

**MEMO# 33721**

August 9, 2021

## **DEI: SEC Issues Order on Nasdaq Diversity Listing Rules**

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TO: ICI Members  
Investment Company Directors  
Diversity and Inclusion Committee  
Equity Markets Advisory Committee  
ESG Advisory Group  
Investment Advisers Committee  
SEC Rules Committee SUBJECTS: ESG  
Fund Governance RE: DEI: SEC Issues Order on Nasdaq Diversity Listing Rules

On August 6, the Securities and Exchange Commission issued an order approving Nasdaq's proposed rule changes on diverse representation on corporate boards and associated reporting for companies listed on its exchange.[\[1\]](#) With these new rules, Nasdaq aims to provide consistent, comparable data regarding diversity for investors and corporate stakeholders and to enhance corporate governance. The rules exempt management investment companies, asset-backed issuers, limited partnerships, and certain other issuers that do not list equities from the new requirements.

The Commission's order approves two new Nasdaq listing rules.[\[2\]](#)

- New rule 5605(f) (Diverse Board Representation) in general will set an objective for Nasdaq-listed companies to have at least one director who self-identifies as female and have at least one director who self-identifies in racial, ethnic, or sexual identity diversity categories, or explain the absence of such directors. Companies with five or fewer directors will be required to have one diverse director or explain the absence. Companies that fail to adhere to the rule will have a period to cure any deficiency identified by Nasdaq before the exchange issues a delisting letter.
- New rule 5606 (Board Diversity Disclosure) in general will require listed companies to provide aggregated data on their boards' gender, racial, ethnic, and sexual identity demographics. Specifically, each company will annually provide its board-level data in a matrix that includes the number of directors who identify as female, male, or non-binary, who meet racial and ethnic demographic categories,[\[3\]](#) who identify as LGBTQ+, or who did not disclose their demographic background. If a company fails to

adhere to rule 5606, Nasdaq will notify the company and allow the company 45 calendar days to submit a plan to regain compliance, with the possibility of an extension. If the company does not submit a plan or regain compliance within the applicable time periods, Nasdaq staff will issue a delisting letter.

The Commission notes that the new rules will establish a disclosure-based framework and provide consistent and comparable statistics to investors about the diversity of directors serving on a Nasdaq-listed company's board. It states that board-level diversity statistics are currently not widely available on a consistent and comparable basis, although Nasdaq believes this type of information is important to investors. The new rules would augment existing Commission requirements for companies to disclose how their boards or board nominating committees consider diversity in nominating new directors.<sup>[4]</sup> The Commission also notes that although the new rules may encourage some Nasdaq-listed companies to increase diversity on their boards, they do not mandate any particular board composition.

Chair Gary Gensler published a statement supporting the new rules as reflecting investors' calls for greater transparency and comparable data while allowing companies the flexibility to make decisions that best serve their shareholders.<sup>[5]</sup> Likewise, Commissioners Allison Herren Lee and Caroline Crenshaw issued a joint statement expecting the new rules will "improve the quality of information available to investors" on diversity metrics but remarking that there is more work to be done on other types of diversity and on diversity in the workforce generally.<sup>[6]</sup>

Commissioner Elad Roisman issued a statement commending Nasdaq's commitment to diversity and inclusion and noting that the SEC has a role in identifying the barriers in its own regulations that may prevent broad participation in capital markets.<sup>[7]</sup> While he supports the goal of having more diverse and inclusive boards of directors, he raises questions whether the order met the legal standards the Commission must abide by in evaluating self-regulatory organization rule proposals. He believes that the Commission, rather than accepting the findings of Nasdaq, is required to do its own reasoned analysis to evaluate the merits of the proposal.

Commissioner Hester Peirce issued a public statement explaining her opposition to Nasdaq's proposal on the grounds that it is beyond the scope of the Exchange Act and contrary to constitutional principles.<sup>[8]</sup> In particular, she expresses her view that the rules' demographic categories are arbitrary and elide the type of detail that may be important to investors trying to assess a board's effectiveness. She also raises concerns that by setting objectives based on self-identification, the new rules will incentivize misleading disclosures or press individuals to make disclosures about private information.

Bridget Farrell  
Assistant General Counsel

#### **endnotes**

<sup>[1]</sup> See Release No.34-92590, *available at* <https://www.sec.gov/rules/sro/nasdaq/2021/34-92590.pdf>; see also Nasdaq Response to Comments and Notice of Filing of Amendment No. 1 of Proposed Rule Change to Adopt Listing Rules Related to Board Diversity (Feb. 26, 2021), *available at*

<https://www.sec.gov/comments/sr-nasdaq-2020-081/srnasdaq2020081-8425992-229601.pdf>. The order was issued by the Commission rather than by delegated authority to the Division of Trading and Markets. The Commission notes that Exchange Act Section 19(b) does not give the Commission the ability to make any changes to the rule proposal as submitted or to disapprove the rule proposal on the ground that the Commission would prefer some alternative rule on the same topic. In its order, the Commission also approved a proposed Nasdaq rule change to offer certain listed companies access to a board recruiting service to advance diversity.

[2] Foreign issuers would have more flexibility in satisfying the rules. For example, new rule 5065(f)(1) would require foreign issuers to have (or explain why they do not have) two diverse members of their boards, with diversity for those issuers meaning female, LGBTQ+, or an underrepresented individual based on national, racial, ethnic, indigenous, cultural, religious, or linguistic identity in the issuer's country. For complying with new rule 5606(a), foreign issuers would be permitted to use an alternative disclosure that would take into account the number of directors that are underrepresented individuals in the issuers' home countries.

[3] These demographic categories would be based on those used in US Equal Employment Opportunity Commission's form EEO-1. See <https://www.eeoc.gov/employers/eeo-1-data-collection>.

[4] See Regulation S-K, Item 407(c)(2)(vi).

[5] See Statement on the Commission's Approval on Nasdaq's Proposal for Disclosure about Board Diversity and Proposal for Board Recruiting Service (Aug. 6, 2021), *available at* <https://www.sec.gov/news/public-statement/gensler-statement-nasdaq-proposal-disclosure-board-diversity-080621>.

[6] See Statement on Nasdaq's Diversity Proposals - A Positive First Step for Investors (Aug. 6, 2021), *available at* <https://www.sec.gov/news/public-statement/statement-nasdaq-diversity-080621>.

[7] See Statement on the Commission's Order Approving Exchange Rules Relating to Board Diversity (Aug. 6, 2021), *available at* <https://www.sec.gov/news/public-statement/roisman-board-diversity>.

[8] See Statement on the Commission's Order Approving Proposed Rule Changes, as Modified by Amendments No. 1, to Adopt Listing Rules Related to Board Diversity submitted by the Nasdaq Stock Market LLC, *available at* <https://www.sec.gov/news/public-statement/peirce-nasdaq-diversity-statement-080621>.