noted:

> To the extent there are certain factual scenarios that would require disclosure not otherwise required under Commission rules, we believe that it is within the purview of a national securities exchange to impose heightened governance requirements, consistent with the Act, that are designed to improve transparency and accountability into corporate decision making and promote investor confidence in the integrity of the securities markets.[148]

Nasdaq is concerned that while investors have increasingly emphasized that they consider board diversity information to be material, the current lack of transparency and consistency makes it difficult for Nasdaq and investors to determine the state of diversity among listed companies as well as each board's philosophy regarding diversity. Investors also have voiced dissatisfaction about having to independently collect board-level data about race, ethnicity and gender identity because such investigations can be time consuming, expensive, and fraught with inaccuracies.[149] Moreover, in some instances, based on Nasdaq's own investigation, such information is either unavailable, or, if available, not comparable across companies. To the extent investors must obtain this information on their own through an imperfect process, Nasdaq is concerned that it increases information asymmetries between larger stakeholders, who are able to collect this data directly from companies, and smaller investors, who must rely on incomplete public disclosures. For all investors who take on the burden of independently obtaining the current information, there is a cost and time burden related to the data collection.

Nasdaq believes that additional disclosure regarding a board's composition and philosophy related to board diversity will improve transparency and accountability into corporate decision making. Nasdaq proposes to improve transparency regarding board diversity by requiring all listed companies to publicly disclose unbundled, consistent data utilizing a uniform, transparent framework on their website or in their proxy statement under Rule 5606. Similarly, Nasdaq proposes to promote accountability in corporate decision-making by requiring companies who do not have at least two Diverse directors on their board to provide investors with a public explanation of the board's reasons for not doing so under Rule 5605(f)(3). Nasdaq designed the proposal to avoid a conflict with existing disclosure requirements under Regulation S–K and to mitigate additional burdens for companies by providing them with flexibility to provide such disclosure on their website or in their proxy statement, and not requiring them to adopt a formal diversity policy.

Nasdaq proposes to foster consistency in board diversity data disclosure by defining ''Diverse'' under Rule 5605(f)(1) as ''an individual who self-identifies in one or more of the following categories: Female, Underrepresented Minority or LGBTQ+,'' and by adopting the following definitions under Rule 5605(f)(1):

- ''Female'' means an individual who self-identifies her gender as a woman, without regard to the individual's designated sex at birth.
- ''LGBTQ+'' means an individual who self-identifies as any of the following: lesbian, gay, bisexual, transgender or a member of the queer community.
- ''Underrepresented Minority'' means an individual who self-identifies as one or more of the following: Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, or Two or More Races or Ethnicities.

The terms in the proposed definition of ''Underrepresented Minority'' reflect the EEOC's categories and are construed in accordance with the EEOC's definitions.[150] The terms in the proposed definition of LGBTQ+ are similar to the identities defined in California's A.B. 979, described below, but have been expanded to include the queer community based on Nasdaq's consultation with stakeholders, including human rights organizations.[151]

In constructing its proposed definition of ''Diverse,'' Nasdaq considered various state and federal legislation, stakeholder sentiments and academic studies. For example, California requires public companies headquartered in the state to have at least one individual who self-identifies as a female on the board by 2019 under S.B. 826[152] and at least one director who is a member of an ''underrepresented community'' by 2021 under A.B. 979.[153] S.B. 826 defines ''Female'' as ''an individual who self-identifies her gender as a woman, without regard to the individual's designated sex at birth,'' consistent with legislation proposed by New Jersey, Michigan and Hawaii related to board gender diversity.[154] A.B. 979 considers directors from underrepresented communities to be individuals who self-identify as Black, African American, Hispanic, Latino, Asian, Pacific Islander, Native American, Native Hawaiian or Alaska Native, or as gay, lesbian, bisexual or transgender. Since S.B. 826 was passed, 669 women have joined public company boards in the state and the number of public companies with all male boards has declined from 30% in 2018 to 3% in 2020.[155]

The state of Washington requires public companies whose boards are not comprised of at least 25% directors who self-identify as women by January 1, 2022 to provide public disclosures related to the board's consideration of ''diverse groups'' during the director nomination process. The state considers ''diverse groups'' to include ''women, racial minorities, and historically underrepresented groups.''[156]

As discussed above, Congress has proposed legislation relating to disclosure of racial, ethnic, gender and veteran status among the company's directors. Section 342 of the Dodd-Frank Act defines ''minority'' as ''Black American, Native American, Hispanic American, and Asian American,''[157] and the Diversity Assessment Report for Entities Regulated by the SEC requires the Exchange to report workforce composition data to the SEC based on

[148] *See* Order Granting Accelerated Approval of a Proposed Rule Change, 81 FR 44,400, 44,403 (July 7, 2016).

[149] *See* Petition for Amendment of Proxy Rule, *supra* note 80, at 2.

[150] While the EEO–1 report refers to ''Hispanic or Latino'' rather than Latinx, Nasdaq proposes to use the term Latinx to apply broadly to all gendered and gender-neutral forms that may be used by individuals of Latin American heritage, including individuals who self-identify as Latino/a/e.

[151] Further, Nasdaq agrees with the United Kingdom Financial Reporting Council that the acronym LGBTQ+ ''does not attempt to exclude other groups, nor does it imply that the experiences of people under its umbrella are the same.'' *See* Hay et al., *supra* note 98, at 14.

[152] *See* Cal. S.B. 826, *supra* note 112.

[153] *See* Cal. A.B. 979, *supra* note 112.

[154] *See* Cal. S.B. 826, *supra* note 112. *See also* N.J. Senate No. 3469, § 3(b)(2) (2019); Mich. S.B. 115, § 505a(2)(b) (2019); Haw. H.B. 2720, § 414–1(b)(2) (2020).

[155] *See* California Partners Project, *Claim Your Seat: A Progress Report on Women's Representation on California Corporate Boards* 4 (2020), available at: *https://www.calpartnersproject.org/claimyourseat.*

[156] *See* Wash. Subst. S.B. 6037, *supra* note 112. At least 11 states have proposed diversity-related requirements. *See* Hatcher and Latham, *supra* note 11.

[157] *See* 12 U.S.C. 5452(g)(3) and Public Law 101–73 § 1204(c)(3).

the EEOC's categories.[158] Most companies are required by law to provide similar workforce data to the EEOC through the EEO–1 Report, which requires employers to report statistical data related to race, ethnicity and gender to the EEOC.[159]

Nasdaq has designed the proposed rule to require all companies to provide consistent, comparable data under Rule 5606 by utilizing the existing EEO–1 reporting categories that companies are already familiar with, and by requiring companies to have, or publicly explain why they do not have, at least two directors who are diverse in terms of race, ethnicity, sexual orientation or gender identity under Rule 5605(f)(2). While the EEO–1 report does not currently include sexual orientation or gender identity, Nasdaq believes it is reasonable and in the public interest to include a reporting category for LGBTQ+ status in recognition of the U.S. Supreme Court's recent decision in *Bostock* v. *Clayton County* that sexual orientation and gender identity are ''inextricably'' intertwined with sex.[160]

The proposal does not preclude companies from considering additional diverse attributes, such as nationality, disability, or veteran status in selecting board members; however, the company would still have to provide the required disclosure under Rule 5605(f)(3) if the company does not also have at least two directors who are otherwise considered Diverse under Rule 5605(f)(1). Nor would the proposal prevent companies from disclosing information related to other diverse attributes of board members beyond those highlighted in the rule if they felt such disclosure would benefit investors. Nasdaq believes such disclosure would provide investors with additional information about the company's philosophy regarding broader diversity characteristics.

Overall, Nasdaq believes the proposal will enhance investor confidence that all listed companies are considering diversity of race, ethnicity, sexual orientation and gender identity in the context of selecting directors. Investors will be confident that board discussions at listed companies with at least two Diverse directors include the perspectives of more than one demographic group. They will also be confident that boardrooms without at least two Diverse directors are having a thoughtful discussion about their reasons for not doing so and publicly explaining those reasons. On balance, the proposal will advance the public interest and enhance investor confidence in the integrity of the securities markets by ensuring investors that Nasdaq is monitoring all listed companies to verify that they have at least two Diverse directors or explain why they do not, and by requiring all listed companies to provide consistent, comparable diversity disclosures.

b. Board Statistical Disclosure

Given the increased interest in, and advocacy for, improvements in board transparency related to diversity disclosure information, the Exchange is proposing to adopt new Rule 5606(a), which would require each company to publicly disclose, to the extent permitted by applicable law, information on each director's voluntary self-identified gender and racial characteristics and LGBTQ+ status.

All Nasdaq-listed companies that are subject to proposed Rule 5605(f), whether they choose to meet the diversity objectives of proposed Rule 5605(f)(2) or to explain why they do not, would be required to make the proposed Rule 5606 disclosure. This proposed rule also will assist the Exchange in assessing whether companies meet the diversity objectives of proposed Rule 5605(f). Under Rule 5606(e), Nasdaq proposes to make proposed Rule 5606 operative for listed companies one year after the SEC Approval Date of this proposal.

Pursuant to proposed Rule 5606(a), each company would be instructed to annually provide its board-level diversity data in a format substantially similar to the Board Diversity Matrix in proposed Rule 5606(a) and attached [sic] as *Exhibit 3.* The company would be required to provide the total number of directors on its board. If a director voluntarily self-identifies, each company, other than a Foreign Issuer (as defined under Rule 5605(f)(1)), would include the following in a table titled ''Board Diversity Matrix,'' in accordance with the instructions accompanying the proposed disclosure format: (1) the number of directors based on gender identity (male, female or non-binary[161]); (2) the number of directors based on race and ethnicity (African American or Black, Alaskan Native or American Indian, Asian, Hispanic or Latinx, Native Hawaiian or Pacific Islander, White, or Two or More Races or Ethnicities); and (3) the number of directors who self-identify as LGBTQ+.

Any director who chooses not to disclose a gender would be included under ''Gender Undisclosed'' and any director who chooses not to identify as any race or not to identify as LGBTQ+ would be included in the ''Undisclosed'' category at the bottom of the table. The defined terms for the race and ethnicity categories in the instructions to the Board Diversity Matrix disclosure format are substantially similar to the terms and definitions used in the EEO–1 Report.[162] LGTBQ+ is defined similarly to proposed Rule 5605(f)(1) as a person who identifies as any of the following: lesbian, gay, bisexual, transgender or a member of the queer community.

Below is an example of a Board Diversity Matrix that companies may use, which is also attached [sic] as *Exhibit 3:*

[158] *See* Securities and Exchange Commission, Diversity Assessment Report for Entities Regulated by the SEC, available at: *https://www.sec.gov/files/OMWI-DAR-FORM.pdf.*

[159] All companies with 100 or more employees are required to complete the EEO–1 Report. *See* U.S. Equal Employment Opportunity Commission, EEO–1: Who Must File, *https://www.eeoc.gov/employers/eeo-1-survey/eeo-1-who-must-file* (last accessed Nov. 27, 2020).

[160] *See Bostock* v. *Clayton Cty.,* 140 S. Ct. 1731, 1742 (2020) (''But unlike any of these other traits or actions, homosexuality and transgender status are inextricably bound up with sex. Not because homosexuality or transgender status are related to sex in some vague sense or because discrimination on these bases has some disparate impact on one sex or another, but because to discriminate on these grounds requires an employer to intentionally treat individual employees differently because of their sex.'').

[161] Although non-binary is included as a category in the proposed Board Diversity Matrix, a company would not satisfy the diversity requirement proposed by Rule 5605(f)(2) if a director self-identifies solely as non-binary.

[162] *See supra* note 159. Additionally, the EEOC does not categorize LGBTQ+ or any other sexual orientation identifier on its EEO–1 Report. The definitions of the EEO–1 race and ethnicity categories may be found in the appendix to the EEO–1 Report instructional booklet, available at *https://www.eeoc.gov/employers/eeo-1-survey/eeo-1-instruction-booklet.*

BOARD DIVERSITY MATRIX

[As of [DATE]]

Board Size:				
Total Number of Directors	#			
Gender:	Male	Female	Non-Binary	Gender undisclosed
Number of directors based on gender identity	#	#	#	#
Number of directors who identify in any of the categories below:				
African American or Black	#	#	#	#
Alaskan Native or American Indian	#	#	#	#
Asian	#	#	#	#
Hispanic or Latinx	#	#	#	#
Native Hawaiian or Pacific Islander	#	#	#	#
White	#	#	#	#
Two or More Races or Ethnicities	#	#	#	#
LGBTQ+	#			
Undisclosed	#			

Nasdaq recognizes that some Foreign Issuers, including Foreign Private Issuers as defined by the Act,[163] may have their principal executive offices located outside of the United States and in jurisdictions that may impose laws limiting or prohibiting self-identification questionnaires, particularly as they relate to race, ethnicity or LGBTQ+ status. In such countries, a Foreign Issuer may be precluded by law from requesting diversity data from its directors. Moreover, Nasdaq's definition of Underrepresented Minority proposed in Rule 5606(f)(1) may be inapplicable to a Foreign Issuer, making this Board Matrix data less relevant for such companies and not useful for investors.

As a result of these limitations, Nasdaq is proposing the option of a separate Board Diversity Matrix for Foreign Issuers. Similar to other companies, a Foreign Issuer would be required to provide the total number of directors on its board. If a director voluntarily self-identifies, the company would include the following in a table titled ''Board Diversity Matrix'': (1) The number of directors based on gender identity (male, female or non-binary [164]); (2) the number of directors who are considered underrepresented in the company's home country jurisdiction;[165] and (3) the number of directors who self-identify as LGBTQ+. An ''Underrepresented Individual in Home Country Jurisdiction'' is defined in the instructions to the Board Diversity Matrix as a person who self-identifies as an underrepresented individual based on national, racial, ethnic, indigenous, cultural, religious or linguistic identity in a Foreign Issuer's home country jurisdiction. Rule 5605(f)(2)(B)(i) also proposes the same definition for Diverse directors of Foreign Issuers.

Nasdaq is also proposing new Rule 5606(b), which would require each company to provide the disclosure required under Rule 5606(a) in either the company's proxy statement or information statement for its annual meeting for shareholders, or on the company's website. If the company elects to disclose the information on its website, the company must also submit such disclosure along with a URL link to the information through the Nasdaq Listing Center within 15 calendar days of the company's annual shareholder meeting. The proposed time period to submit the information to the Nasdaq Listing Center is aligned with the time period provided in proposed Rule 5605(f)(3) for a company to submit its explanation for why it does not have at least two Diverse directors. Disclosure of the statistical data is not in lieu of any SEC requirements for a company to disclose any required information pursuant to Regulation S–K or any other federal, state or foreign laws or regulations. As described in the instructions to the Board Diversity Matrix and Rule 5606(a), each year following the first year that a company publishes its annual Board Diversity Matrix, the company would be required to publish its data for the current and immediately prior years.

Additionally, Nasdaq is proposing Rule 5606(c), which exempts the following types of companies from proposed Rule 5606(a): acquisition companies listed under IM–5101–2; asset-backed issuers and other passive issuers (as set forth in Rule 5615(a)(1)); cooperatives (as set forth in Rule 5615(a)(2)); limited partnerships (as set forth in Rule 5615(a)(4)); management investment companies (as set forth in Rule 5615(a)(5)); issuers of non-voting preferred securities, debt securities and Derivative Securities (as set forth in Rule 5615(a)(6)); and issuers of securities listed under the Rule 5700 Series. The exemption of these companies is consistent with the approach taken by Nasdaq in Rule 5615 as it relates to certain Nasdaq corporate governance standards for board composition.

Nasdaq is also proposing Rule 5606(d) to allow for a company newly listing on Nasdaq, including a company listing in connection with a business combination under IM–5101–2, to satisfy the requirement of Rule 5606 within one year of listing on Nasdaq. The disclosure required by proposed Rule 5606(d) would be required to be included in the company's annual proxy statement or information statement for its annual meeting of shareholders or on the company's website. If the company provides such disclosure on its website, the company must also submit the disclosure and a URL link to the disclosure through the Nasdaq Listing Center no later than 15 calendar days after the company's annual shareholder meeting.

When a company does not timely provide the required disclosure, Nasdaq will notify the company that it is not in compliance with a listing requirement

[163] *See* 17 CFR 240.3b–4.

[164] Although non-binary is included as a category in the proposed Board Diversity Matrix, a company would not satisfy any aspect of the diversity requirement proposed by Rule 5605(f)(2) if a director self-identifies solely as non-binary.

[165] To clarify, although a Foreign Issuer may disclose directors that meet the requirement of Underrepresented Minority pursuant to new Rule 5605(f)(1), such disclosure may not meet the diversity objectives of new Rule 5605(f)(2)(B)(ii).

and allow the company to provide a plan to regain compliance. Consistent with deficiencies from most other rules that allow a company to submit a plan to regain compliance,[166] Nasdaq proposes to allow companies deficient under proposed Rule 5606 45 calendar days to submit a plan in accordance with Rule 5810(c)(2) to regain compliance and, based on that plan, Nasdaq can provide the company with up to 180 days to regain compliance. If the company does not do so, it would be issued a Staff Delisting Determination, which the company could appeal to a Hearings Panel pursuant to Rule 5815. Although proposed Rule 5606 is not identical to the current Commission requirements, it is similar to, and does not deviate from, the Commission's CD&I related to Items 401(e)(1) and 407(c)(2)(vi) of Regulation S–K. Moreover, the proposed rule strengthens the Commission's requirements by providing clarity to the definition of diversity and streamlining investors' desire for clear, complete and consistent disclosures. Nasdaq believes that the format of the Board Diversity Matrix and the information that it will provide offers greater transparency into a company's board composition and will enable the data to be easily aggregated across issuers.[167] Nasdaq also believes that requiring annual disclosure of the data will ensure that the information remains current and easy for investors, data analysts and other parties to track.

c. Diverse Board Representation or Explanation

Nasdaq is proposing to adopt new Rule 5605(f)(2) to require each listed company to have, or explain why it does not have, at least two members of its board of directors who are Diverse, including at least one who self-identifies as Female and one who self-identifies as an Underrepresented Minority or LGBTQ+.[168] A company does not need to provide additional public disclosures if the company discloses under Rule 5606 that it has at least two Diverse directors satisfying this requirement. The terms in the proposed definition of ''Underrepresented Minority'' reflect the EEOC's categories and are construed in accordance with the EEOC's definitions. Nasdaq has provided additional flexibility for Smaller Reporting Companies and Foreign Issuers (including Foreign Private Issuers).

Under proposed Rule 5605(f)(3), if a company satisfies the requirements of Rule 5605(f)(2) by explaining why it does not have two Diverse directors, the company must: (i) Specify the requirements of Rule 5605(f)(2) that are applicable (*e.g.,* the applicable subparagraph, the applicable diversity objectives, and the timeframe applicable to the company's market tier); and (ii) explain the reasons why it does not have two Diverse directors. Such disclosure must be provided: (i) In the company's proxy statement or information statement for its annual meeting of shareholders; or (ii) on the company's website. If the company provides such disclosure on its website, the company must also notify Nasdaq of the location where the information is available by submitting the URL link through the Nasdaq Listing Center no later than 15 calendar days after the company's annual shareholder meeting.

Nasdaq would not assess the substance of the company's explanation, but would verify that the company has provided one. If the company has not provided any explanation, or has provided an explanation that does not satisfy subparagraphs (i) and (ii) of Rule 5605(f)(3), the explanation will not satisfy the requirements of Rule 5605(f)(3). For example, it would not satisfy Rule 5605(f)(3) merely to state that ''the Company does not comply with Nasdaq's diversity rule.'' As described above, the company must specify the requirements of Rule 5605(f)(2) that are applicable and explain the reasons why it does not have two Diverse directors. For example, a company could disclose the following to satisfy subparagraph (i) of Rule 5605(f)(3): ''As a Smaller Reporting Company listed on the Nasdaq Capital Market tier, the Company is subject to Nasdaq Rule 5605(f)(2)(C), which requires the company to have, or explain why it does not have, at least two Diverse directors, including at least one director who self-identifies as Female. Under Rule 5605(f)(7), the Company is required to have at least one Diverse director by March 10, 2023, and a second Diverse director by March 10, 2026. The Company has chosen to satisfy Rule 5605(f)(2)(C) by explaining its reasons for not meeting the diversity objectives of Rule 5605(f)(2)(C), which the Company has set forth below.''

i. Effective Dates and Phase-in Period

Proposed Rule 5605(f)(7) provides a transition period before companies must fully satisfy the requirement to have two Diverse directors or explain why they do not upon the initial implementation of the rule. Under this transition rule, each company must have, or explain why it does not have, one Diverse director no later than two calendar years after SEC approval of the proposed rule (the ''Approval Date''), and two Diverse directors no later than (i) four calendar years after the Approval Date for companies listed on the Nasdaq Global Select (''NGS'') or Global Market (''NGM'') tiers, or (ii) five calendar years after the Approval Date for companies listed on the Nasdaq Capital Market (''NCM'') tier. For example, if the Approval Date is March 10, 2021, all companies would be required to have, or explain why they do not have, one Diverse director by March 10, 2023 and two Diverse directors by March 10, 2025 (for NGS/NGM companies) or March 10, 2026 (for NCM companies).

Under proposed Rule 5605(f)(5)(A), a newly listed company that was not previously subject to a substantially similar requirement of another national securities exchange will be allowed one year from the date of listing to satisfy the requirement described above. This ''phase-in'' period applies to companies listing in connection with an initial public offering, a direct listing, a transfer from another exchange or the over-the-counter market, or through a business combination with an acquisition company listed under IM–5101–2, such that the company is no longer subject to IM–5101–2 after the combination. This phase-in period will apply after the end of the transition period provided in Rule 5605(f)(7). As a result, companies listing after the expiration of the phase-in periods provided by Rule 5605(f)(7) would be provided with one year from the date of listing to satisfy the applicable requirement of Rule 5605(f)(2) to have, or explain why they do not have, at least two Diverse directors. Companies listing after the Approval Date, but prior to the expiration of the phase-in periods provided by Rule 5605(f)(7), would be

[166] Pursuant to Nasdaq Rule 5810(c)(2)(A)(iii), a company is provided 45 days to submit a plan to regain compliance with Rules 5620(a) (Meetings of Shareholders), 5620(c) (Quorum), 5630 (Review of Related Party Transactions), 5635 (Shareholder Approval), 5250(c)(3) (Auditor Registration), 5255(a) (Direct Registration Program), 5610 (Code of Conduct), 5615(a)(4)(D) (Partner Meetings of Limited Partnerships), 5615(a)(4)(E) (Quorum of Limited Partnerships), 5615(a)(4)(G) (Related Party Transactions of Limited Partnerships), and 5640 (Voting Rights). Pursuant to Nasdaq Rule 5810(c)(2)(A)(iv), a company is also provided 45 days to submit a plan to regain compliance with Rule 5250(b)(3)(Disclosure of Third Party Director and Nominee Compensation). A company is generally provided 60 days to submit a plan to regain compliance with the requirement to timely file periodic reports contained in Rule 5250(c)(1).

[167] Various stakeholders have requested easier aggregation. *See* Petition for Amendment of Proxy Rule, *supra* note 80, at 1.

[168] Nasdaq plans to publish an FAQ on the Listing Center clarifying that ''two members of its board of directors who are Diverse'' would exclude emeritus directors, retired directors and members of an advisory board.

provided with the latter of the periods set forth in Rule5605(f)(7) or one year from the date of listing.

Nasdaq believes this proposed period is consistent with the phase-in periods granted to companies for Nasdaq's other board composition requirements. For example, Rule 5615(b)(1) provides a company listing in connection with its initial public offering one year to fully comply with the compensation and nomination committee requirements of Rules 5605(d) and (e), and with the majority independent board requirement of Rule 5605(b). Similarly, SEC Rule 10A–3(b)(1)(iv)(A) allows a company up to one year from the date its registration statement is effective to fully comply with the applicable audit committee composition requirements. Nasdaq Rule 5615(b)(3) provides a one-year timeframe for compliance with the board composition requirements for companies transferring from other listed markets that do not have a substantially similar requirement.

ii. Foreign Issuers

Nasdaq recognizes that the EEOC categories of race and ethnicity may not extend to all countries globally because each country has its own unique demographic composition. However, Nasdaq observed that on average, women tend to be underrepresented in boardrooms across the globe, holding an estimated 16.9% of board seats in 2018.[169] As an official supporter of the United Nations Sustainable Stock Exchanges Initiative, Nasdaq recognizes that ensuring women have equal opportunities for leadership in economic decision making is one of the United Nations Sustainable Development Goals to be accomplished by 2030.[170] However, studies estimate that at current rates, it could take 18 [171] to 34 years [172] for U.S. companies to achieve gender parity on their boards.

Accordingly, under proposed Rule 5605(f)(2)(B), each Foreign Issuer must have, or explain why it does not have, at least two Diverse directors on its board, including at least one Female. Nasdaq proposes to provide Foreign Issuers with additional flexibility in that Foreign Issuers may satisfy the diversity requirement by having two Female directors. In addition, Foreign Issuers may also satisfy the diversity requirement by having one Female director, and an individual who self identifies as (i) LGBTQ+ or (ii) an underrepresented individual based on national, racial, ethnic, indigenous, cultural, religious or linguistic identity in the company's home country jurisdiction. Alternatively, a company could satisfy Rule 5605(f)(2)(B) by publicly explaining the company's reasons for not meeting the diversity objectives of the rule.

Nasdaq proposes to define a Foreign Issuer under Rule 5605(f)(1) as (a) a Foreign Private Issuer (as defined in Rule 5005(a)(19)) or (b) a company that: (i) Is considered a ''foreign issuer'' under Rule 3b–4(b) under the Act; [173] and (ii) has its principal executive offices located outside of the United States. This definition will include all Foreign Private Issuers (as defined in Rule 5005(a)(19)),[174] and any foreign issuers that are not foreign private issuers so long as they are also headquartered outside of the United States. This is designed to recognize that companies that are not Foreign Private Issuers but are headquartered outside of the United States are foreign companies notwithstanding the fact that they file domestic SEC reports. It is also designed to exclude companies that are domiciled in a foreign jurisdiction without having a physical presence in that country. Proposed Rule 5605(f)(5)(B) will allow any company that ceases to be a Foreign Issuer one year from the date that the company no longer qualifies as a Foreign Issuer to satisfy the requirements of Rule 5605(f).

Nasdaq also proposes to revise Rule 5615 and IM–5615–3, which currently permit a Foreign Private Issuer to follow home country practices in lieu of the requirements set forth in the Rule 5600 Series, subject to several exclusions. Nasdaq proposes to revise Rule 5615 and IM–5615–3 to add Rules 5605(f) and 5606 to the list of excluded corporate governance rules. As a result, Foreign Private Issuers must satisfy the requirements of Rule 5605(f) and 5606 and may not follow home country practices in lieu of such requirements. However, Foreign Private Issuers that elect to follow an alternative diversity objective in accordance with home country practices, or are located in jurisdictions that restrict the collection of personal data, may satisfy the requirements of Rule 5605(f) by explaining their reasons for doing so instead of meeting the diversity objectives of the rule.

iii. Smaller Reporting Companies

Nasdaq also recognizes that smaller companies, especially pre-revenue companies that depend on the capital markets to fund ground-breaking research and technological advancements, may not have the resources necessary to compensate an additional director or engage a search firm to search outside of directors' networks. In recognition of the resource constraints faced by smaller companies, Nasdaq proposes to provide each Smaller Reporting Company with additional flexibility. Specifically, these companies could satisfy the two Diverse directors objective under Rule 5605(f)(2)(C) by having two Female directors.

Like other companies, Smaller Reporting Companies could also satisfy the two Diverse directors by having one Female director and one director who self-identifies as either (i) an Underrepresented Minority, or (ii) a member of the LGBTQ+ community. Alternatively, a company could satisfy Rule 5605(f)(2)(C) by publicly explaining the company's reasons for not meeting the diversity objectives of the rule. Under Rule 5605(f)(1), Nasdaq proposes to define a Smaller Reporting Company as set forth in Rule 12b–2 under the Act.[175] Proposed Rule 5605(f)(5)(B) will allow any company that ceases to be a Smaller Reporting Company one year from the date that the company no longer qualifies as a Smaller Reporting Company to satisfy the requirements of Rule 5605(f).

iv. Cure Period

Nasdaq proposes to adopt Rule 5605(f)(6) and a new Rule 5810(c)(3)(F) to specify what happens if a company does not have at least two Diverse directors as set forth under Rule 5605(f)(2) and fails to provide the disclosure required by Rule

[169] *See* Deloitte, *Women in the Boardroom, supra* note 86.

[170] *See* United Nations Sustainable Stock Exchanges Initiative, *Gender Equality, https://www.un.org/sustainabledevelopment/gender-equality/* (last accessed Nov. 24, 2020).

[171] *See* McKinsey & Company, *supra* note 36, at 17.

[172] *See* GAO Report, *supra* note 44, at 9 (estimating ''it could take about 10 years from 2014 for women to comprise 30 percent of board directors and more than 40 years for the representation of women on boards to match that of men'').

[173] *See* 17 CFR 240.3b–4(b) (''The term foreign issuer means any issuer which is a foreign government, a national of any foreign country or a corporation or other organization incorporated or organized under the laws of any foreign country.'').

[174] Under Nasdaq Rule 5005(a)(19), the term Foreign Private Issuer has ''the same meaning as under Rule 3b–4 under the Act.''

[175] Under 12b–2 of the Act, a Smaller Reporting Company ''means an issuer that is not an investment company, an asset-backed issuer (as defined in § 229.1101 of this chapter), or a majority-owned subsidiary of a parent that is not a smaller reporting company and that: (1) Had a public float of less than $250 million; or (2) Had annual revenues of less than $100 million and either: (i) No public float; or (ii) A public float of less than $700 million.'' *See* 17 CFR 240.12b–2.

5605(f)(3).[176] Under those provisions, the Listing Qualifications Department will promptly notify the company that it has until the latter of its next annual shareholders meeting, or 180 days from the event that caused the deficiency, to cure the deficiency. The company can cure the deficiency either by nominating additional directors so that it satisfies the Diversity requirement of Rule 5605(f)(2) or by providing the disclosure required by Rule 5605(f)(3). If a company does not regain compliance within the applicable cure period, the Listings Qualifications Department would issue a Staff Delisting Determination Letter. A company that receives a Staff Delisting Determination can appeal the determination to the Hearings Panel through the process set forth in Rule 5815. Nasdaq also proposes revising Rule 5810(c)(2)(A)(iv) to make a non-substantive change clarifying that Rule 5250(b)(3) is related to ''Disclosure of Third Party Director and Nominee Compensation.''

v. Exempt Companies

Under proposed Rule 5605(f)(4), Nasdaq proposes to exempt the following types of companies from the requirements of Rule 5605(f) (''Exempt Companies''): acquisition companies listed under IM–5101–2; asset-backed issuers and other passive issuers (as set forth in Rule 5615(a)(1)); cooperatives (as set forth in Rule 5615(a)(2)); limited partnerships (as set forth in Rule 5615(a)(4)); management investment companies (as set forth in Rule 5615(a)(5)); issuers of non-voting preferred securities, debt securities and Derivative Securities (as set forth in Rule 5615(a)(6)); and issuers of securities listed under the Rule 5700 Series. Proposed Rule 5605(f)(5)(B) will allow any company that ceases to be an Exempt Company one year from the date that the company no longer qualifies as an Exempt Company to satisfy the requirements of Rule 5605(f).

Nasdaq believes it is appropriate to exempt these types of companies from the proposed rule because such companies do not have boards, do not list equity securities, or are not operating companies. These companies are already exempt from certain of Nasdaq's corporate governance standards related to board composition, as described in Rule 5615.

d. Alternatives Considered

Nasdaq considered whether requiring listed companies to have, or explain why they do not have, two Diverse directors would better promote the public interest than an alternative threshold or approach. Nasdaq's reasoned decision-making process included considering: (i) Mandate and disclosure-based approaches; (ii) higher and lower diversity objectives; (iii) longer and shorter timeframes; and (iv) broader and narrower definitions of ''Diverse.''

i. Mandate vs. Disclosure Based Approach

Globally, gender mandates range from requiring at least one woman on the board,[177] requiring two or more women based on board size,[178] or requiring 30 to 50% women on the board.[179] Some mandates vary by board size—for example, Norway imposes different standards for boards of two to three directors, four to five directors, six to eight directors, nine directors and ten or more directors.[180] California imposes a higher standard for gender diversity that boards with five directors or six or more directors must satisfy by the end of 2021 under S.B. 826, and a higher standard for underrepresented communities that boards with five to eight directors and nine or more directors must satisfy by the end of 2022 under A.B. 979. Nasdaq did not observe a common denominator among the mandates applicable to varying board sizes. However, Nasdaq considered criticism that a model based on various board sizes could subject companies to a higher threshold by virtue of adding directors.[181] Based on Nasdaq data, the average board size of its listed companies is eight directors.

Soft targets ranging from 25% to 40% women on boards have been suggested by various corporate governance codes and corporate governance organizations. For example, Rule 4.1 of the Swedish Corporate Governance Code (the ''Code'') provides that listed companies are to ''strive for gender balance on the board.'' [182] Each company's nominations committee is to publish a statement on its website at the time it issues notice of its shareholders meeting ''with regard to the requirement in rule 4.1, that the proposed composition of the board is appropriate according to the criteria set out in the Code and that the company is to strive for gender balance.'' [183] Companies are not

[176] Nasdaq proposes that existing Rules 5810(c)(3)(F) and (G) be renumbered as Rules 5810(c)(3)(G) and (H) respectively.

[177] For example, the Securities and Exchange Board of India requires public companies to have at least one woman on the board. *See* Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, Regulation 17(1)(a) (2015), available at: *https://www.sebi.gov.in/legal/regulations/jan-2020/securities-and-exchange-board-of-india-listing-obligations-and-disclosure-requirements-regulations-2015-last-amended-on-january-10-2020-_37269.html.* Similarly, the Israeli Companies Law requires public companies to have at least one woman on the board. *See* Paul Hastings, *Breaking the Glass Ceiling: Women in the Boardroom* 139 (2018), available at: *https://www.paulhastings.com/genderparity/.* In the United States, California's S.B. 826 requires public companies headquartered in California to have at least one woman on the board. *See* Cal. S.B. 826, *supra* note 112, at § 301.3(b)(3).

[178] For example, California's S.B. 826 requires public companies headquartered in California to have at least two women on the board if their board is comprised of five directors, and at least three women on the board if their board is comprised of six or more directors. *See* Cal. S.B. 826, *supra* note 112, at § 301.3(b)(1) and (2). Similar legislation has been proposed in New Jersey, Michigan and Hawaii. *See* N.J. Senate No. 3469, § 3(b)(2) (2019); Mich. S.B. 115, § 505a(2)(b) (2019); Haw. H.B. 2720, § 414–1(b)(2) (2020).

[179] For example, Norway imposes a gender quota ranging from 33%–50% depending on board size. *See* Paul Hastings, *supra* note 177, at 103. Portugal requires listed companies to have at least 33.3% women on boards by 2020. *See* Deloitte, *Women in the Boardroom, supra* note 86, at 143. Germany requires public companies with co-determined boards (at least 50% employee representation) to have at least 30% women, and all other listed companies to establish a company-defined target. *See* Ulrike Binder and Guido Zeppenfeld, Mayer Brown, *Germany Introduces Rules on Female Quota for Supervisory Boards and Leadership Positions* (March 13, 2015), available at *https://www.mayerbrown.com/en/perspectives-events/publications/2015/03/germany-introduces-rules-on-female-quota-for-super.* Belgium requires listed companies to have at least 33% women on the board. *See* Deloitte, *Women in the Boardroom, supra* note 86, at 85. Austria requires listed companies with more than 1,000 employees to have at least 30% women on the board. *See id.* at 81. Iceland requires public companies with more than 50 employees to have at least 40% women on the board. *See* Act respecting Public Limited Companies No. 2/199, Article 63, available at: *https://www.government.is/publications/legislation/lex/2018/02/06/TRANSLATION-OF-RECENT-AMENDMENTS-OF-ICELANDIC-PUBLIC-AND-PRIVATE-LIMITED-COMPANIES-LEGISLATION-2008-2010-including-Acts-13-2010-sex-ratios-and-68-2010-minority-protection-remuneration/.* France and Italy both require public companies to have at least 40% women on their boards. *See* Paul Hastings, *supra* note 177, at 91; White & Case, *Italy increases gender quotas in corporate boards of listed companies* (Jan. 29, 2020), available at: *https://www.whitecase.com/publications/alert/italy-increases-gender-quotas-corporate-boards-listed-companies*).

[180] *See* Paul Hastings, *supra* note 177, at 103.

[181] *See* David A. Katz and Laura A. McIntosh, Wachtell, Lipton, Rosen & Katz, *Gender Diversity and Board Quotas,* New York Law Journal (July 25, 2018), available at: *https://www.wlrk.com/webdocs/wlrknew/AttorneyPubs/WLRK.26150.18.pdf* (''California legislators dispute that the bill requires men to be displaced by women, noting that boards can simply increase their size. This may be easier said than done, however: Because the required quota increases with board size, a company with a four-man board that did not wish to force out a current director would need to add three women to accommodate the requirements of the law by 2021.'').

[182] *See* Swedish Corporate Governance Board, *The Swedish Corporate Governance Code* § 4.1 17 (eff. Jan. 1, 2020), available at: *http://www.bolagsstyrning.se/UserFiles/Koden/The_Swedish_Corporate_Governance_Code_1_January_2020.pdf.*

[183] *See* Swedish Corporate Governance Board, *Annual Report 2020* 22 (August 2020), available at:

required to comply with the Code, ''but are allowed the freedom to choose alternative solutions which they feel are better suited to their particular circumstances, as long as they openly report every deviation, describe the alternative solution they have chosen and explain their reasons for doing so.'' [184] Signifying progress, in 2019, 7% of nominations committees did not issue a statement on board gender balance, compared to 58% in 2013.[185]

In 2015, the Swedish Corporate Governance Board, which is responsible for administering the Code, established a goal to achieve representation of women on boards of small/mid cap (and Swedish companies listed on NGM Equity) and large cap companies of 30% and 35%, respectively, by 2017. Further, the Board aimed to achieve 40% representation of women on boards of all listed Swedish companies by 2020.[186] Based on data as of June 30, 2020, among listed companies, women accounted for 32.7% of board seats on small/mid cap companies and NGM Equity, 38.6% of large cap companies and 34.7% of all listed companies.[187]

In the United Kingdom, the Financial Conduct Authority requires companies with a premium listing on the London Stock Exchange to publicly disclose whether or not they comply with the Financial Reporting Council's U.K. Corporate Governance Code (the ''U.K. Code''), and if not, to explain their reasons for non-compliance.[188]

Provision 23 of the U.K. Code requires each company to publicly describe ''the work of the nomination committee, including . . . the policy on diversity and inclusion, its objectives and linkage to company strategy, how it has been implemented and progress on achieving the objectives,'' [189] and Principle J states that board appointments and succession planning should, among other things, ''promote diversity of gender, social and ethnic backgrounds.'' [190] In addition, the Companies Act requires companies to disclose gender diversity statistics among the board, management and employees.[191] In 2018, the Financial Reporting Council reported that 83% of FTSE 100 and 74% of FTSE 250 companies had established a board diversity policy specifying gender, with approximately ⅓ specifying ethnicity.[192] More recently, a report commissioned by the Financial Reporting Council concluded that there is a lack of public disclosure regarding the LGBTQ+ status among directors and executives of public companies. While the report did not recommend amending Principle J of the U.K. Code to consider sexual orientation or gender identity, it emphasized that the U.K. Code ''seeks to promote diversity and inclusion of all minority groups within business'' [193] and suggested that the government ''update corporate reporting requirements to require companies to demonstrate how they intend to capture data on the sexual orientation and gender identity of staff.'' [194]

In 2011, the Davies Review called on FTSE 100 boards to achieve 25% women on boards by 2015.[195] After that milestone was achieved, the Hampton Alexander Review encouraged FTSE 350 boards to have ⅓ women by 2020, and it has been achieved by FTSE 100 companies.[196] In 2017, the Parker Review called on FTSE 100 and 250 companies to have at least one director of color by 2021 and 2024, respectively.[197] As of February 2020, approximately 37% of FTSE 100 companies surveyed and 59% of FTSE 350 companies surveyed did not have one director of color on their board.[198]

Australian Securities Exchange (''ASX'')-listed companies must comply with the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (the ''ASX Recommendations'') or explain why they do not. The ASX Recommendations require companies to have and disclose a diversity policy with measurable objectives and report on progress towards meeting those objectives. If the company is in the ASX/S&P 300, its objective for achieving gender diversity should be at least 30%.[199] The Australian government also requires companies with 100 or more employees to provide an annual report about gender equality indicators, including the gender composition of the board and the rest of the workforce.[200] In 2015, the ASX and KPMG found that 99% of S&P/ASX 200 companies and 88% of ASX 201–500 companies disclosed establishing a diversity policy rather than explaining why they do not have one.[201] As of July 2020, women account for 28.4% and 31.8% of board seats among ASX 300 and ASX 100 companies, respectively.[202]

Nasdaq observed that women account for at least 30% of the boards of the largest companies in Australia, Sweden and the United Kingdom, and in three other countries that have implemented disclosure requirements or suggested milestones on a comply-or-explain

http://www.bolagsstyrning.se/userfiles/archive/3930/kodkoll_arsrapport-2020_eng.pdf.

[184] *See* Swedish Corporate Governance Board, *Gender balance on boards of listed companies: The Swedish Corporate Governance Board assesses the situation ahead of this year's AGMs* (February 3, 2015), available at: *http://www.bolagsstyrning.se/userfiles/archive/3856/pressrelease_gender_2014-02-03.pdf.*

[185] *See* Swedish Corporate Governance Board, *Annual Report 2020, supra* note 183, at 22.

[186] *See* Swedish Corporate Governance Board, *Gender balance, supra* note 184.

[187] *See* Swedish Corporate Governance Board, *Statistics regarding gender balance* (July 15, 2020), available at: *http://www.bolagsstyrning.se/userfiles/archive/3922/200715_gender_balance_on_boards.pdf; see also Sammanfattning,* available at *http://www.bolagsstyrning.se/userfiles/archive/3922/statistik_konsfordelning_2020.pdf.*

[188] *See* Financial Conduct Authority, LR 9.8.6(6), available at: *https://www.handbook.fca.org.uk/handbook/LR/9/8.html; see also* Financial Reporting Council, *The UK Corporate Governance Code* 3 (July 2018), available at *https://www.frc.org.uk/getattachment/88bd8c45-50ea-4841-95b0-d2f4f48069a2/2018-UK-Corporate-Governance-Code-FINAL.PDF.* In addition, ''[i]n 2016, the [UK] Government also implemented the relevant provision of the EU Non-Financial Reporting Directive with a new reporting requirement in the FCA's Disclosure and Transparency Rules. This requires issuers (excluding [small and medium-sized enterprises]) admitted to trading on an EU regulated market to disclose their diversity policy in the corporate governance statement.'' *See* Financial Reporting Council, *Board Diversity Reporting* 5 (September 2018), available at: *https://www.frc.org.uk/getattachment/62202e7d-064c-4026-bd19-f9ac9591fe19/Board-Diversity-Reporting-September-2018.pdf.*

[189] *See* Financial Reporting Council, *The UK Corporate Governance Code, supra* note 188, at 9.

[190] *Id.* at 8.

[191] *See* UK Companies Act 2006, § 414C.

[192] *See* Financial Reporting Council, Board Diversity Reporting, *supra* note 188, at 9.

[193] *See* Hay et al., *supra* note 98, at 37.

[194] *Id.*

[195] *See Women on boards, supra* note 96.

[196] *See Hampton-Alexander Review: FTSE Women Leaders* (November 2016), available at: *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/613085/ftse-women-leaders-hampton-alexander-review.pdf.*

[197] *See* Parker, *supra* note 97.

[198] *See* Sir John Parker, *Ethnic Diversity Enriching Business Leadership* 19 (Feb. 5, 2020), available at: *https://assets.ey.com/content/dam/ey-sites/ey-com/en_uk/news/2020/02/ey-parker-review-2020-report-final.pdf.*

[199] *See* ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* 9 (4th ed. Feb. 2019), available at: *https://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-fourth-edn.pdf.*

[200] Workplace Gender Equality Act 2012, Part IV § 13 (March 25, 2015), available at: *https://www.legislation.gov.au/Details/C2015C00088.*

[201] *See* KPMG and ASX, *ASX Corporate Governance Council Principles and Recommendations on Diversity: Analysis of disclosures for financial years ended 1 January 2015 and 31 December 2015* 4 (2016) available at: *https://www.asx.com.au/documents/asx-compliance/asx-corp-governance-kpmg-diversity-report.pdf.*

[202] *See* KPMG and 30% Club, *Building Gender Diversity on ASX 300 Boards: Seven Learnings from the ASX 200* 4 (July 2020), available at: https://assets.kpmg/content/dam/kpmg/au/pdf/2020/building-gender-diversity-asx-300-boards.pdf. The report also noted that diversity counteracts groupthink and that ASX 201–299 companies with at least 30% female directors ''are more likely than not to [have seen] market capitalisation increases over the past 12 months.'' *Id.* at 6.

basis: Finland, New Zealand, and Canada.[203] Nasdaq considered that countries that have implemented mandates have also seen progress in women's representation on boards, including, for example, Austria, Iceland, Belgium, France, Germany, Italy and Portugal.[204] On average, women account for 31% of board seats in countries with gender mandates.[205]

Nasdaq discussed the benefits and challenges of mandate and comply-or-explain models with over a dozen stakeholders, and while the majority of organizations were in agreement that companies would benefit from a regulatory impetus to drive meaningful and systemic change in board diversity, the majority also stated that a disclosure-based approach would be more palatable to the U.S. business community than a mandate. Most organizations Nasdaq spoke with expressed general discomfort with mandates, although they acknowledged that opposition is lessening in the wake of California's S.B. 826 [206] and A.B. 979.[207] While many recognized that mandates can force boards to act more quickly and accelerate the rate of change, they believe that a disclosure-based approach is less controversial and would spur companies to take action and achieve the same results. Some stakeholders also highlighted additional challenges that smaller companies and companies in certain industries may face finding diverse board members. In contrast, a disclosure-based framework that provides companies with flexibility would empower companies to maintain decision-making authority over their board's composition while providing stakeholders with a better understanding of the company's current board composition and its philosophy regarding diversity. This approach would better inform the investment community and enable more informed analysis of, and conversations with, companies. Nasdaq believes that these goals will be achieved through the disclosure of consistent, comparable data across companies, as would be required by the Exchange's proposed definition of Diverse.

For example, if, under Israeli law regarding board diversity, an Israeli company is required only to have a minimum of one woman on the board and such Israeli company chooses to comply with Israeli home country law in lieu of meeting the diversity objectives of Rule 5605(f)(2)(B), it may choose to disclose that ''the Company is incorporated in Israel and required by Israeli law to have a minimum of one woman on the board, and satisfies home country requirements in lieu of Nasdaq Rule 5605(f)(2)(B), which requires each Foreign Issuer to have at least two Diverse directors.'' If a U.S. company had two Diverse directors but one resigned due to unforeseen circumstances, it could disclose, for example: ''Due to the unexpected resignation of Ms. Smith this year, the Company does not have at least one director who self-identifies as Female and one director who self-identifies as an Underrepresented Minority or LGBTQ+. We intend to undertake reasonable efforts to meet the diversity objectives of Rule 5605(f)(2)(A) prior to our next annual shareholder meeting and have engaged a search firm to identify qualified Diverse candidates. However, due to unforeseen circumstances, we may not achieve this goal.'' Or a U.S. company may disclose that it chooses to define diversity more broadly than Nasdaq's definition by considering national origin, veteran status or individuals with disabilities when identifying nominees for director because it believes such diversity brings a wide range of perspectives and experiences to the board. In each case, investors will have a better understanding of the company's reasons for not having at least two Diverse directors and can use that information to make an informed investment or voting decision.

ii. Higher vs. Lower Diversity Objectives

Nasdaq observed that existing empirical research spanned companies across several countries, including the United States, Spain, China, Canada, France and Norway. Nasdaq considered that the studies related to company performance and board diversity found positive associations at various levels and measures of board diversity, including having at least one woman on the board,[208] two or more diverse directors (with diverse considered female, Black, Hispanic or Asian),[209] at least three women on the board [210] and being in the top quartile for gender and ethnic diversity.[211]

Nasdaq considered that the academic studies related to investor protection and board diversity found positive associations at various levels and measures of board diversity, including having at least one woman on the board [212] or up to 50% women on the board, and the assertions of certain academics that their findings may extend to other forms of diversity, including racial and ethnic diversity.[213] Nasdaq also reviewed academic research suggesting that ''critical mass'' is achieved by having three or more women on the board, and that having only one diverse director on the board risks ''tokenism.'' [214] Nasdaq considered that although the legislation enacted by Norway and California, and proposed by several other states, varies based on board size, the academic research considered companies across a spectrum of sizes and board sizes, including Fortune 100, S&P 500, Fortune 1000 and smaller (non-Fortune 1000) companies.

Nasdaq concluded that there is no ''one-size fits all'' approach to promoting board diversity and that the academic literature regarding the relationship between board diversity, company performance and investor protections is continuing to evolve. However, in Nasdaq's survey of academic studies described above—and of the targets or mandates promulgated by regulatory bodies and organizations worldwide—Nasdaq observed a common denominator of having at least one woman on the board. Similarly, Nasdaq observed a common denominator of having at least one director who is diverse in terms of race, ethnicity or sexual orientation among

[203] *See* The Conference Board of Canada, *Data Dashboard* (Sept. 23, 2020), available at: *https://www.conferenceboard.ca/focus-areas/inclusion/2020/aob-comparisons-around-the-world-table?AspxAutoDetectCookieSupport=1;* Andrew MacDougall et al., Osler, *Diversity Disclosure Practices* 4 (2020), available at *https://www.osler.com/osler/media/Osler/reports/corporate-governance/Diversity-and-Leadership-in-Corporate-Canada-2020.pdf. But see* Heike Mensi-Klarbach et al., *The Carrot or the Stick: Self-Regulation for Gender-Diverse Boards via Codes of Good Governance,* J. Bus. Ethics 11 (2019), available at: *https://doi.org/10.1007/s10551-019-04336-z* (reviewing longitudinal data from 2006 to 2016 on listed and state-owned companies in Austria and concluding that ''self-regulation of gender diversity on boards is ineffective if merely based on recommendations in codes of good governance''). Mensi-Klarbach recommends setting concrete targets and providing public monitoring to improve the effectiveness of comply-or-explain frameworks.

[204] *See* Paul Hastings, *supra* note 177; *see also* Deloitte, *Women in the Boardroom, supra* note 86.

[205] *See* Paul Hastings, *supra* note 177; The Conference Board of Canada, *supra* note 203.

[206] *See* Cal. S.B. 826, *supra* note 112.

[207] *See* Cal. A.B. 979, *supra* note 112.

[208] *See* Credit Suisse, *supra* note 30, at 16.

[209] *See* Thomas and Starr, *supra* note 23, at 5.

[210] *See* Eastman et al., *supra* note 31, at 3; Wagner, *supra* note 32.

[211] *See* McKinsey, *supra* note 36.

[212] *See* Abbott et al., *supra* note 58; Chen et al., *supra* note 64.

[213] *See* Wahid, *supra* note 59; Cumming et al., *supra* note 62, at 34.

[214] *See* Alison M. Konrad et al., *Critical Mass: The Impact of Three or More Women on Corporate Boards,* 37(2) Org. Dynamics 145 (April 2008); Miriam Schwartz-Ziv, *Gender and Board Activeness: The Role of a Critical Mass,* 52(2) J. Fin. & Quant. Analysis 751 (April 2017); Mariateresa Torchia et al., *Women Directors on Corporate Boards: From Tokenism to Critical Mass,* 102(2) J. Bus. Ethics. 299 (Feb. 25, 2011), available at *https://ssrn.com/abstract=1858347.*

the requirements related to, and academic research considering, board diversity beyond gender identity. Nasdaq therefore believes that a diversity objective of at least two Diverse directors provides a reasonable baseline for comparison across companies. Companies are not precluded from meeting a higher or lower alternative measurable objective. For example, a company may choose to disclose that it does not meet the diversity objectives under Rule 5605(f)(2) because it is subject to an alternative standard under state or foreign laws and has chosen to satisfy that diversity objective instead. On the other hand, many firms may strive to achieve even greater diversity than the objectives set forth in Nasdaq's proposed rule. Nasdaq believes that providing flexibility and clear disclosure when the company determines to follow a different path will improve the quality of information available to investors who rely on this information to make informed investment and voting decisions.

iii. Longer vs. Shorter Timeframes

Nasdaq considered whether an alternative timeframe for satisfying the diversity objectives of Rule 5605(f)(2) would better promote the public interest than the timeframe Nasdaq has proposed under Rule 5605(f)(7). While companies are not precluded from adding additional directors to their boards to satisfy Rule 5605(f)(2) by having two Diverse directors sooner than contemplated by the proposed rule, Nasdaq understands that some companies may need to obtain shareholder approval to amend their governing documents to allow for board expansion. Other companies may choose to replace an existing director on the board with a Diverse director, and board turnover may be low.[215] Nasdaq recognizes that it also takes substantial lead time to identify, interview and select board nominees. To provide companies with sufficient time to satisfy Rule 5605(f) by having two Diverse directors, while recognizing that investors are calling for expedient change, Nasdaq has structured its proposal similarly to the approach taken by California, where companies must achieve one target by an earlier date and satisfy the entire diversity objective at a later date. Nasdaq also considered the approaches taken by foreign jurisdictions to implement diversity objectives. For example, Belgium and France implemented diversity objectives under a phased approach that provided companies with at least five years to fully satisfy the objectives,[216] whereas Iceland and Portugal provided companies with three years or less.[217]

While companies may choose to satisfy Rule 5605(f)(2) on an alternative timeframe, a company that chooses a timeframe that is longer than the timeframes set forth in Rule 5605(f)(7) also must publicly explain its reasons for doing so. For example, an NGM-listed company that, while not technically a Smaller Reporting Company, views itself as similarly situated to a NCM-listed Smaller Reporting Company may disclose the following: ''While the Company is listed on NGM and technically qualifies as a Smaller Reporting Company, it does not file its SEC reports utilizing the Smaller Reporting Company designation. However, the Company believes that it is similarly situated to other Smaller Reporting Companies listed on NCM in terms of its annual revenues and public float, and therefore has chosen to satisfy Rule 5605(f)(2)(C) in lieu of Rule 5605(f)(2)(A) and has satisfied this requirement by having at least two Diverse directors on the board who self-identify as Female within the timeframe provided under Rule 5605(f)(7) applicable to NCM-listed companies.''

iv. Broader vs. Narrower Definition of Diverse

Nasdaq considered whether the definition of Diverse should include broader characteristics than those reported on the EEO–1 report, such as the examples provided by the Commission's CD&I, including LGBTQ+, nationality, veteran status, and individuals with disabilities. During its stakeholder outreach, Nasdaq inquired whether a broad definition of Diversity would promote the public interest. While recognizing the diverse perspectives that different backgrounds can provide, most stakeholders supported a narrower definition of Diversity focused on gender, race and ethnicity, with several supporting broadening the definition to include the LGBTQ+ community.

As discussed above, companies currently are permitted to define diversity ''in ways they consider appropriate'' under federal securities laws. One of the challenges of this principles-based approach has been the disclosure of inconsistent and noncomparable data across companies. However, most companies are required by law to report data on race, ethnicity and gender to the EEOC through the EEO–1 Report. Nasdaq believes that adopting a broad definition of Diverse would maintain the status quo of inconsistent, noncomparable disclosures, whereas a narrower definition of Diverse focused on race, ethnicity, sexual orientation and gender identity will promote the public interest by improving transparency and comparability. Nasdaq also is concerned that the broader definitions of diversity utilized by some companies may result in Diverse candidates being overlooked, and may be hindering meaningful progress on improving diversity related to race, ethnicity, sexual orientation and gender identity. For example, a company may consider diversity to include age, education and board tenure. While such characteristics may provide laudable cognitive diversity, this focus may result in a homogenous board with respect to race, ethnicity, sexual orientation and gender identity that, by extension, does not reflect the diversity of a company's communities, employees, investors or other stakeholders.

Nasdaq also believes that a transparent, consistent definition of Diverse would provide stakeholders with a better understanding of the company's current board composition and its philosophy regarding diversity if it does not have two Diverse directors. This would enable the investment community to conduct more informed analysis of, and have more informed conversations with, companies. To the extent a company chooses to satisfy the requirement of Rule 5605(f)(2) by having at least two Diverse directors on its board, it will have the ancillary benefit of making meaningful progress in improving board diversity related to race, ethnicity, sexual orientation and gender identity.

Nasdaq's review of academic research on board diversity revealed a dearth of empirical analysis on the relationship between investor protection or company performance and broader diversity characteristics such as veteran status or individuals with disabilities.[218] Nasdaq

[215] *See* Matteo Tonello, *Corporate Board Practices in the Russell 3000 and S&P 500,* Harv. L. Sch. Forum on Corp. Governance (Oct. 18, 2020), *https://corpgov.law.harvard.edu/2020/10/18/corporate-board-practices-in-the-russell-3000-and-sp-500/* (last accessed Nov. 24, 2020).

[216] *See* Paul Hastings, *supra* note 177, at 79 and 90; *see also supra* note 179.

[217] *See* Deloitte, Women in the Boardroom, *supra* note 86, at 115 and 143; *see also supra* note 179.

[218] KPMG (2020) states that veterans are underrepresented in boardrooms, with retired General and Flag Officers (''GFOs'') occupying less than 1% of Fortune 500 board seats. *See* KPMG, *The value of veterans in the boardroom* 1 (2020), available at: *https://boardleadership.kpmg.us/content/dam/boardleadership/en/pdf/2020/the-value-of-veterans-in-the-boardroom.pdf* (noting that

Continued

acknowledges that there also is a lack of published research on the issue of LGBTQ+ representation on boards.[219] This may be due to a lack of consistent, transparent data on broader diverse attributes, or because there is no voluntary self-disclosure workforce reporting requirements for LGBTQ+ status, such as the EEO–1 reporting framework for race, ethnicity, and gender. In any event, it is evident that while ''[b]oardroom diversity is a topic that has gained significant traction . . . LGBT+ diversity, however, has largely been left out of the conversation.'' [220]

Nonetheless, Nasdaq believes it is reasonable and in the public interest to include a reporting category for LGBTQ+ in recognition of the U.S. Supreme Court's recent affirmation that sexual orientation and gender identity are ''inextricably'' intertwined with sex,[221] and based on studies demonstrating a positive association between board diversity and decision making, company performance and investor protections. Nasdaq also believes that the proposed rule would foster the development of data to conduct meaningful assessments of the association between LGBTQ+ board diversity, company performance and investor protections.

As noted above, the proposal does not preclude companies from considering additional diverse attributes, such as nationality, disability, or veteran status in selecting board members; however, company would still have to provide the required disclosure under Rule 5605(f)(3) if the company does not also have at least two directors who are Diverse. Nor would the proposal prevent companies from disclosing information related to other diverse attributes of board members beyond those highlighted in the rule if they felt such disclosure would benefit investors. Nasdaq believes such disclosure would help inform the evolving body of research on the relationship between broader diverse attributes, company performance and investor protection and provide investors with additional information about the company's philosophy regarding broader diversity characteristics.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,[222] in general, and furthers the objectives of Section 6(b)(5) of the Act,[223] in that it is designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, to prevent fraudulent and manipulative acts and practices, and, in general, to protect investors and the public interest, for the reasons set forth below. Further, Nasdaq believes the proposal is not designed to permit unfair discrimination between issuers or to regulate by virtue of any authority conferred by the Act matters not related to the purposes of the Act or the administration of the Exchange, for the reasons set forth below.

I. Board Statistical Disclosure

Nasdaq has proposed what it believes to be a straightforward and clear approach for companies to publish their statistical data pursuant to proposed Rule 5606. The disclosure will assist investors in making more informed decisions by making meaningful, consistent, and reliable data readily available and in a clear and comprehensive format prescribed by the proposed rule. Nasdaq also believes that the disclosure format required by proposed Rule 5606 protects investors by eliminating data collection inaccuracies and decreasing costs, while enhancing investors' ability to utilize the information.

As a threshold matter, as discussed above, diversity has become an increasingly important subject and, in recent years, investors increasingly have been advocating for greater board diversity and for the disclosure of board diversity statistics. The current board diversity disclosure regime is lacking in several respects, and Nasdaq believes that its proposed Rule 5606 addresses many of the current concerns and responds to investors' demands for greater transparency into the diversity characteristics of a company's board composition by mandating disclosure and curing certain deficiencies that exist within the current SEC disclosure requirements.

Investors have expressed their dissatisfaction with having to independently collect board-level data about race, ethnicity and gender identity because such investigations can be time consuming, expensive, and fraught with inaccuracies.[224] The lack of consistency and specificity in Regulation S–K has been a major impediment for many investors and data collectors. As a general matter, the Commission's requirements have not addressed the concerns expressed by commenters that ''disclosure about board diversity was important information to investors.'' [225] Nasdaq believes that its proposed Rule 5606 addresses many of the concerns that have been raised.

Nasdaq believes that requiring the annual disclosure of a company's board diversity, as proposed in Rule 5606(a), will provide consistent information to the public and will enable investors to continually review the board composition of a company to track trends and simplify or eliminate the need for a company to respond to multiple investor requests for information about the diverse characteristics of the company's board. Requiring annual disclosures also would make information available to investors who otherwise would not be able to obtain individualized disclosures.[226] Moreover, consistent disclosures may encourage boards to consider a wider range of board candidates in the nomination process, including candidates with fewer ties to the current board.[227]

The Commission's 2009 amendments to Regulation S–K provide no definition for diversity and do not explicitly require disclosures specifically related to details about the board's gender, racial, ethnic and LGBTQ+ composition. Additionally, the Commission's CD&I does not address the definition of diversity, and it requires a registrant to disclose diversity information only in certain limited circumstances. Investors have expressed that current regulations and accompanying interpretations impair their ability to obtain clear and consistent data.[228] As a result, Nasdaq believes that proposed Rule 5606(a) protects investors and the public

''[r]etired GFOs who have honed their leadership and critical decision-making skills in a high-threat environment can bring extensive risk oversight experience to the board, which may be especially valuable in the context of today's risk landscape''). Accenture (2018) observed that companies that offered inclusive working environments for employees with disabilities achieved an average of 28% higher revenue, 30% higher economic profit margins, and 2x net income than their industry peers. *See* Accenture, *Getting to Equal: The Disability Inclusion Advantage* (2018), available at: *https://www.accenture.com/_acnmedia/PDF-89/Accenture-Disability-Inclusion-Research-Report.pdf.*

[219] *See* Credit Suisse ESG Research, *supra* note 33, at 1; *see also* Out Leadership, *supra* note 35.

[220] *See* Out Leadership, *supra* note 35, at 3.

[221] *See Bostock* v. *Clayton Cnty., supra* note 160.

[222] *See* 15 U.S.C. 78f(b).

[223] *Id.* § 78f(b)(5).

[224] *See* Petition for Amendment of Proxy Rule, *supra* note 80, at 2.

[225] *See* Proxy Disclosure Enhancements, 74 FR at 68,343–44 (amending Item 407(c)(2)(vi) of Regulation S–K, codified at 17 CFR 229.407(c)(2)(vi)).

[226] *See* Petition for Rulemaking, *supra* note 123.

[227] *See* Proxy Disclosure Enhancements, 74 FR at 68,355 (''To the extent that boards branch out from the set of candidates they would ordinarily consider, they may nominate directors who have fewer existing ties to the board or management and are, consequently, more independent.''); Hazen and Broome, *supra* note 114, at 57–58.

[228] *See* Petition for Amendment of Proxy Rule, *supra* note 80, at 2; Petition for Rulemaking, *supra* note 123, at 7.

interest by making clear that a company's annual diversity data disclosure must include information related to gender identity, race, ethnicity and LGBTQ+ status, thereby leaving less discretion for companies to selectively disclose certain diversity information and enhancing the comparability of such data across companies. Moreover, it is in the public interest to provide clear requirements for diversity disclosure, and Nasdaq's proposed Board Diversity Matrix format provides such clarity.

Nasdaq does not intend to obligate directors to self-identify in any of the categories related to gender identity, race, ethnicity and LGBTQ+. Nasdaq believes that a director should have autonomy to decide whether to provide such information to their company. Therefore, Nasdaq believes that it is reasonable and in the public interest to allow directors to opt out of disclosing the information required by proposed Rule 5606(a) by permitting a company to identify such directors in the ''Undisclosed'' category.

Nasdaq believes that it is in the public interest to utilize the Board Diversity Matrix format for all companies as proposed in Rule 5606(a). Additionally, Nasdaq believes that the format removes any impediments to aggregating and analyzing data across all companies by requiring each company to disclose separately the number of male, female, and non-binary directors, the number of male, female, and non-binary directors that fall into certain racial and ethnic categories, and the number of directors that identify as LGBTQ+. The format allows investors to easily disaggregate the data and track directors with multiple diversity characteristics.

As discussed above, most listed companies are required by law to complete an EEOC Employer Information Report EEO–1 Form. Although outside directors generally are not employees and therefore are not covered in the EEO–1,[229] Nasdaq believes that collecting the information required by proposed Rule 5606(a) is familiar to most companies, and that it is reasonable to require disclosure of the additional board information.

Nasdaq also believes that requiring currently listed companies to comply with proposed Rule 5606 within one year from the date of Commission approval is a reasonable amount of time, given that most companies already collect similar information for certain employees. Moreover, most companies are required to prepare an annual proxy statement and update the Commission within four business days when a new director is appointed to the board.[230]

Further, Nasdaq believes that the disclosure required by proposed Rule 5606(a) will remove impediments to shareholders by making available information related to board-level diversity in a standardized manner, thereby enhancing the consistency and comparability of the information and helping to better protect investors. The proposed disclosure will also help protect investors and the public interest by enabling investors to determine the total number of diverse directors, which is information that is not consistently available in existing proxy disclosures in cases where a single director has multiple diverse characteristics. While companies can elect to make this information available either in a proxy statement or on the company's website, Nasdaq believes it is in the public interest to allow companies the option to provide the disclosure in a way they believe will be most meaningful to their shareholders.

Nasdaq recognizes that the proposed definition of Underrepresented Minority in Rule 5605(f)(1) may not apply to companies outside of the United States because each country has its own unique demographic composition. Moreover, Nasdaq's definition of Underrepresented Minority proposed in Rule 5606(f)(1) may be inapplicable to a Foreign Issuer, making this Board Matrix data less relevant for such companies and not useful for investors. Therefore, Nasdaq believes that offering Foreign Issuers the option of a separate template that requires different disclosure categories will provide investors with more accurate disclosures related to the diversity of directors among the board of a Foreign Issuer. Additionally, Nasdaq believes that providing an ''Underrepresented Individual in Home Country Jurisdiction'' category provides Foreign Issuers with more flexibility to identify and disclose diverse directors within their home countries.

The annual requirement in the proposed rule will guarantee that the information is available to the public on a continuous and consistent basis. As described in the instructions to the Board Diversity Matrix disclosure form and Rule 5606(a), each year following the first year that a company publishes the Board Diversity Matrix, the company will be required to publish its data for the current and immediately prior years. Nasdaq believes that disclosing at least two years of data allows the public to view any changes and track a board's diversity progress.

In addition to providing a means for shareholders to assess a company's board-level diversity and measure its progress in improving that diversity over time, Nasdaq believes that proposed Rule 5606 will provide a means for Nasdaq to assess whether companies meet the diversity objectives of proposed Rule 5605(f). The ability to determine satisfaction of the proposed listing rule's diversity objectives will protect investors and the public interest.

Moreover, the proposed rule provides transparency into diversity based not only on race, ethnicity, and gender identity, but also on a director's self-identified sexual orientation. Nasdaq believes that expanding the diversity characteristics beyond those which are commonly reported by companies currently will broaden the way boards view diversity, and ensure that board diversity is occurring across all protected groups.

Finally, Nasdaq believes that the proposal is not unfairly discriminatory because proposed Rule 5606 will apply to all Nasdaq-listed companies, except for the following companies: Acquisition companies listed under IM–5101–2; asset-backed issuers and other passive issuers (as set forth in Rule 5615(a)(1)); cooperatives (as set forth in Rule 5615(a)(2)); limited partnerships (as set forth in Rule 5615(a)(4)); management investment companies (as set forth in Rule 5615(a)(5)); issuers of non-voting preferred securities, debt securities and Derivative Securities (as set forth in Rule 5615(a)(6)); and issuers of securities listed under the Rule 5700 Series—which meet the definition of Exempt Companies as defined under proposed Rule 5605(f)(4). Nasdaq believes it is reasonable and not unfairly discriminatory to exempt these companies from the proposed rule because the exemption of these companies is consistent with the approach taken by Nasdaq in Rule 5615 as it relates to certain Nasdaq corporate governance standards for board composition.

Nasdaq further believes it is reasonable to provide companies with a one-year phase-in period to comply with proposed Rule 5606. Nasdaq believes there is only a *de minimis* burden placed on companies to collect the board data and prepare the Board Diversity Matrix. Moreover, as discussed above, companies already are required to gather similar information for certain employees. Therefore, Nasdaq believes that one year is

[229] The EEO–1 Form does not require a company to disclose data for outside directors because such directors are not company employees.

[230] *See* SEC Form 8–K, available at: *https://www.sec.gov/files/form8-k.pdf.*

sufficient time for companies to incorporate their directors into their data collection. Furthermore, newly listed companies have many obligations to meet under Nasdaq listing rules. Therefore, Nasdaq believes that it is reasonable under proposed Rule 5606(d) to provide newly listed Nasdaq companies, including companies listing in connection with a business combination under IM–5101–2, with one year from the time of listing to comply with the proposed rule.

II. Diverse Board Representation or Explanation

a. Removes Impediments to and Perfects the Mechanism of a Free and Open Market and a National Market System

As discussed above, studies suggest that the traditional director candidate selection process may create barriers to considering qualified diverse candidates for board positions by limiting the search for director nominees to existing directors' social networks and candidates with C-suite experience.[231] In analyzing Norway's experience in implementing a gender mandate, Dhir (2015) observed that ''[b]oard seats tend to be filled by directors engaging their networks, and the resulting appointees tend to be of the same socio-demographic background.'' [232] Dhir concluded that broadening the search for directors outside of traditional networks ''is unlikely to occur without some form of regulatory intervention, given the prevalence of homogenous social networks and in-group favoritism.'' [233] Regulatory action was effective in increasing the representation of women on boards in Norway by ''democratiz[ing] access to a space previously unavailable to women.'' [234] The number of public company board seats held by women in Norway increased from 6% in 2002 to 42% in 2020.[235] One Norwegian director ''grudgingly accept[ed] that the free market principles she held so dearly had disappointed her—and that the [mandate] was a necessary correction of market failure.'' [236]

In contrast, Nasdaq observed that other countries have made comparable progress using a disclosure-based model. Women account for at least 30% of the largest boards of companies in six countries using comply-or-explain models:[237] Australia, Finland, Sweden, New Zealand, Canada and the United Kingdom.[238] Nasdaq discussed the benefits and challenges of mandate and disclosure-based models with over a dozen stakeholders, and the majority of organizations were in agreement that companies would benefit from a regulatory impetus to drive meaningful and systemic change in board diversity, and that a disclosure-based approach would be more palatable to the U.S. business community than a mandate. While many organizations recognized that mandates can force boards to act more quickly and accelerate the rate of change, they believe that a disclosure-based approach is less controversial and would spur companies to take action and achieve the same results. Some stakeholders also highlighted additional challenges that smaller companies and companies in certain industries may face finding diverse board members. However, leaders from across the spectrum of stakeholders with whom Nasdaq spoke reinforced the notion that if companies recruit by skill set and expertise rather than title, then they will find there is more than enough diverse talent to satisfy demand.

Nasdaq also considered Commissioner Lee's observation that disclosure ''gets investors the information they need to make investment decisions based on their own judgment of what indicators matter for long-term value. Importantly, it can also drive corporate behavior.'' Specifically, she observed that:

> For one thing, when companies have to formulate disclosure on topics it can influence their treatment of them, something known as the ''what gets measured, gets managed'' phenomenon. Moreover, when companies have to be transparent, it creates external pressure from investors and others who can draw comparisons company to company. The Commission has long-recognized that influencing corporate behavior is an appropriate aim of our regulations, noting that ''disclosure may, depending on determinations made by a company's management, directors and shareholders, influence corporate conduct'' and that ''[t]his sort of impact is clearly consistent with the basic philosophy of the disclosure provisions of the federal securities laws.[239]

Nasdaq believes that a disclosure-based framework may influence corporate conduct if a company chooses to meet the diversity objective of Rule 5605(f)(2) by having two Diverse directors on the board. A company may satisfy that objective by broadening the search for qualified candidates and considering candidates from other professional pathways that bring a wider range of skills and perspectives beyond traditional C-suite experience.[240] Nasdaq believes that this will help increase opportunities for Diverse candidates that otherwise may be overlooked due to the impediments of the traditional director recruitment process, which will thereby remove impediments to a free and open market and a national market system. Further, boards that choose to have at least two Diverse directors may experience other benefits from diversity that perfect the mechanism of a free and open market and national market system. As discussed above in Section II.A.1.II.b (*Diversity and Investor Protection*), and further discussed below in Section II.A.2.II.b (*Prevent Fraudulent and Manipulative Acts and Practices*), studies suggest that diversity is positively associated with reduced stock volatility,[241] more transparent public disclosures,[242] and less information asymmetry,[243] leading to stock prices that better reflect public information, and further removing impediments to and perfecting a free and open market and a national market system. Importantly, Nasdaq believes that the disclosure-based framework proposed under Rule 5605(f) will not create additional impediments to a free and open market and a national market system because it will empower

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[231] *See* GAO Report, *supra* note 44; Vell, *supra* note 100; Rhode & Packel, *supra* note 104, at 39; Deloitte, *Women in the Boardroom, supra* note 86; *see also* Parker, *supra* note 97, at 38 (acknowledging that, ''as is the case with gender, people of colour within the UK have historically not had the same opportunities as many mainstream candidates to develop the skills, networks and senior leadership experience desired in a FTSE Boardroom'').

[232] *See* Dhir, *supra* note 78, at 52.

[233] *Id.* at 51. *See also* Albertine d'Hoop-Azar et al., *Gender Parity on Boards Around the World,* Harv. L. Sch. Forum on Corp. Governance (January 5, 2017), available at: *https://corpgov.law.harvard.edu/2017/01/05/gender-parity-on-boards-around-the-world/* (comparing gender diversity on boards in countries with varying requirements and enforcement measures and concluding that external pressures—''progressive societal norms'' and regulations—are needed to increase board diversity).

[234] *See* Dhir, *supra* note 78, at 101.

[235] *See* Marianne Bertrand et al., *Breaking the Glass Ceiling? The Effect of Board Quotas on Female Labor Market Outcomes in Norway,* Nat'l Bureau of Econ. Rsch. Working Paper 20256 (June 2017), available at *https://www.nber.org/papers/w20256;* Statistics Norway, *Board and management in limited companies* (Mar. 6, 2020), *https://www.ssb.no/en/styre* (last accessed Nov. 27, 2020).

[236] *See* Dhir, *supra* note 78, at 116.

[237] *See* Paul Hastings, *supra* note 177; Deloitte, *Women in the Boardroom, supra* note 86.

[238] *See* Conference Board of Canada, *supra* note 201; Osler, *supra* note 203, at 4.

[239] *See* Lee, *supra* note 22.

[240] *See, e.g.,* Hillman et al., *supra* note 105 (finding that African-American and white women directors were more likely to have specialized expertise in law, finance, banking, public relations or marketing, or community influence from positions in politics, academia or clergy).

[241] *See* Bernile et al., *supra* note 28.

[242] *See* Gul et al., *supra* note 66; Bravo and Alcaide-Ruiz, *supra* note 56.

[243] *See* Abad et al., *supra* note 67.

companies to maintain decision-making authority over the composition of their boards.

To the extent a company chooses not to meet the diversity objectives of Rule 5605(f)(2) to have at least two Diverse directors, Nasdaq believes that proposed Rule 5605(f)(3) will provide analysts and investors with a better understanding about the company's reasons for not doing so and its philosophy regarding diversity. Rule 5605(f) will thus remove impediments to a free and open market and a national market system by enabling the investment community to conduct more informed analyses of, and have more informed conversations with, companies. Nasdaq believes that such analyses and conversations will be better informed by consistent, comparable data across companies, which Nasdaq proposes to achieve by adopting a consistent definition of ''Diverse'' under Rule 5605(f)(1). Nasdaq further believes that providing such disclosure will improve the quality of information available to investors who rely on this information to make informed investment and voting decisions, thereby promoting capital formation and efficiency and perfecting the mechanism of a free and open market and a national market system.

b. Prevent Fraudulent and Manipulative Acts and Practices

Nasdaq's analysis discussed above in Section II.A.1.II raises the concern that the failure of homogenous boards to consider a broad range of viewpoints can result in suboptimal decisions that have adverse effects on company performance, board performance and stakeholders. Nasdaq believes that including diverse directors with a broader range of skills, perspectives and experiences may help detect and prevent fraudulent and manipulative acts and practices by mitigating ''groupthink.'' Increased board diversity also may reduce the likelihood of insider trading and other fraudulent and manipulative acts and practices.

Nasdaq reached this conclusion by reviewing public statements by investors and organizations regarding the impact of groupthink on decision making processes, as well as academic studies on the relationship between diversity, groupthink and fraud. Nasdaq observed that groupthink can result in ''self-censorship'' [244] and failure to voice dissenting viewpoints in pursuit of ''consensus without critical evaluation and without considering different possibilities.'' [245] In contrast, ''board members who possess a variety of viewpoints may raise different ideas and encourage a full airing of dissenting views. Such a broad pool of talent can be assembled when potential board candidates are not limited by gender, race, or ethnicity.'' [246]

Dhir (2015) concluded that gender diversity may ''promote cognitive diversity and constructive conflict in the boardroom'' and may be more effective at overseeing management.[247] One respondent in Dhir's survey of Norwegian directors observed that:

> I've seen situations where the women were more willing to dig into the difficult questions and really go to the bottom even if it was extremely painful for the rest of the board, but mostly for the CEO . . . when it comes to the really difficult situations, [where] you think that the CEO has . . . done something criminal . . . [o]r you think that he has done something negligent, something that makes it such that you . . . are unsure whether he's the suitable person to be in the driving seat.[248]

Another director observed that ''[i]f you have different experiences and a more diversified board, you will have different questions asked.'' [249] Dhir concluded that ''women directors may be particularly adept at critically questioning, guiding and advising management without disrupting the overall working relationship between the board and management.'' [250]

Pucheta-Martínez et al. (2016) reasoned that questioning management is a critical part of the audit committee's oversight role, along with ensuring that management does not pressure the external auditor to issue a clean audit opinion notwithstanding the identification of any uncertainties or scope limitations.[251] Otherwise, ''[a]uditors may accept the demands of management for a clean audit report when the firm deserves a scope limitation and an uncertainty qualification.'' [252] The authors found that ''the percentage of female [directors] on [audit committees] reduces the probability of [audit] qualifications due to errors, non-compliance or the omission of information,'' [253] and further found a positive association between gender-diverse audit committees and disclosing audit reports with uncertainties and scope limitations. This suggests that gender-diverse audit committees better ''ensure that managers do not seek to pressure auditors into issuing a clean opinion instead of a qualified opinion'' when any uncertainties or scope limitations are identified.[254]

Nasdaq also reviewed other studies that found a positive association between board gender diversity and important investor protections regardless of whether women are on the audit committee, and considered the assessment of some academics that their findings may extend to other forms of diversity, including racial and ethnic diversity. Nasdaq therefore believes that such findings with respect to audit committees would be expected to be more broadly applicable to the quality of the broader board's decision-making process, and to other forms of diversity, including diversity of race, ethnicity and sexual orientation.

In examining the association between broader board gender diversity and fraud, Cumming, et al. observed that ''[g]ender diversity in particular facilitates more effective monitoring by the board and protection of shareholder interests by broadening the board's expertise, experience, interests, perspectives and creativity.'' [255] They observed that the presence of women on boards is associated with a lower likelihood of securities fraud; indeed, they found ''strong evidence of a negative and diminishing effect of women on boards and the probability of being in our fraud sample.'' [256] The authors suggested that ''other forms of board diversity, including but not limited to gender diversity, may likewise reduce fraud.'' [257]

Similarly, Wahid (2017) noted that board gender diversity may ''lead to less biased and superior decision-making'' because it ''has a potential to alter group dynamics by affecting cognitive conflict and cohesion.'' [258] Wahid (2017) concluded that ''gender-diverse boards commit fewer financial reporting mistakes and engage in less fraud,'' [259] finding that companies with female directors have ''fewer irregularity-type [financial] restatements, which tend to be indicative of financial manipulation.'' [260] Wahid also suggested that other forms of diversity, including

[244] *See* Forbes and Milliken, *supra* note 74, at 496.

[245] *See* Dhir, *supra* note 78, at 124.

[246] *See* Petition for Amendment of Proxy Rule, *supra* note 80, at 4.

[247] *See* Dhir, *supra* note 78, at 150.

[248] *Id.* at xiv.

[249] *Id.* at 120.

[250] *Id.* at 35.

[251] *See* Pucheta-Martínez et al., *supra* note 52, at 368.

[252] *Id.* at 364.

[253] *Id.* at 363.

[254] *Id.* at 368.

[255] *See* Cumming et al., *supra* note 62, at 34.

[256] *Id.* at 12–14.

[257] *Id.* at 33.

[258] *See* Wahid, *supra* note 59, at 6.

[259] *Id.* at 1.

[260] *Id.* at 23.

racial diversity, could introduce additional perspectives to the boardroom,[261] which Nasdaq believes could further mitigate groupthink.

Abbott, Parker and Persley (2012) posited that ''a female board presence contribut[es] to the board's ability to maintain an attitude of mental independence, diminish[es] the extent of groupthink and enhance[es] the ability of the board to monitor financial reporting.'' [262] They noted that ''poorer [internal] controls and the lack of an independent and questioning board-level attitude toward accounting judgments can create an opportunity for fraud.'' [263] They observed a lower likelihood of a material financial restatements stemming from fraud or error in companies with at least one woman on the board.[264]

Nasdaq believes that these studies provide substantial evidence suggesting an association between gender diverse boards or audit committees and a lower likelihood of fraud; a lower likelihood of receiving audit qualifications due to errors, non-compliance or omission of information; and a greater likelihood of disclosing audit reports with uncertainties and scope limitations. Moreover, academics have suggested that other forms of diversity, including racial and ethnic diversity, may reduce fraud and mitigate groupthink. Further, while homogenous boards may unwittingly fall into the trap of groupthink due to a lack of diverse perspectives, ''heterogeneous groups share conflicting opinions, knowledge, and perspectives that result in a more thorough consideration of a wide range of interpretations, alternatives, and consequences.'' [265] Nasdaq therefore believes that the proposed rule is designed to reduce groupthink, and otherwise to enhance the functioning of boards, and thereby to prevent fraudulent and manipulative acts and practices.

Further, the Commission has suggested that in seeking board diversity, ''[t]o the extent that boards branch out from the set of candidates they would ordinarily consider, they may nominate directors who have fewer existing ties to the board or management and are, consequently, more independent.'' [266] Nasdaq believes that the benefits of the proposed rule are analogous to the benefits of Nasdaq's rules governing and requiring director independence. In 2003, Nasdaq adopted listing rules requiring, among other things, that independent directors comprise a majority of listed companies' boards, which were ''intended to enhance investor confidence in the companies that list on Nasdaq.'' [267] The Commission observed that self-regulatory organizations ''play an important role in assuring that their listed issuers establish good governance practices,'' and concluded that the proposed rule changes would secure an ''objective oversight role'' for issuers' boards of directors, and ''foster greater transparency, accountability, and objectivity'' in that role.'' [268] Along the same lines, in approving Nasdaq's application for registration as a national securities exchange, the Commission found Nasdaq's rules governing the independence of members of boards and certain committees to be consistent with Section 6(b)(5) of the Act because they advanced the ''interests of shareholders'' in ''greater transparency, accountability, and objectivity'' in oversight and decision-making by corporate boards.[269] Nasdaq proposes to promote accountability in corporate decision-making by requiring companies who do not have at least two Diverse directors on their board to provide investors with a public explanation of the board's reasons for not doing so under Rule 5605(f)(3).

Nasdaq believes it is critical to the detection and prevention of fraudulent and manipulative acts and practices to have directors on the board who are willing to critically question management and air dissenting views. Nasdaq believes that boards comprised of directors from Diverse backgrounds enhance investor confidence by ensuring that board deliberations consider the perspectives of more than one demographic group, leading to robust dialogue and better decision making. However, Nasdaq recognizes that directors may bring diverse perspectives, skills and experiences to the board, notwithstanding that they have similar attributes. Nasdaq therefore believes it is in the public interest to permit a company that chooses not to meet the diversity objectives of Rule 5605(f)(2) to explain why it does not, in accordance with Rule 5605(f)(3)—for example, if it believes that defining diversity more broadly than Nasdaq, for example by considering national origin, veteran status and disabilities, brings a wide range of perspectives and experiences to the board. Nasdaq believes such disclosure will provide investors with a better understanding of the company's philosophy regarding diversity. This would better inform the investment community and enable more informed analyses of, and conversations with, companies. Therefore, Nasdaq believes satisfying Rule 5605(f)(2) through disclosure pursuant to Rule 5605(f)(3) is consistent with Section 6(b)(5) of the Act because it advances the ''interests of shareholders'' in ''greater transparency, accountability, and objectivity'' of boards and their decision-making processes.[270] In addition, as discussed further in Section II.A.2.II.c (*Promotes Investor Protection and the Public Interest*) below, Nasdaq believes that the proposed diversity requirement could help to reduce information asymmetry, and thereby reduce the risk of insider trading or other opportunistic insider behavior.

c. Promotes Investor Protection and the Public Interest

Nasdaq has found substantial evidence that board diversity is positively associated with more transparent public disclosures and higher quality financial reporting, thereby promoting investor protection. Specifically, studies have concluded that companies with gender-diverse boards are associated with more transparent public disclosures and less information asymmetry, leading to stock prices that better reflect public information. Gul, Srinidhi & Ng (2011) found that ''gender diversity improves stock price informativeness by increasing voluntary public disclosures in large firms and increasing the

[261] *Id.* at 24–25; *see also* Shecter, *supra* note 61 (quoting Wahid as saying that ''[i]f you're going to introduce perspectives, those perspectives might be coming not just from male versus female. They could be coming from people of different ages, from different racial backgrounds. . .. If we just focus on one, we could be essentially taking away from other dimensions of diversity and decreasing perspective.'').

[262] *See* Abbott et al., *supra* note 58, at 607.

[263] *Id.* at 610.

[264] *Id.* at 613 (''The previously discussed lines of research lead us to form our hypothesis. In summary, restatements may stem from error or fraud. In either instance, the internal control system (to which the board of directors contributes by setting the overall tone at the top) has failed to detect or prevent a misstatement. Ineffective internal controls may stem from insufficient questioning of assumptions underlying financial reporting, inadequate attention to the internal control systems, or insufficient support for the audit committee's activities.'').

[265] *See* Dallas, *supra* note 76, at 1391.

[266] *See* Proxy Disclosure Enhancements, *supra* note 73, 74 FR at 68,355.

[267] *See* Order Approving Proposed Rule Changes, 68 FR at 64,161.

[268] *Id.* at 64, 175.

[269] *See* In re Nasdaq Stock Market, 71 FR 3550, 3565 (Jan. 23, 2006). *See also* 68 FR 18,788, 18,815 (April 16, 2003) (in adopting Rule 10A–3, setting standards for the independence of audit committee members, the Commission concluded that such standards would ''enhance the quality and accountability of the financial reporting process and may help increase investor confidence, which implies increased efficiency and competitiveness of the U.S. capital markets'').

[270] *Id.*

incentives for private information collection in small firms.'' [271] Bravo and Alcaide-Ruiz (2019) found a positive association between women on the audit committee with financial or accounting expertise and the voluntary disclosure of forward-looking information.[272] Abad et al. (2017) concluded that companies with gender-diverse boards are associated with lower levels of information asymmetry, suggesting that ''the policies recently implemented in several European countries to increase the presence of female directors in company boards could have beneficial effects on stock markets by reducing the risk of informed trading and enhancing stock liquidity.'' [273]

Nasdaq believes that one consequence of information asymmetry is that insiders may engage in opportunistic behavior prior to a public announcement of financial results and before the market incorporates the new information into the company's stock price. This can result in unfair gains or an avoidance of losses at the expense of shareholders who did not have access to the same information. This may exacerbate the principal-agent problem, in which the interests of a company's board and shareholders are not aligned. Lucas-Perez et al. (2014) found that board gender diversity is positively associated with linking executive compensation plans to company performance,[274] which may be an effective mechanism to deter opportunistic behavior by management and better align their interests with those of their company's shareholders.[275]

Another concern is that ''[w]hen information asymmetry is high, stakeholders do not have sufficient resources, incentives, or access to relevant information to monitor managers' actions, which gives rise to the practice of earnings management.'' [276] Earnings management ''is generally defined as the practice of using discretionary accounting methods to attain desired levels of reported earnings.'' [277] Manipulating earnings is particularly concerning to investors because ''[i]f users of financial data are 'misled' by the level of reported income, then investors' allocation of resources may be inappropriate when based on the financial statements provided by management,'' [278] thereby undermining the efficacy of the capital formation process for investors who rely on such information to make informed investment and voting decisions.

Gull et al. (2018) [279] observe that overseeing management is a crucial component of investor protection, particularly with regard to earnings management:

> The role of the board of directors and board characteristics (*i.e.* board independence and gender diversity) is usually associated with the protection of shareholder interests. . .. This role is particularly crucial with regard to the issue of earnings management, in that one of the responsibilities of boards is to monitor management.[280]

The authors of that study found that the presence of female audit committee members with business expertise is associated with a lower magnitude of earnings management. Srinidhi, Gul and Tsui (2011) observed that better oversight of management combined with lower information asymmetry leads to better earnings quality. They noted that ''[e]arnings quality is an important outcome of good governance demanded by investors and therefore its improvement constitutes an important objective of the board.'' [281] They found that companies with women on the board, specifically on the audit committee, exhibit ''higher earnings quality'' and ''better reporting discipline by managers.'' [282] They concluded that ''including female directors on the board and the audit committee are plausible ways of improving the firm's reporting discipline and increasing investor confidence in financial statements.'' [283]

Chen, Eshleman and Soileau (2016) suggested that the relationship between gender diversity and higher earnings quality observed by Srinidhi, Gul and Tsui (2011) is ultimately driven by reduced internal control weaknesses, noting that ''prior literature has established a negative relationship between internal control weaknesses and earnings quality.'' [284] Internal control over financial reporting are procedures designed ''to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.'' [285] Weaknesses in internal controls can ''lead to poor financial reporting quality'' and ''more severe insider trading'' [286] or failure to detect a material misstatement. According to the PCAOB:

> A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis.[287]

A material misstatement can occur ''as a result of some type of inherent risk, whether fraud or error (*e.g.,* management's aggressive accounting practices, erroneous application of GAAP).'' [288] The failure to prevent or detect a material misstatement before financial statements are issued can require the company to reissue its financial statements and potentially face costly shareholder litigation. Chen et al. found that having at least one woman on the board (regardless of whether or not she is on the audit committee) ''may lead [a] to reduced likelihood of material weaknesses [in internal control over financial reporting],'' [289] and Abbott, Parker and Persley (2012) found ''a significant association between the presence of at least one woman on the board and a lower likelihood of [a material financial] restatement.'' [290] Notably, while the Sarbanes-Oxley Act (''SOX'') implemented additional measures to ensure that a company has robust internal controls, the findings of Abbott et al. were consistent among a sample of pre- and post-SOX restatements, suggesting that ''an additional, beneficial layer of independence in group decision-making is associated with gender diversity.'' [291]

Nasdaq believes that the proposal to require listed companies to have at least two Diverse directors under Rule 5605(f) could help to lower information asymmetry and reduce the risk of insider trading or other opportunistic insider behavior, which would help to increase stock price informativeness and enhance stock liquidity, thereby protecting investors and promoting capital formation and efficiency. Nasdaq

[271] *See* Gul et al., *supra* note 66, at 2.

[272] *See* Bravo and Alcaide-Ruiz, *supra* note 56, at 151.

[273] *See* Abad et al., *supra* note 67, at 202.

[274] *See* Lucas-Perez et al., *supra* note 69.

[275] *Id.*

[276] *See* Vernon J. Richardson, *Information Asymmetry and Earnings Management: Some Evidence,* 15 Rev. Quantitative Fin. and Acct. 325 (2000).

[277] *See* Gull et al., *supra* note 55, at 2.

[278] *Id.*

[279] *See generally id.*

[280] *Id.* at 6 (citations omitted).

[281] *See* Srinidhi et al., *supra* note 50, at 1638.

[282] *Id.* at 1612.

[283] *Id.*

[284] *See* Chen et al., *supra* note 64, at 18.

[285] *See* Public Company Accounting Oversight Board, *Auditing Standard No. 5: Appendix A,* A5 available at: *https://pcaobus.org/oversight/standards/archived-standards/details/Auditing_Standard_5_Appendix_A.*

[286] *See* Chen et al., *supra* note 64, at 12.

[287] *See* Public Company Accounting Oversight Board, *supra* note 285, at A7.

[288] *See* Abbott et al., *supra* note 58, at 609–10.

[289] *See* Chen et al., *supra* note 64, at 18.

[290] *See* Abbott et al., *supra* note 58, at 607.

[291] *Id.* at 609.

believes that information asymmetry could also be reduced by permitting companies to satisfy Rule 5605(f)(2) by publicly disclosing their reasons for not meeting its diversity objectives in accordance with Rule 5605(f)(3), because the requirement will improve the quality of information available to investors who rely on this information to make informed investment and voting decisions, which will further protect investors and promote capital formation and efficiency.

Moreover, Nasdaq believes that proposed Rule 5605(f) could foster more transparent public disclosures, higher quality financial reporting, and stronger internal control over financial reporting and mechanisms to monitor management. This could be particularly beneficial for Smaller Reporting Companies that are not subject to the SOX 404(b) requirement to obtain an independent auditor's attestation of management's assessment of the effectiveness of internal control over financial reporting, thereby promoting investor protection.

Nasdaq believes that the body of research on the relationship between economic performance and board diversity summarized under Section II.A.1.II.a above provides substantial evidence supporting the conclusion that board diversity does not have adverse effects on company financial performance, and therefore Nasdaq believes the proposal will not negatively impact capital formation, competition or efficiency among its public companies.[292] Nasdaq considered that some studies on gender diversity alone have had mixed results,[293] and that the U.S. GAO (2015) and Carter et al. (2010) concluded that the mixed results are due to differences in methodologies, data samples and time periods.[294] This is not the first time Nasdaq has considered whether, on balance, various studies finding mixed results related to board composition and company performance are sufficient rationale to propose a listing rule. For example, in 2003, notwithstanding the mixed results of studies regarding the relationship between company performance and board independence,[295] Nasdaq adopted listing rules requiring a majority independent board that were ''intended to enhance investor confidence in the companies that list on Nasdaq.'' [296] In its Approval Order, the SEC noted that ''[t]he Commission has long encouraged exchanges to adopt and strengthen their corporate governance listing standards in order to, among other things, enhance investor confidence in the securities markets;'' the Commission concluded that the independence rules would secure an ''objective oversight role'' for issuers' boards, and ''foster greater transparency, accountability, and objectivity'' in that role.[297] Nasdaq believes this reasoning applies to the current proposed rule as well. Even without clear consensus among studies related to board diversity and company performance, the heightened focus on corporate board diversity by investors demonstrates that investor confidence is undermined when data on board diversity is not readily available and when companies do not explain the reasons for the apparent absence of diversity on their boards.[298] Legislators are increasingly taking action to encourage corporations to diversify their boards and improve diversity disclosures.[299] Moreover, during its discussions with stakeholders, Nasdaq found consensus across every constituency that there is inherent value in board diversity. Lastly, it has been a longstanding principle that ''Nasdaq stands for integrity and ethical business practices in order to enhance investor confidence, thereby contributing to the financial health of the economy and supporting the capital formation process.'' [300]

For all the foregoing reasons, Nasdaq believes that proposed Rule 5605(f) will promote investor protection and the public interest by enhancing investor confidence that all listed companies are considering diversity in the context of selecting directors, either by including at least two Diverse directors on their boards or by explaining their rationale for not meeting that objective. To the extent a company chooses not to meet the diversity objectives of Rule 5605(f)(2), Nasdaq believes that the proposal will provide investors with additional disclosure about the company's reasons for doing so under Rule 5605(f)(3). For example, the company may choose to disclose that it does not meet the diversity objectives of Rule 5605(f)(2) because it is subject to an alternative standard under state or foreign laws and has chosen to satisfy that diversity objective instead. On the other hand, many firms may strive to achieve even greater diversity than the objectives set forth in our proposed rule. Nasdaq believes that providing such flexibility and clear disclosure where the company determines to follow a different path will improve the quality of information available to investors who rely on this information to make informed investment and voting decisions, thereby promoting capital formation and efficiency, and further promoting the public interest.

d. Not Designed to Permit Unfair Discrimination Between Customers, Issuers, Brokers, or Dealers

Nasdaq believes that proposed Rule 5605(f) is not designed to permit unfair discrimination among companies because it requires all companies subject to the rule to have at least two Diverse directors or explain why they do not. Further, the proposal requires at least one of the two Diverse directors to be an individual who self-identifies as Female. While the proposal provides different requirements for the second Diverse director among Smaller Reporting Companies, Foreign Issuers and other companies, Nasdaq believes that the rule is not designed to permit unfair discrimination among companies. In all cases, a company can choose to meet the diversity objectives of the entire rule or to satisfy only certain elements of the rule. Further, the proposed rule does not limit board sizes—if a board chooses to nominate a Diverse individual to the board to meet the diversity objectives of the proposed rule, it is not precluded from also nominating a non-Diverse director for an additional board seat.

[292] *See* Alexandre Di Miceli and Angela Donaggio, *Women in Business Leadership Boost ESG Performance: Existing Body of Evidence Makes Compelling Case,* 42 International Finance Corporation World Bank Group, Private Sector Opinion at 11 n.15 (2018), available at: *https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+cg/resources/private+sector+opinion/women+in+business+leadership+boost+esg+performance* (''The overwhelming majority of empirical studies conclude that a higher ratio of women in business leadership does not impair corporate performance (virtually all studies find positive or non-statistically significant results)''). *See also* Wahid, *supra* note 59, at 6 (suggesting that ''at a minimum, gender diversity on corporate boards has a neutral effect on governance quality, and at best, it has positive consequences for boards' ability to monitor firm management'').

[293] *See, e.g.,* Pletzer et al., *supra* note 38; Post and Byron, *supra* note 39; Adams and Ferreira, *supra* note 42.

[294] *See* GAO Report, *supra* note 44, at 5 (''Some research has found that gender diverse boards may have a positive impact on a company's financial performance, but other research has not. These mixed results depend, in part, on differences in how financial performance was defined and what methodologies were used''); Carter (2010), *supra* note 40, at 400 (observing that the different ''statistical methods, data, and time periods investigated vary greatly so that the results are not easily comparable.'').

[295] *See supra* note 45.

[296] *See* Order Approving Proposed Rule Changes, 68 FR at 64,161.

[297] *Id.* at 64,176.

[298] *See supra* notes 4 and 8.

[299] *See supra* note 112.

[300] *See* Nasdaq Rulebook, Rule 5101.

i. Rule 5605(f)(2)(B): Foreign Issuers

Similar to all other companies subject to Rule 5605(f), the proposal requires all Foreign Issuers to have, or explain why they do not have, at least two Diverse directors, including one director who self-identifies as Female. However, Nasdaq proposes to provide Foreign Issuers with additional flexibility with regard to the second Diverse director. Foreign Issuers could satisfy the second director objective by including another Female director, or an individual who self-identifies as LGBTQ+ or as an underrepresented individual based on national, racial, ethnic, indigenous, cultural, religious or linguistic identity in the company's home country jurisdiction. While the proposal provides a different requirement for the second Diverse director for Foreign Issuers, Nasdaq believes it is not designed to permit unfair discrimination between Foreign Issuers and other companies because it recognizes that the unique demographic composition of the United States, and its historical marginalization of Underrepresented Minorities and the LGBTQ+ community, may not extend to all countries outside of the United States. Further, Nasdaq believes that it is challenging to apply a consistent definition of minorities to all countries globally because ''[t]here is no internationally agreed definition as to which groups constitute minorities.'' [301] Similarly, ''there is no universally accepted international definition of indigenous peoples.'' [302] Rather, the United Nations *Declaration on the Rights of Indigenous Peoples* recognizes ''that the situation of indigenous peoples varies from region to region and from country to country and that the significance of national and regional particularities and various historical and cultural backgrounds should be taken into consideration.'' [303] Accordingly, Nasdaq believes that it is not unfairly discriminatory to allow an alternative mechanism for Foreign Issuers to satisfy Rule 5605(f)(2) in recognition that the U.S.-based EEOC definition of Underrepresented Minorities is not appropriate for every Foreign Issuer. In addition, Foreign Issuers have the ability to satisfy Rule 5605(f)(2)(B) by explaining that they do not satisfy this alternative definition. Similarly, any company that is not a Foreign Issuer, but that prefers the alternative definition available for Foreign Issuers, could follow Rule 5605(f)(2)(B) and disclose its reasons for doing so.

Under the proposal, Foreign Issuer means (a) a Foreign Private Issuer (as defined in Rule 5005(a)(19)) or (b) a company that (i) is considered a ''foreign issuer'' under Rule 3b–4(b) under the Act, and (ii) has its principal executive offices located outside of the United States. For example, a company that is considered a ''foreign issuer'' under Rule 3b–4(b) under the Act and has its principal executive offices located in Ireland would qualify as a Foreign Issuer for purposes of Rule 5605(f)(2), even if it is not considered a Foreign Private Issuer under Nasdaq or SEC rules.

Nasdaq recognizes that Foreign Issuers may be located in jurisdictions that impose privacy laws limiting or prohibiting self-identification questionnaires, particularly as they relate to race or ethnicity. In such countries, a company may not be able to determine each director's self-identified Diverse attributes due to restrictions on the collection of personal information. The company may instead publicly disclose pursuant to Rule 5605(f)(3) that ''Due to privacy laws in the company's home country jurisdiction limiting its ability to collect information regarding a director's self-identified Diverse attributes, the company is not able to determine that it has two Diverse directors as set forth under Rule 5605(f)(2)(B)(ii).''

ii. Rule 5605(f)(2)(C): Smaller Reporting Companies

While the proposal provides a different requirement for the second Diverse director for Smaller Reporting Companies, Nasdaq believes that this distinction is not designed to permit unfair discrimination among companies. Nasdaq has designed the proposed rule to ensure it does not have a disproportionate economic impact on Smaller Reporting Companies by imposing undue costs or burdens. Nasdaq recognizes that Smaller Reporting Companies, especially pre-revenue companies that depend on the capital markets to fund ground-breaking research and technological advancements, may not have the resources to compensate an additional director or engage a search firm to find director candidates outside of the directors' traditional networks. Nasdaq believes that this is a reasonable basis to distinguish Smaller Reporting Companies from other companies subject to the rule.

Smaller Reporting Companies already are provided certain exemptions from Nasdaq's listing rules. For example, under Rule 5605(d)(3), Smaller Reporting Companies must have a compensation committee comprised of at least two independent directors and a formal written compensation committee charter or board resolution that specifies the committee's responsibilities and authority, but such companies are not required to grant authority to the committee to retain or compensate consultants or advisors or consider certain independence factors before selecting such advisors, consistent with Rule 10C–1 of the Act.[304] In its approval order, the SEC concluded as follows:

> The Commission believes that these provisions are consistent with the Act and do not unfairly discriminate between issuers. The Commission believes that, for similar reasons to those for which Smaller Reporting Companies are exempted from the Rule 10C–1 requirements, it makes sense for Nasdaq to provide some flexibility to Smaller Reporting Companies regarding whether the compensation committee's responsibilities should be set forth in a formal charter or through board resolution. Further . . . in view of the potential additional costs of an annual review, it is reasonable not to require a Smaller Reporting Company to conduct an annual assessment of its charter or board resolution.[305]

The Commission also makes accommodations for Smaller Reporting Companies based on their more limited resources, allowing them to comply with scaled disclosure requirements in certain SEC reports rather than the more rigorous disclosure requirements for larger companies. For example, Smaller Reporting Companies are not required to include a compensation discussion and analysis in their proxy or Form 10–K describing the material elements of the compensation of its named executive officers.[306] Eligible Smaller Reporting Companies also are relieved from the SOX 404(b) requirement to obtain an independent auditor's attestation of management's assessment of the effectiveness of internal control over

[301] *See* United Nations, *Minority Rights: International Standards and Guidance for Implementation* 2 (2010), available at: *https://www.ohchr.org/Documents/Publications/MinorityRights_en.pdf. See also* G.A. Res. 47/135. art. 1.1 (Dec. 18, 1992) (''States shall protect the existence and the national or ethnic, cultural, religious and linguistic identity of minorities within their respective territories and shall encourage conditions for the promotion of that identity.''). The preamble to the Declaration also ''[r]eaffirm[s] that one of the basic aims of the United Nations, as proclaimed in the Charter, is to promote and encourage respect for human rights and for fundamental freedoms for all, without distinction as to race, sex, language or religion.''

[302] *See* United Nations, *Minority Rights, supra* note 301, at 3.

[303] *See* G.A. Res. 61/295 (Sept. 13, 2007).

[304] *See* Nasdaq Rulebook, Rule 5605(d)(3).

[305] *See* Order Granting Accelerated Approval of Proposed Rule Change, 78 FR 4,554, 4,567 (Jan. 22, 2013).

[306] *See* 17 CFR 229.402(l).

financial reporting.[307] In each case, companies may choose to comply with the more rigorous requirements in lieu of relying on the exemptions.

Any company that is not a Smaller Reporting Company, but prefers the alternative rule available for Smaller Reporting Companies, could follow Rule 5605(f)(2)(C) and disclose their reasons for doing so. As such, Nasdaq believes that the proposed alternative rule for Smaller Reporting Companies is not designed to, and does not, unfairly discriminate among companies. Lastly, Nasdaq believes that Rule 5605(f)(2)(C) is not designed to permit unfair discrimination among companies because it requires Smaller Reporting Companies to have at least one director who self-identifies as Female, similar to other companies subject to Rule 5065(f).

iii. Rule 5605(f)(3): Public Disclosure of Non-Diverse Board

Under proposed Rule 5605(f)(3), if a company determines not to meet the diversity objectives of Rule 5605(f) in its entirety, it must specify the applicable requirements of the Rule and explain its reasons for not having at least two Diverse directors. Nasdaq designed the proposal to avoid unduly burdening competition or efficiency, or conflicting with existing securities laws, by providing all companies subject to Rule 5605(f) with the option to make the public disclosure required under Rule 5605(f)(3) in the company's proxy statement or information statement for its annual meeting of shareholders or, alternatively on the company's website, provided that the company submits a URL link to such disclosure to Nasdaq through the Listing Center no later than 15 calendar days after the company's annual shareholder meeting. Nasdaq believes Rule 5605(f)(3) is not designed to permit unfair discrimination among companies because the proposed rule provides all companies subject to Rule 5605(f) the option to disclose an explanation rather than meet the diversity objectives of Rule 5605(f)(2).

Certain federal securities laws similarly permit companies to satisfy corporate governance requirements through disclosure of reasons for not meeting the applicable requirement. For example, under Regulation S–K, Item 407 requires a company to disclose whether or not its board of directors has determined that the company has at least one audit committee financial expert. If a company does not have a financial expert on the audit committee, it must provide an explanation.[308] Item 406 requires a company to disclose whether it has adopted a written code of ethics that applies to the chief executive officer and senior financial or accounting officers. If a company has not adopted such a code of ethics, it must disclose the reasons why not.[309] Item 402 regarding pay ratio disclosure defines how total compensation for employees should be calculated, but permits companies to use a different measure as long as they explain their approach.[310]

Furthermore, Nasdaq rules and SEC guidance already recognize that website disclosure can be a method of disseminating information to the public. For example, Nasdaq listing rules permit companies to provide website disclosures related to third party director compensation,[311] foreign private issuer home country practices,[312] and reliance on the exception relating to independent compensation committee members.[313] The SEC has recognized that "[a] company's website is an obvious place for investors to find information about the company" [314] and permits companies to make public disclosure of material information through website disclosures if, among other things, the company's website is "a recognized channel of distribution of information." [315]

iv. Rule 5605(f)(4): Exempt Companies

Under proposed Rule 5605(f)(4), Nasdaq proposes to exempt the following types of companies from the requirements of Rule 5605(f) (defined as "Exempt Companies"): acquisition companies listed under IM–5101–2; asset-backed issuers and other passive issuers (as set forth in Rule 5615(a)(1)); cooperatives (as set forth in Rule 5615(a)(2)); limited partnerships (as set forth in Rule 5615(a)(4)); management investment companies (as set forth in Rule 5615(a)(5)); issuers of non-voting preferred securities, debt securities and Derivative Securities (as set forth in Rule 5615(a)(6)); and issuers of securities listed under the Rule 5700 Series. Each of the types of Exempt Companies either has no board of directors, lists only securities with no voting rights towards the election of directors, or is not an operating company, and the holders of the securities they issue do not expect to have a say in the composition of their boards. As such, Nasdaq believes the proposal is not designed to permit unfair discrimination by excluding Exempt Companies from the application of proposed Rule 5605(f). These companies already are exempt from certain of Nasdaq's corporate governance standards related to board composition, as described in Rule 5615.

v. Rule 5605(f)(5): Phase-in Period

Proposed Rule 5605(f)(5)(A) will allow any newly listing company that was not previously subject to a substantially similar requirement of another national securities exchange one year from the date of listing to satisfy the requirements of Rule 5605(f). Proposed Rule 5605(f)(5)(B) also will allow any company that ceases to be a Foreign Issuer, a Smaller Reporting Company or an Exempt Company one year from the date that the company no longer qualifies as a Foreign Issuer, a Smaller Reporting Company or an Exempt Company, respectively, to satisfy the requirements of Rule 5605(f). This phase-in period will apply after the end of the transition period provided in Rule 5605(f)(7).

Nasdaq believes this approach is not designed to permit unfair discrimination because it provides all companies that become newly subject to the rule the same time period within which to comply. In addition, this approach is similar to other phase-in periods granted to companies listing on or transferring to Nasdaq. For example, Rule 5615(b)(1) provides a company listing in connection with its initial public offering one year to fully comply with the compensation and nomination committee requirements of Rules 5605(d) and (e), and the majority independent board requirement of Rule 5605(b). Similarly, SEC Rule 10A–3(b)(1)(iv)(A) allows a company up to one year from the date its registration statement is effective to fully comply with the applicable audit committee composition requirements. Nasdaq Rule 5615(b)(3) provides a one-year timeframe for compliance with the board composition requirements for companies transferring from other listed markets that do not have a substantially similar requirement.

[307] *See* Accelerated Filer and Large Accelerated Filer Definitions, 85 FR 17,178 (March 26, 2020).

[308] *See* 17 CFR 229.407(d)(5).

[309] *Id.* § 229.406(a).

[310] *Id.* § 229.402.

[311] *See* Nasdaq Rulebook, Rule 5250(b)(3)(A).

[312] *Id.,* Rule 5615(a)(3)(B) and IM–5615–3.

[313] *Id.,* Rules 5605(d)(2)(B) (non-independent compensation committee member under exceptional and limited circumstances) and 5605(e)(3) (non-independent nominations committee member under exceptional and limited circumstances).

[314] *See* Commission Guidance on the Use of Company websites, 73 FR 45,862, 45,864 (Aug. 7, 2008).

[315] *Id.* at 45,867.

vi. Rule 5605(f)(7): Effective Dates/ Transition

Under proposed Rule 5605(f)(7), each company must have, or explain why it does not have, one Diverse director no later than two calendar years after the Approval Date,[316] and two Diverse directors no later than (i) four calendar years after the Approval Date for companies listed on the NGS or NGM tiers, or (ii) five calendar years after the Approval Date for companies listed on the NCM tier.

Nasdaq believes this approach is not designed to permit unfair discrimination because it recognizes that companies listed on the Nasdaq Capital Market may not have the resources necessary to compensate an additional director or engage a search firm to search for director candidates outside of the directors' traditional networks. Therefore, Nasdaq believes it is in the public interest to provide such companies with one additional year to meet the diversity objectives of Rule 5605(f), should they choose to do so. Nasdaq notes that all companies may choose to follow a timeframe applicable to a different market tier, provided they publicly describe their explanation for doing so. They also may construct their own timeframe for meeting the diversity objectives of Rule 5605(f), provided they publicly disclose their reasons for not abiding by Nasdaq's timeframe.

e. Not Designed to Regulate by Virtue of any Authority Conferred by the Act Matters Not Related to the Purposes of the Act or the Administration of the Exchange

Nasdaq believes that the proposal is not designed to regulate by virtue of any authority conferred by the Act matters not related to the purposes of the Act or the administration of the Exchange.[317] The proposal relates to the Exchange's corporate governance standards for listed companies. As discussed above, ''[t]he Commission has long encouraged exchanges to adopt and strengthen their corporate governance listing standards in order to, among other things, enhance investor confidence in the securities markets.'' [318] And because ''it is not always feasible to define . . . every practice which is inconsistent with the public interest or with the protection of investors,'' the Act leaves to SROs ''the necessary work'' of rulemaking pursuant to Section 6(b)(5).[319]

Nasdaq recognizes that U.S. states are increasingly proposing and adopting board diversity requirements, and because corporations are creatures of state law, some market participants may believe that such regulation is best left to states. However, Nasdaq considered that certain of its listing rules related to corporate governance currently relate to areas that are also regulated by states. For example, states impose standards related to quorums [320] and shareholder approval of certain transactions,[321] which also are regulated under Nasdaq's listing rules.[322] Nasdaq has adopted rules relating to such matters to ensure uniformity of such rules among its listed companies. Similarly, Nasdaq believes that the proposed rule will create uniformity among listed companies by helping to assure investors that all non-exempt companies have at least two Diverse directors on their board or publicly describe why they do not.

Further, Nasdaq believes the proposal will enhance investor confidence that listed companies that have two Diverse directors are considering the perspectives of more than one demographic group, leading to robust dialogue and better decision making, as well as the other corporate governance benefits of diverse boards discussed above in Section II.A.1.II. To the extent companies choose to disclose their reasons for not meeting the diversity objectives of Rule 5605(f)(2) pursuant to Rule 5605(f)(3), Nasdaq believes that such disclosure will improve the quality of information available to investors who rely on this information to make an informed voting decision, thereby promoting capital formation and efficiency. It has been the Exchange's longstanding principle that ''Nasdaq stands for integrity and ethical business practices in order to enhance investor confidence, thereby contributing to the financial health of the economy and supporting the capital formation process.'' [323]

In addition, as discussed in Section II.A.1.I, in passing Section 342 of the Dodd-Frank Act, Congress recognized the need to respond to the lack of diversity in the financial services industry, and the Standards designed by the Commission and other financial regulators provide a framework for addressing that industry challenge. The Standards themselves identify several focus areas, including the importance of ''Organizational Commitment,'' which speaks to the critical role of senior leadership—including boards of directors—in promoting diversity and inclusion across an organization. In addition, like the proposed rule, the Standards also consider ''Practice to Promote Transparency,'' and recognize that transparency is a key component of any diversity initiative. Specifically, the Standards provide that the ''transparency of an entity's diversity and inclusion program promotes the objectives of Section 342,'' and also is important because it provides the public with necessary information to assess an entity's diversity policies and practices.[324]

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. Nasdaq reviewed requirements related to board diversity in two dozen foreign jurisdictions, and almost every jurisdiction imposes diversity-focused requirements on listed companies, either through a securities exchange, financial regulator or the government. Nasdaq competes for listings globally, including in countries that have implemented a more robust regulatory reporting framework for diversity and ESG disclosures. Currently in the U.S., the Long Term Stock Exchange (''LTSE''), which includes a number of sponsors which have investment businesses, has communicated to institutional investors that it that it seeks to distinguish itself by focusing on corporate governance, including, for example, diversity and inclusion. Under Rule 14.425, companies listed on LTSE must adopt and publish a long-term stakeholder policy that explains, among other things, ''the Company's approach to diversity and inclusion.'' [325]

[316] The ''Approval Date'' is the date that the SEC approves the proposed rule.

[317] *See* 15 U.S.C. 78f(b)(5).

[318] *See* Order Approving Proposed Rule Changes, 68 FR at 64,161.

[319] *See Heath* v. *SEC,* 586 F.3d 122, 132 (2d Cir. 2009) (citing *Avery* v. *Moffat,* 55 N.Y.S.2d 215, 228 (Sup. Ct. 1945)).

[320] *See, e.g.,* 8 Del. Code § 216 (providing that a quorum at a shareholder's meeting shall consist of no less than ⅓ of the shares entitled to vote at such meeting).

[321] *See, e.g., id.* §§ 251, 271 (providing that shareholder approval by a majority of the outstanding voting shares entitled to vote is required for mergers and the sale of all or substantially all of a corporation's assets).

[322] *See, e.g.,* Nasdaq Rulebook, Rules 5620(c) and 5635(a).

[323] *Id.,* Rule 5101.

[324] Final Interagency Policy Statement Establishing Joint Standards for Assessing the Diversity Policies and Practices of Entities Regulated by the Agencies, 80 FR 33,016 (June 10, 2015).

[325] *See* Long-Term Stock Exchange Rule Book, Rule 14.425.

I. Board Statistical Disclosure

The Exchange does not believe that proposed Rule 5606 will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. Specifically, the Exchange believes that the adoption of Rule 5606 will not impose any undue burden on competition among listed companies for the reasons set forth below.

With a few exceptions, all companies would be required to make the same disclosure of their board-level statistical information. The average board size of a company that is currently listed on the Exchange is eight directors. Although a company would be required to disclose its board-level statistical data, directors may choose to opt out rather than reveal their diversity characteristics to their company. A company would identify such directors in the ''Undisclosed'' category. For directors who voluntarily disclose their diversity characteristics, the company would collect their responses and disclose the information in either the company's proxy statement, information statement of shareholder meeting or on the company's website, using Nasdaq's required format. While the time and economic burden may vary based on a company's board size, Nasdaq does not believe there is any significant burden associated with gathering, preparing and reporting this data. Therefore, Nasdaq believes that there will be a *de minimis* time and economic burden on listed companies to collect and disclose the diversity statistical data.

Some investors value demographic diversity, and list it as an important factor influencing their director voting decisions.[326] Investors have stated that consistent data would make its collection and analysis easier and more equitable for investors that are not large enough to demand or otherwise access individualized disclosures.[327] Therefore, Nasdaq believes that any burden placed on companies to gather and disclose their board-level diversity statistics is counterbalanced by the benefits that the information will provide to a company's investors.

Moreover, as discussed above, most listed companies are required to submit an annual EEO–1 Report, which provides statistical data related to race and gender data among employees similar to the data required under proposed Rule 5606(a). Because most companies are already collecting similar information annually to satisfy their EEOC requirement, Nasdaq does not believe that adding directors to the collection will place a significant burden on these companies. Additionally, the information requested from Foreign Issuers is limited in scope and therefore does not impose a significant burden on them.

Nasdaq faces competition in the market for listing services. Proposed Rule 5606 reflects that competition, but it does not impose any burden on competition with other exchanges. As discussed above, investors have made clear their desire for greater transparency into public companies' board-level diversity as it relates to gender identity, race, and ethnicity. Nasdaq believes that the proposed rule will enhance the competition for listings. Other exchanges can set similar requirements for their listed companies, thereby increasing competition to the benefit of those companies and their shareholders. Accordingly, Nasdaq does not believe the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

II. Diverse Board Representation or Explanation

Nasdaq believes that proposed Rule 5605(f) will not impose burdens on competition among listed companies because the Exchange has constructed a framework for similarly-situated companies to satisfy similar requirements (*i.e.,* Foreign Issuers, Smaller Reporting Companies and other companies), and has provided all companies with the choice of satisfying the requirements of Rule 5605(f)(2) by having at least two Diverse directors, or by explaining why they do not. Nasdaq believes that this will avoid imposing undue costs or burdens on companies that, for example, cannot afford to compensate an additional director or believe it is not appropriate, feasible or desirable to meet the diversity objectives of Rule 5605(f) based on the company's particular circumstances (for example, the company's size, operations or current board composition). Rather than requiring a company to divert resources to compensate an additional director, and place the company at a competitive disadvantage with its peers, the rule provides the flexibility for such company to explain why it does not meet the diversity objective.

The cost of identifying director candidates can range from nothing or a nominal fee (via personal, work or school-related networks, or board affinity organizations, as well as internal research by the corporate secretary's team) to amounts that can vary widely depending on the specific search firm and the size of the company. Some industry observers estimate board searches for independent directors cost about one-third of a director's annual compensation, while others estimate it costs between $75,000 and $150,000. The underlying figures vary; for example, one search firm generally charges $25,000 to $50,000. Nasdaq observes that total annual director compensation can range widely; median director pay is estimated at $134,000 for Russell 3000 companies and $232,000 for S&P 500 companies. Moreover, there is a wider range of underlying compensation amounts. For example, Russell 3000 directors may receive approximately $32,600 (10th percentile), or up to $250,000 (90th percentile) or more. S&P 500 directors may receive approximately $100,000 (10th percentile) or up to $310,000 (90th percentile) or more.[328] Most, if not all, of these costs would be borne in any event in the search for new directors regardless of the proposed rule. While the proposed rule might lead some companies to search for director candidates outside of already established networks, the incremental costs of doing so would be tied directly to the benefit of a broader search.

To reduce costs for companies that do not currently meet the diversity objectives of Rule 5605(f)(2), Nasdaq is proposing to provide listed companies that have not yet met their diversity objectives with free access to a network of board-ready diverse candidates and a tool to support board evaluation, benchmarking and refreshment. This offering is designed to ease the search for diverse nominees and reduce the costs on companies that choose to meet the diversity objectives of Rule 5605(f)(2). Nasdaq is contemporaneously submitting a rule filing to the Commission regarding the provision of such services. Nasdaq also plans to publish FAQs on its Listing Center to provide guidance to companies on the application of the proposed rules, and to establish a dedicated mailbox for companies and their counsel to email additional questions to Nasdaq regarding the application of the proposed rule. Nasdaq believes that these services will

[326] *See* Hunt et al., *supra* note 26.

[327] *See* Petition for Rulemaking, *supra* note 123, at 2.

[328] Total annual director compensation varies by compensation elements and structure as well as amount, which is generally based on the size, sector, maturity of the company, and company specific situation. *See* Mark Emanuel et al., Semler Brossy and the Conference Board, *Director Compensation Practices in the Russell 3000 and S&P 500* (2020 ed.), available at *https://conferenceboard.esgauge.org/directorcompensation/report.*

help to ease the compliance burden on companies whether they choose to meet the listing rule's diversity objectives or provide an explanation for not doing so.

Nasdaq also has structured the proposed rule to provide companies with at least four years from the Approval Date to satisfy Rule 5605(f)(2) so that companies do not incur immediate costs striving to meet the diversity objectives of Rule 5605(f)(2). Nasdaq also has reduced the compliance burden on Smaller Reporting Companies and Foreign Issuers by providing them with additional flexibility when satisfying the requirement related to the second Diverse director. Smaller Reporting Companies could satisfy the proposed diversity objective to have two Diverse directors under Rule 5605(f)(2)(C) with two Female directors. Like other companies, Smaller Reporting Companies also could satisfy the second director objective by including an individual who self-identifies as an Underrepresented Minority or a member of the LGBTQ+ community. Foreign Issuers could satisfy the second director objective by including another Female director, or an individual who self-identifies as LGBTQ+ or an underrepresented individual based on national, racial, ethnic, indigenous, cultural, religious or linguistic identity in the company's home country jurisdiction. Nasdaq has further reduced the compliance burdens on companies listed on the Nasdaq Capital Market tier by providing them with five years from the Approval Date to satisfy Rule 5605(f)(2), recognizing that such companies may face additional challenges and resource constraints when identifying additional director nominees who self-identify as Diverse.

For the foregoing reasons, Nasdaq does not believe that proposed Rule 5605(f) will impose any burden on competition among issuers that is not necessary or appropriate in furtherance of the purposes of the Act. Further, Nasdaq does not believe the proposed rule will impose any burden on competition among listing exchanges. As described above, Nasdaq competes with other exchanges globally for listings, including exchanges based in jurisdictions that have implemented disclosure requirements related to diversity. Within the United States, LTSE requires listed companies to adopt and publish a long-term stakeholder policy that explains, among other things, ''the Company's approach to diversity and inclusion.'' [329] Other listing venues within the United States may propose to adopt rules similar to LTSE's requirements or the Exchange's proposal if they believe companies would prefer to list on an exchange with diversity-related listing standards.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve or disapprove the proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's internet comment form (*http://www.sec.gov/rules/sro.shtml*); or
- Send an email to *rule-comments@sec.gov.* Please include File Number SR–NASDAQ–2020–081 on the subject line.

Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–1090.

All submissions should refer to File Number SR–NASDAQ–2020–081. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website (*http://www.sec.gov/rules/sro.shtml*). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–NASDAQ–2020–081, and should be submitted on or before January 4, 2021.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[330]

J. Matthew DeLesDernier,

Assistant Secretary.

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[329] *See* Long-Term Stock Exchange Rule Book, Rule 14.425.

[330] 17 CFR 200.30–3(a)(12).