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United We Stand, Divided We Fall: A Survey of Current Public and Private Initiatives Addressing Board Diversity & a Proposed SEC Diversity Disclosure to Help Increase Board Diversity

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UNITED WE STAND, DIVIDED WE FALL: A SURVEY OF CURRENT PUBLIC AND PRIVATE INITIATIVES ADDRESSING BOARD DIVERSITY & A PROPOSED SEC DIVERSITY DISCLOSURE TO HELP INCREASE BOARD DIVERSITY

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INTRODUCTION

As of 2022, no *Fortune* 500 board of directors is proportional to the United States in its racial, ethnic, and gender composition.[1] From statutes that study, encourage, or mandate board diversity to ESG investments to proxy voting guidelines amendments, public and private actors alike recognize this disparity and are taking action to achieve greater board diversity.

Board diversity activism in America began in the early 2000s and called for greater female representation on boards.[2] Throughout the 2000s and 2010s, most of the debate, activism, and academic research regarding board diversity focused on increased female—specifically white, female—directorship. Still, the activism inspired some change.[3] In 1995, women occupied 9.6% of *Fortune* 500 board seats.[4] Twenty-five years later, that number rose to 20.9%.[5] Still, more progress is necessary to achieve gender parity because women account for over half of the United States population.[6]

Unfortunately, the movement for increased female directors often excludes racial and ethnic identities board diversity. However, global attention to racial and ethnic disparities on corporate boards took center stage in the summer of 2020.[7] Pre- and post-2020 data demonstrates the power of national demands for increased representation.[8] For example, the percentage of Russel 3000 companies with no racial or ethnically diverse directors on their board in 2020 but only 10% lacked diverse directors in 2022.[9] 2022 was also the first year in which all S&P 500 companies had at least one person of color director.[10] Now,

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1 *Missing Pieces Report: The Board Diversity Census of Women and Minorities on Fortune 500 Boards*, DELOITTE, (6th ed. 2020) https://www2.deloitte.com/us/en/pages/center-for-board-effectiveness/articles/missing-pieces-report-board-diversity.html.

2 *See* Katherine Sharpless, *California's S.B. 826: Will the Supreme Court Get on Board?*, 42 WOMEN'S RTS. L. REP. 172, 190 (2021) (noting that Norway 's mandatory quotas began the wave of activism focused on increasing female board membership).

3 *See generally* DELOITTE & ALLIANCE FOR BOARD DIVERSITY, *supra* note 1.

4 PEW RESEARCH CENTER, *The Data on Women Leaders* (Jan. 2021), https://www.pewresearch.org/social-trends/fact-sheet/the-data-on-women-leaders/.

5 DELOITTE, *supra* note 1 at 17.

6 UNITED STATES CENSUS, *Quick Facts* (2022), https://www.census.gov/quickfacts/fact/table/US/LFE046221.

7 Subdoh Mishra & Institutional Shareholder Services, Inc., *Racial and Ethnic Diversity on U.S. Corporate Boards—Progress Since 2020*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNACE (July 21, 2022), https://corpgov.law.harvard.edu/2022/07/21/racial-and-ethnic-diversity-on-u-s-corporate-boards-progress-since-2020/.

8 *Id.*

9 *Id.*

10 *Id.*

36% of the S&P 500 companies have at least three racially or ethnically diverse directors.[11] George Floyd's, Ahmaud Arbery's, and Breonna Taylor's brutal murders achieved this shift in boards' racial and ethnic composition—later termed the "George Floyd Effect.[12] Despite recent progress in board diversity, America has more progress to do to achieve representative boards.[13]

A 2020 study found an overwhelming majority of participating companies either made either no progress or regressed in achieving board diversity in recent years.[14] Even when companies realize gains in diversity, white women benefit the most.[15] At the current rate, minority women could achieve a proportional amount of board seats in *Fortune* 500 companies no earlier than 2046.[16] Thus, both public and private actors must pressure corporations more to achieve today for what should have been won yesterday—boards of directors that look like the people they serve.

This Comment analyzes legal routes of activism that are likely to achieve greater board diversity and withstand constitutional challenges. Section I surveys the current public and private initiatives that address board diversity and their effectiveness. Section II details the current legal challenges to board diversity initiatives, *Alliance for Fair Board Recruitment v. SEC and Crest v. Padilla I* and *II*. Section III anticipates those constitutional challenges' impact on board diversity advocacy and ESG investing. Finally, Section IV proposes a board diversity disclosure framework as a potential way to address board diversity that will likely aid efforts to increase board diversity and withstand legal challenges.

I. AN OVERVIEW OF CURRENT REFORMS TO ENCOURAGE CORPORATE BOARD DIVERSITY

The private and public sectors increasingly recognize the value of board diversity and respond in different ways. This section surveys the public and private sectors', Nasdaq's, and other countries' approaches to board diversity and evaluates their effectiveness, limitations, and potential legal challenges.

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11 *Id.*
12 *Id.*
13 *Id.*
14 SUNDIATU DIXON-FYLE ET AL., DIVERSITY WINS: HOW INCLUSION MATTERS 24 (3rd ed. 2020), https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters#.
15 DELOITTE, *supra* note 1 at 26.
16 *Id.*at 5.

A. *Public Sector Responses*

1. *State Statutory Initiatives*

As there is no federal board diversity law, states led the charge in public policies that address board diversity. [17] The result is a patchwork of policies as diverse as the United States. However, the American approach does not operate in a vacuum. European countries acted long before America, and the literature categorizes the four approaches to redress as (1) mandatory quotas, (2) comply or explain, (3) voluntary, or (4) non-binding resolutions.[18]

California is the only state to implement mandatory quotas.[19] California Corporations Code § 301.3 and § 301.4 (also known as S.B. 826 and A.B. 979, respectively) require that every publicly held domestic and foreign corporation whose principal executive office is in California have at least one director who self-identifies as a woman and one director from an "underrepresented community."[20] A member of an underrepresented community is someone who "self-identifies as Black, African American, Hispanic, Latino, Asian, Pacific Islander, Native American, Native Hawaiian, or Alaska Native" or someone "who self-identifies as gay, lesbian, bisexual, or transgender."[21] The number of requisite directors correspond to the corporation's board size, but every public corporation with its principal place of business in California needs at least one female director and one director from an underrepresented community.[22] On the other hand, corporations with nine or more board members need at least three female directors and three directors from an underrepresented community.[23] Before injunctions were issued preempting enforcement of these statutes, corporations faced up to a $300,000 fine for noncompliance.[24]

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[17] Kimberly A. Houser & Jamillah Bowman Williams, *Board Gender Diversity: A Path to Achieving Substantive Equality in the United States*, 63 WM. & MARY L. REV. 497, 529 (2021).

[18] *See* Katherine Sharpless, *California's S.B. 826: Will the Supreme Court Get on Board?*, 42 WOMEN'S RTS. L.REP. 172, 186-91 (2021).

[19] Erin Griffith, *California Law Requiring Board Diversity Is Struck Down*, THE NEW YORK TIMES (Apr. 3, 2022), https://www.nytimes.com/2022/04/03/business/california-board-diversity-law.html#:~:text=Other%20states%2C%20including%20Maryland%20and,the%20same%20argument%20against%20quotas.

[20] Cal. Corp. Code § 301.4 (West); *see* Female Directors; Minimum Number of Female Directors; Reports; Adoption Of Regulations; fines Cal. Corp. Code § 301.3 (West).

[21] § 301.4 (e)(1).

[22] *See* § 301.3 (b); § 301.4(b)(3).

[23] § 301.3 (b)(1) (noting that boards with six directors or more "shall have a minimum of three female directors"); § 301.4(b)(1).

[24] § 301.3(d)(1)(A)-(C); § 301.4(e)(1)(A)-(C).

While both California statutes were eventually held unconstitutional,[25] California's legislative advocacy achieved more diverse boards. Women hold 34.1% of presently existing board seats in Californian companies, which is the highest rate of female representation in the country. [26] Of the female directors appointed within a year after the passage of § 301.3, 76% held advanced degrees, and 73% were "employed on top of their new board roles, most commonly in C-suite positions."[27] This data harshly rebuts the allegations that mandatory quotas force corporations to elevate unqualified candidates to board positions.[28] One year after § 301.4 enacted § 301 of the § 358 impacted California corporations complied with the law despite legal challenges.[29] While courts have since enjoined California's mandatory quota approach, [30] it demonstrates that a mandatory quota approach with a harsh fine can quickly and effectively achieve greater board diversity, even amidst legal challenges.[31]

Other states take their own unique approaches to bridge corporate board disparities. For example, Washington adopted a version of the comply-or-explain approach in the Women on Corporate Boards Act.[32] The Women on Corporate Boards Act requires that 25% of individuals on public companies' board of directors self-identify as a woman or the company must deliver a "diversity discussion and analysis" to its shareholders at the annual shareholder meeting.[33] The presentation must include many of the same disclosures that Item 407 requires, such as a discussion of whether the board considers diversity when nominating candidates, the existence of any policy for identifying or nominating diverse board members, and any company-specific mechanisms for refreshing

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[25] *Crest v. Padilla*, No. 19STCV2756, slip op. at 23 (Cal. Super. Ct. 2022); *Crest v. Padilla*, No. 20 STCV 37513, 2022 WL 1073294, at 19 (Cal. Super. Ct 2022).

[26] Alexandria Olson & The Associated Press, *Women Hold a Record Number of Corporate Board Seats. The Bad News: It's Barely Over 25%, and It's Slowing Down*, FORTUNE (Sept. 30, 2022, 5:38 PM), https://fortune.com/2022/09/30/how-many-women-sit-corporate-boards-record-28-percent-russell-3000/.

[27] Katherine Sharpless, *California's S.B. 826: Will the Supreme Court Get on Board?*, 42 WOMEN'S RTS. L. REP. 172, 196(2021).

[28] *See id.*

[29] Shirley Weber, *Diversity on Boards: March 2022 Report, Corporations Code Sections 301.3 and 301.4*, CALIFORNIA SECRETARY OF STATE (Mar. 2022) (noting that forty publicly held corporations moved headquarters out of state after the laws were placed into effect, but no study proved causation).

[30] *See generally* Cydney S. Posner, *California Appeals Court Reinstates Injunctions Against California Board Laws*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE (Dec. 19, 2022), https://corpgov.law.harvard.edu/2022/12/19/california-appeals-court-reinstates-injunctions-against-california-board-diversity-laws/.

[31] *Crest v. Padilla*, No. 19STCV2756, slip op. at 23 (Cal. Super. Ct. 2022); *Crest v. Padilla*, No. 20 STCV 37513, 2022 WL 1073294, at 19 (Cal. Super. Ct 2022).

[32] *See generally* Women on Corporate Boards Act, Wash. Rev. Code Ann. § 23B.08.120 (West).

[33] WASH. REV. CODE § 23B.08.120(1)-(3).

the board, like term or age limits for directors.[34] Washington is second in female representation on boards, falling only four percentage points behind California.[35] However, Washington has not yet amended or adopted any law that addresses diversity in race, ethnicity, or sexual orientation.[36]

Maryland law, on the other hand, only addresses racial diversity.[37] It requires all commercial enterprises incorporated or registered to do business in Maryland and all Maryland non-profits either (1) demonstrate diverse membership within the board of directors or executive leadership or (2) demonstrate "support for underrepresented communities in the entity's mission" to qualify for a state benefit of more than $1,000,000.[38] The law also requires all businesses, to disclose their racial and ethnic composition of their board of directors and C-suite.[39] Maryland uses this data to create and update a "State Equity Report," which publishes diversity data on each organization.[40]

Many states also utilize non-binding resolutions. For example, Colorado and Massachusetts take a soft-handed approach to gender diversity and fail to address race, ethnicity, or sexual orientation.[41] Both states passed non-binding resolutions that set voluntary goals for the number of female directors based on the number of total seats on the board.[42] Alternatively, the Massachusetts resolution applies to both public and private companies and encourages companies to disclose the total size of the board and the number of female

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34 *Compare* § 23B.08.120(1)-(3), *with* Item 407, 17 C.F.R. § 229.407 (2019) (whereas the Item 407 disclosure also requires companies to disclose the manner in which nominees are recommended, whether the board or nominating committee considers diversity in identifying nominees, and if so, how).

35 Alexandria Olson & The Associated Press, *Women Hold a Record Number of Corporate Board Seats. The Bad News: It's Barely Over 25%, and It's Slowing Down*, FORTUNE (Sept. 30, 2022, 5:38 PM), https://fortune.com/2022/09/30/how-many-women-sit-corporate-boards-record-28-percent-russell-3000/.

36 *See* WASH. REV. CODE § 23B.08.120(1)-(3).

37 *See generally* Md. Code Ann., Bus. Reg. § 19-106 (West).

38 Md. Code Ann., Bus. Reg. § 19-106(a)(2); *id. at (C).* (State benefits under the statute include capital grant funding, tax credits, and state contracts).

39 Md. Code Ann., Bus. Reg. § 19-106(d).

40 *Id.* (Note, there is not published State Equity Report as of the time of publication because the statute was effective July 1, 2022.)

41 *See* H.J. Resol. 17-1017, 71st Gen. Asemb., Reg. Sess. (Colo. 2017); S.Resol. 1007, 189th Gen. Ct., Reg. Sess. (Mass. 2015).

42 *See id.*

directors.[43] Today, women occupy 24% of Colorado boards[44] and 29.6% of Massachusetts boards.[45] However, these approaches are not mutually exclusive.

States can also use disclosures to address board diversity. Maryland requires all public and private corporations with an operating budget or total annual sales exceeding five million to disclose the total number of directors and the number of female board members in addition to its non-binding resolution encouraging diversity.[46] In 2019, Illinois amended the Business Corporation Act of 1983 to include a mandatory board diversity disclosure.[47] Illinois now requires corporations with a principal executive office in the state to disclose the race, ethnicity, gender identity, and sexual orientation of each of its board members.[48] Illinois corporations also must disclose the following: the process they use to identify and evaluate board nominees, whether diversity is considered when nominating directors, and how the corporation promotes DEI among its board and executive officers.[49] The University of Illinois analyzes the data collected from the mandatory disclosures to publicly rate corporations based on their compliance, DEI initiatives, and board composition. [50] The most recent report revealed women account for only 29% of directors in Illinois.[51] Furthermore, whereas approximately 40% of Illinois' population are people of color, only 17% of board seats at the average Illinois firm are occupied by members of a racial or ethnic minority.[52] 19% of Illinois firms have no people of color on their board of directors. [53] Astonishingly, despite the statute's requirement to disclose

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43 S. Resol. 1007, 189th Gen. Ct., Reg. Sess. (Mass. 2015).

44 Judith Kohler, *Women Make UP 24% of Colorado C*ompany Boards, up from 7% a Decade Ago, THE DENVER POST (Mar. 16, 2022), https://www.denverpost.com/2022/03/19/colorado-company-boards-women-diversity/.

45 Shirley Leung, *Women on Corporate Boards in Massachusetts Breaks Another Record According to New Report*, THE BOSTON GLOBE (Nov. 15, 2022, 7:29 AM), https://www.bostonglobe.com/2022/11/15/business/women-corporate-boards-massachusetts-breaks-another-record-according-new-report/.

46 Md. Code Ann., Tax-Prop. § 11-101(c) (West).

47 805 Ill. Comp. Stat. Ann. 5/8.12 (2019).; *See also* H.R. 0439, 100th Gen. Assemb., Reg. Sess. (Ill. 2017). (Illinois mandates diversity disclosures and uses a non-binding resolution to encourage board diversity. Illinois illustrates that these approaches are not mutually exclusive, but rather can work hand in hand to encourage diversity.)

48 805 Ill. Comp. Stat. Ann. 5/8.12(c)(3-6).

49 805 Ill. Comp. Stat. Ann. 5/8.12(c)(7-9).

50 805 Ill. Comp. Stat. Ann. 5/8.12 (d)- (e).

51 Richard A. Benton & Eunmi Mun, *Illinois Corporate Board Diversity, Inclusion, and Representation Report – 2022*, SCHOOL OF LABOR & EMPLOYMENT RELATIONS UNIVERSITY OF ILLINOIS AT URBANA-CHAMPAIGN 1, at 2 (2022), https://ler.illinois.edu/wp-content/uploads/2022/02/Illinois-Board-Diversity-Report-2021-20220224.pdf.

52 *Id.*

53 *Id.* at 4.

the sexual orientation, the state has never published any data about the sexual orientation of Illinois board members.[54]

New York adopted a similar approach. New York passed the "Women on Corporate Boards Study" Act in the 2019-2020 legislative session, which requires all for-profit corporations authorized to transact business in New York disclose the total number of directors on the board and the number of female directors biannually.[55] The first Women On Corporate Boards Study found that from 2020 to 2022, the aggregate percentage of female directors was 25.8%; however, the study did not address the law's impact on female directorship.[56]

In conclusion, the states are all over the map in their remedies to corporate board disparities. States differ in the type of businesses impacted, the approach used, and whether the policy addresses gender, race, ethnicity, sexuality, or some combination thereof. Despite the diversity of these state policies, this survey of state board diversity policies does highlight three key takeaways. First, states incorporate a very similar language to Item 407 in their policies, which indicates that states keep in close step with the SEC's policymaking. Second, although the states differ in what demographic information companies are required to disclose, every state includes a diversity disclosure in their policies except for Colorado. Finally, every state with a board diversity policy on the books voted blue in the last presidential election.[57]

2. State Investment Fund Initiatives

Outside of statutory remedies, states are making efforts to addresses board diversity through their role as institutional investors.[58] By wielding the power of the purse, states have pressured corporations to diversify their boards through their pension funds and proxy guidelines.[59]

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[54] *See id.*; Richard A. Benton & Eunmi Mun, *Illinois Corporate Board Diversity, Inclusion, and Representation Report – 2021*, SCHOOL OF LABOR & EMPLOYMENT RELATIONS UNIVERSITY OF ILLINOIS AT URBANA-CHAMPAIGN 1 (2021), https://ler.illinois.edu/wp-content/uploads/2023/02/Illinois-Board-Diversity-Report-2022-20230223.pdf; Richard A. Benton & Eunmi Mun, *Illinois Corporate Board Diversity, Inclusion, and Representation Report – 2020*, SCHOOL OF LABOR & EMPLOYMENT RELATIONS UNIVERSITY OF ILLINOIS AT URBANA-CHAMPAIGN 1 (2020), https://ler.illinois.edu/wp-content/uploads/2021/07/Illinois-Board-Diversity-Report-2020-Revised-2.pdf.

[55] N.Y. Bus. Corp. Law § 408(1)(d) (McKinney).

[56] NEW YORK DEPARTMENT OF STATE, REPORT: WOMEN ON CORPORATE BOARS PURSUANT TO THE WOMEN ON CORPORATE BOARDS STUDY ACT 2 (2022) at 2,3.

[57] *2020 Electoral College Results*, NATIONAL ARCHIVES (2021), https://www.archives.gov/electoral-college/2020.

[58] *See* Dorothy S. Lund, *Toward A Fair and Sustainable Corporate Governance System: Reflections on Leo Strine, Jr.'s Writing on Institutional Investors*, 24, 842 U. PA. J. BUS. L. 835 (2022).

[59] *Id.*

For example, in 2014, New York City Comptroller, Scott Stringer, and the New York City Pensions Fund created the "Boardroom Accountability Project" to increase board diversity and environmental responsibility among corporations. [60] In 2019, "Phase 3.0" of the Boardroom Accountability Project launched, where Scott Stringer and the New York City Pension Fund called publicly-traded companies to adopt a version of the National Football League's "Rooney Rule."[61] The Board Accountability Project's version of the Rooney Rule requires every publicly-traded company with a vacant board or CEO position consider at least one woman and one person of color.[62] Comptroller Stringer sent a letter to the fifty-six S&P 500 companies urging those companies to adopt a version of the Rooney Rule immediately and filed shareholder proposals at companies that "lack[ed] apparent racial diversity at the highest levels".[63]

On the other side of the country, the California State Teachers' Retirement System ("CalSTRS"), America's third-largest retirement fund, has leveraged its investments to encourage board diversity.[64] CalSTRS invests in companies that adopt the Rooney Rule, disclose the backgrounds of current directors, and commits to nominating "qualified candidates of diverse racial, and ethnic backgrounds."[65] Furthermore, the pension fund threatened companies with shareholder proposals, which signals a willingness to act more directly.[66]

Other pension funds incorporate a different approach to promote board diversity such as adopting proxy voting guidelines advising shareholders to vote against incumbent directors unless the company achieves specified diversity

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[60] *Boardroom Accountability Project,* NEW YORK CITY COMPTROLLER, (last visited Jan. 5, 2023), https://comptroller.nyc.gov/services/financial-matters/boardroom-accountability-project/overview/.

[61] *Id.*; *see also The Rooney Rule*, NFL FOOTBALL OPERATIONS (last visited Jan. 5, 2023), https://operations.nfl.com/inside-football-ops/inclusion/the-rooney-rule/ (explaining that the first iteration of the Rooney Rule required every team in the NFL with a vacant coaching position to interview at least one diverse candidate before filling the position and later expanded to include a many other various positions across the NFL).

[62] *See id.*

[63] *Id.* (alteration added).

[64] Karen Doron, *CalSTRS Finishes with -1.3% Return, Beats Total Fund Benchmark in Volatile Fiscal Year 2021-22*, CALSTRS (Jul. 29, 2022), https://www.calstrs.com/calstrs-finishes-with-1-3-return-beats-total-fund-benchmark-in-volatile-fiscal-year 202122#:~:text=(July%2029%2C%202022)%20%E2%80%93,as%20of%20June%2030%2C %202022.

[65] *2020 Annual Progress Report – CALSTRS Investments, Diversity In The Management Of Investments*, CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM, (2022), https://www.calstrs.com/files/41d841987/diversityinthemanagementofinvestments-2020.pdf.

[66] Kimberly A. Houser & Jamillah Bowman Williams, *Board Gender Diversity: A Path to Achieving Substantive Equality in the United States*, 63 WM. & MARY L. REV. 497, 526-27 (2021).

metrics. For example, the New York State Common Retirement Fund, America's fourth largest pension fund, adopted proxy voting guidelines in which it pledges to vote against incumbent directors and nominating committee members when: (1) there is no person of color or female director, (2) there is no people of color on the nominating committee, (3) the corporation does not disclose the race or ethnicity of its directors, or (4) the corporation does not consider racial or ethnic diversity in its director search.[67]

Similarly, as of March 2022, the Massachusetts Pension Reserves Investment Management ("PRIM") Board's proxy voting guidelines state that the fund will vote against, or withhold votes from, all board nominees if the current board is less than 35% "diverse," when accounting for race and gender.[68] Neighboring state Rhode Island also adopted proxy voting guidelines for state pension funds that promise to vote against incumbent directors if at least 30% of board seats are not occupied by women or racial minorities.[69] One potential roadblock to this form of shareholder activism is that the Department of Labor has regulatory authority over the management of mutual funds for retirement plans under the Employee Retirement Income Security Act of 1974 ("ERISA").[70] Additionally, the Department of Labor responded to this activism with regulation.[71] In November 2020, the Department of Labor issued a regulation clarifying the role of ESG investments in pension funds.[72] In that regulation, the Department of Labor explicitly rejected a growing academic argument that ESG considerations are necessarily pecuniary because of their tendency to increase profitability.[73] Consequently, states were left with less legal protection when deciding to incorporate ESG considerations into their mutual fund investments.[74]

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[67] *DiNapoli: Corporate America Must Show Progress on Diversity, Equity & Inclusion*, OFFICE OF THE NEW YORK STATE COMPTROLLER (Feb. 16, 2022), https://www.osc.state.ny.us/press/releases/2022/02/dinapoli-corporate-america-must-show-progress-diversity-equity-inclusion.

[68] *Massachusetts Pension Reserves Investment Management Board, PRIM Board – Custom Proxy Voting Guidelines – 2022*, MASSACHUSETTS PENSION RESERVES INVESTMENT MANAGEMENT BOARD (2022), https://www.mapension.com/wp-content/uploads/2022/03/PRIM-Board-Custom-Proxy-Voting-Guidelines-Approved-by-Board-02172022.pdf.

[69] *Proxy Voting Guidelines*, RHODE ISLAND OFFICE OF THE GENERAL TREASURER, (Sept. 26, 2018), https://d10k7k7mywg42z.cloudfront.net/assets/5c08053023f8124fa8129f50/Existing_Rhode_Island_Proxy_Policy_Matrix_2016_Proposed_Exec_Comp___version_2_.pdf.

[70] Employee Retirement Income Security Act (ERISA) of 1974, Pub. L. No. 93-406, 88 Stat. 829.

[71] *Id.*

[72] 29 CFR § 2550.404a-1(c)(1).

[73] Financial Factors in Selecting Plan Investments, 85 FR 72846-01, at 72848-49, 72858.

[74] *See id.*

The 2020 regulation was quickly rescinded in May of 2021 by an executive order from President Biden.[75] On November 22, 2022, the Department of Labor published a new rule which overturned the 2020 rule and clarified that fiduciaries who manage 401(k)s may consider ESG factors when screening investments and crafting proxy voting guidelines.[76] The rule has yet to go into effect, but when it does, it serves as a win for diversity advocates and a signal to ERISA fiduciaries that they can implement more ESG considerations in their investments and proxy guidelines, at least during the Biden administration.[77]

3. *SEC Board Diversity Disclosure Rules*

A 2009 SEC rule, often referred to as Item 407, requires public companies to "[d]escribe the nominating committee's process for identifying and evaluating nominees for directors" in their annual mandated disclosures.[78] Public companies must also disclose whether the board of directors or the nominating committee considers diversity when nominating members and, if so, what that looks like.[79] Item 407 does not require companies to consider diversity when either nominating directors to their boards or disclosing any data regarding board composition.[80] Rather, the rule only requires companies to disclose and explain their search and evaluation process for director nominees, and the extent of which the company considers "diversity," however the company defines it.[81]

Notably, the SEC's definition of "diversity" faced substantial criticism for its expansive breadth.[82] In its Compliance and Disclosure Interpretations ("C&DIs"), the SEC explained the disclosures are not limited to "self-identified diversity characteristics," such as race, gender, sexual orientation, nationality, or ethnicity.[83] Instead, the SEC's interpretation of diversity includes many other qualifications or experiences that companies might consider in their nomination process.[84] Examples include, but are not limited to, diverse work experiences, military service, or socio-economic or demographic characteristics."[85] The most

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75 Climate-Related Financial Risk, Exec. Order No. 14,030, 86 Fed. Reg. 27967 (May 20, 2021)

76 *Id.*

77 *Id.*

78 Item 407, 17 C.F.R. § 229.407 (2019).

79 *Id.*

80 Item 407, 17 C.F.R. § 229.407 (2019).

81 *Id.*

82 Katherine Sharpless, *California's S.B. 826: Will the Supreme Court Get on Board?*, 42 WOMEN'S RTS. L. REP. 172, 186-87 (2021).

83 *Regulation S-K: Compliance & Disclosure Interpretations*, U.S. SEC. & EXCH. COMM'N, https://www.sec.gov/divisions/corpfin/guidance/regs-kinterp.htm (last updated Sept. 21, 2020).

84 *Id.*

85 *Id.*

prominent critique of the SEC's broad definition of "diversity" is that it permitted companies to consistently define diversity in terms of the nominee's work history and experience rather than demographic characteristics.[86] Consequently, a diverse candidate could be a white, cis-gendered male from rural America.[87] Critics of Item 407 claim this is not what diversity should look like in 2023.[88]

B. Private Sector Responses

1. ESG Investing & Proxy Disclosures

Yet state actors are not the only advancers of social change. Private actors are continuously promoting an increase in boardroom diversity and addressing other environmental, social, and governance ("ESG") considerations. One-way private sectors are addressing the lack of diversity in corporate boardrooms is through the rise of ESG-specific funds; however, not all ESG funds or exchange-traded funds ("ETFs") are created equal.[89]

ESG-specific funds take many different forms and are rapidly evolving.[90] ESG funds range from single-issue funds addressing issues such as the environment or religion to funds that use an index to identify a company's performance on a wide range of ESG considerations.[91] These funds are created either by negative screening where a fund excludes certain types of companies (like tobacco or oil), or with positive screening, where a fund limits its investments to companies that meet their predetermined investment criteria.[92]

There is still much unknown about how ESG funds operate, despite their drastic increase in popularity in recent years.[93] For example, it is unknown if ESG funds invest in companies that already have diversity in upper management, if they advocate for consideration of diversity in the director nomination process, or if they account for diversity at all.[94] Perhaps the answer

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86 Katherine Sharpless, *California's S.B. 826: Will the Supreme Court Get on Board?*, 42 WOMEN'S RTS. L. REP. 172, 187 (2021).

87 *Id.*

88 *Id.*

89 *See generally* Quinn Curtis et al., *Do ESG Mutual Funds Deliver on Their Promises?*, 120 MICH. L. REV. 393 (2021).

90 *Id.* at 395.

91 *Id.*

92 *See id.* at 399, 404.

93 *Id.* at 397-98.

94 *See* Ron S Bernblat & Elizabeth R. Gonzales-Sussman, *Racial Equity Audits: A New ESG Initiative*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE (Oct. 30, 2021),

is different for each index fund.[95] Consequently, despite the $161 billion dollars invested in over 600 American ESG funds and ETFs, private actors may realize that ESG investing is not the most precise or effective measure of achieving boardroom diversity—at least not yet.[96] ESG funds could become a more prominent tool to achieve board diversity in the future with the proposal of a new SEC rule. The proposed SEC rule would require those who operate ESG funds to disclose the "specific impacts they seek to achieve and summarize their progress on achieving those impacts" to the SEC.[97] If such a rule is finalized, investors could more easily understand the ESG factors these funds consider when making investments and invest accordingly.

Additionally, some of the world's largest investment funds amended their proxy voting guidelines to help elect diverse directors and support activist shareholder proposals. BlackRock, the world's largest asset management firm,[98] recommends that 30% of board members be "diverse," when accounting for demographic factors (such as gender, race, ethnicity, and disability), professional background, and geography as an example.[99] BlackRock also recommends that boards have a minimum of two members who identify as female and one member who identifies as a member of an "underrepresented group," which includes ethnic and racial minorities, those who identify as a member of an underrepresented religion or culture, are disabled, or are a veteran.[100] The world's second-largest asset management fund, Vanguard, expects diverse boards in experience, tenure, race, gender, and ethnicity; Vanguard will also support shareholder proposals that seek transparency and

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https://corpgov.law.harvard.edu/2021/10/30/racial-equity-audits-a-new-esg-initiative/ (noting that the social component of ESG investing can include issues impacting diversity, equity, and inclusion and the governance component often focuses on issues relating to the make up the board of directors).

[95] *Id.*

[96] *See id.*

[97] *SEC Proposes to Enhance Disclosures by Certain Investment Advisers and Investment Companies About ESG Investment Practices*, U.S. SEC. & EXCH. COMM'N (May 25, 2022), https://www.sec.gov/news/press-release/2022-92.

[98] *World's Top Asset Management Firms*, ADV RATINGS, (last visited Jan. 5, 2023) https://www.advratings.com/top-asset-management-firms.

[99] *Proxy Voting Guidelines for U.S. Securities*, BLACKROCK INVESTMENT STEWARDSHIP (2023) https://www.blackrock.com/corporate/literature/fact-sheet/blk-responsible-investment-guidelines-us.pdf.

[100] *Id.* at 7, n.3.

increased diversity.[101] Fidelity Investments,[102] State Street Global Advisors,[103] Morgan Stanley,[104] and JPMorgan Chase account for the remaining top six global asset management companies, and each adopted proxy voting guidelines similar to BlackRock and Vanguard. [105] Each of these proxy voting guidelines cite the asset management firm's belief that diverse boards signal good corporate governance and promise to withhold support from incumbent directors where the company does not meet the requisite indicia of board diversity.[106]

2. *The Goldman Sachs IPO Pledge*

In 2020, Goldman Sachs announced it would only underwrite IPOs for American or Western European companies with at least one diverse board member.[107] In 2021, Goldman Sachs amended the rule; Goldman will only underwrite IPOs if a company has a minimum of two directors of color and at least one female director.[108] According to the company's website, 297 companies currently comply with the policy.[109] Goldman Sachs facilitated seventy-five "diverse placements" for both private and public companies as of

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101 *Proxy Voting Policy for U.S. Portfolio Companies*, VANGUARD FUNDS, 7-8 (2022) https://corporate.vanguard.com/content/dam/corp/advocate/investment-stewardship/pdf/policies-and-reports/US_Proxy_Voting.pdf.

102 *Proxy Voting Guidelines*, FIDELITY INVESTMENTS (2022) (stating that Fidelity will oppose the election of directors when there are no female directors or fewer than two female directors on a board of ten or more people but lacking any voting policy considering race or ethnicity) https://www.fidelity.com/binpublic/060_www_fidelity_/codocuments/Full-Proxy-Voting-Guidelines-for-Fidelity-Funds-Advised-by-FMRCo-and-SelectCo.pdf.

103 *See generally Guidance on Diversity Disclosures and Practices*, STATE STREET GLOBAL ADVISORS' ASSET STEWARDSHIP 2-3 (2022) (outlining a diversity matrix that will determine how they vote in director elections that account for gender and race as well as the financial market the business is in) https://www.ssga.com/library-content/pdfs/asset-stewardship/guidance-on-diversity-disclosures-practices.pdf.

104 *Proxy Voting Policy and Guidelines*, MORGAN STANLEY INVESTMENT MANAGEMENT, (2022) (stating that the investment firm will consider withholding support form nominees if diversity is not considered in the nomination process or disclose information regarding employee and board diversity and that it will support all shareholder proposals aimed at increasing board diversity) https://www.morganstanley.com/im/publication/resources/proxyvotingpolicy_msim_en.pdf.

105 *Global Proxy Voting Guidelines*, J.P. MORGAN ASSET MANAGEMENT, 14 (2022) (stating that the investment firm will vote against the chair of the Nominating Committee where the racial, gender, or ethnic composition of the board is not disclosed or where the chair of the Nominating Committee "lacks any gender diversity or any racial/ethnic diversity unless there are mitigating factors.") https://am.jpmorgan.com/content/dam/jpm-am-aem/global/en/institutional/communications/lux-communication/corporate-governance-principles-and-voting-guidelines.pdf.

106 *Id.*

107 *Corporate Board Engagement,* GOLDMAN SACHS, (last visited Jan. 3, 2023). https://www.goldmansachs.com/our-commitments/diversity-and-inclusion/board-diversity/2022-update/index.html

108 *Id.*

109 *Id.*

December 2022.[110] Of those seventy-five board placements, 88% were women, and 47% of newly appointed directors identified as Black, Hispanic, or Asian.[111]

3. *Shareholder Action: Racial Equity Audits & Board Diversity Shareholder Proposals*

Racial equity audits gained traction in the wake of the murders of George Floyd, Breonna Taylor, and Ahmaud Arbery.[112] As companies released public statements of support for the Black Lives Matter movement, shareholders quickly used racial equity audits as a tool to pressure corporations to colloquially "put their money where their mouth is" and turn illusory promises into concrete, measurable outcomes which promote and achieve racial justice.[113] The Harvard Law School Forum on Corporate Governance defines a racial equity audit as an "independent, objective and holistic analysis of a company's policies, practices, products, services and efforts to combat systemic racism in order end discrimination within or exhibited by the company with respect to its customers, suppliers or other stakeholders."[114]

Racial equity audits focus on many different parts of a company's business, such as "the treatment of customers at a company's physical locations, the diversity of senior management, the targeting of products, and even political contributions."[115] While a company can voluntarily undergo such an audit, a racial equity audit usually comes from a shareholder proposal pursuant to Rule 14a-8 of the Securities Exchange Act of 1934 ("Rule 14a-8").[116] Racial equity audits, like shareholder proposals, have many challenges generally.

Per Rule 14a-8, a company must list the proposal on its proxy card for vote if: "(a) the shareholder satisfies specified eligibility and procedural requirements; and (b) the proposal is not excludable under Rule 14a-8(i)."[117] While a proposal may satisfy the requirements under 14a-8, a company that wishes not to list the proposal in its proxy statements can (1) request "no action

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110 *Id.*

111 *Id.*

112 Ron S. Berenblat & Elizabeth R. Gonzales-Sussman, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE, *Racial Equity Audits: A New ESG Imitative* (Oct. 30, 2021), https://corpgov.law.harvard.edu/2021/10/30/racial-equity-audits-a-new-esg-initiative/.

113 *See id.*

114 *Id.*

115 *Id.*

116 *Id.* (citing the 2018 Starbucks audit as a voluntary racial equity audit, which the company elected to perform after a racially motivated incident resulted in two Black businessmen being arrested while waiting on coffee before a business meeting).

117 *Id.*

relief" from the SEC, which, if granted, assures the company that, if they exclude the proposal, the SEC will seek no punitive action against the company; (2) petition a court for exclusion under Rule 14a-8(i); or (3) negotiate with the shareholders that file the proposal to withdraw.[118] Most companies that receive a shareholder proposal that requests a racial equity audit, even those that publicly supported Black Lives Matter and pledged to promote racial equity in 2020, seek no-action relief from the SEC.[119]

Under the Trump administration, SEC guidance on Rule 14a-8(i) required that shareholders specify how their proposals would affect the company's bottom line and often excluded detailed shareholder proposals under a theory of shareholder "micro-management," which made it easier for the SEC to grant no-action relief to companies. [120] The SEC, under the Biden administration's guidance, published in November 2021 an SEC Staff Legal Bulletin ("SLB") No. 14L that rescinded SLB Nos. 14I, 14J, and 14k, which were in effect during the Trump administration.[121] SLB No. 14L expansively interprets Rule 14a-8(i)(5), the economic relevance exception, and Rule 14a-8(i)(7), the ordinary business exception.[122] Specifically, SLB No. 14L carves out a "Significant Social Policy Exception," which means that shareholders need not prove a nexus between the company and the policy issue that is the subject of the shareholder proposal; rather, the company must prove the significance of the social issue.[123] Additionally, SLB No. 14L protects "issues of broad social or ethical concern" from exclusion under the economic relevance exception and de-facto overturn the prior administration's "micromanagement" theory..[124] In effect, SLB No. 14L reverses the main theories that excluded shareholder proposals under Trump-era guidance. It also sends a clear message to shareholders and companies alike under the Biden administration: it is much more difficult for corporations to achieve no action relief from the SEC. [125]

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118 *Id.*

119 *Id.*

120 Karin Rives, *New SEC Guidance Emboldens Shareholder Activists as 2022 Proxy Season Ramps Up*, S&P GLOBAL MARKET INTELLIGENCE (Nov. 17, 2021), https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/new-sec-guidance-emboldens-shareholder-activists-as-2022-proxy-season-ramps-up-67678895.

121 *Shareholder Proposals: Staff Legal Bulletin No. 14L (CF)*, SEC DIVISION OF CORPORATE FINANCE, (Nov. 3, 2021), https://www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals.

122 *Id.*

123 *Id.*

124 *Id.*

125 *See* Rives, *supra* note 120; *see also* SEC DIVISION OF CORPORATE FINANCE, *supra* note 121 (noting that a SLB itself is not a rule or regulation and consequently has not legal effect or force).

Unsurprisingly, SLB No. 14L set the tone for a record-breaking proxy season. [126] The 2022 poxy season saw 941 shareholder proposals submitted and 562 brought to a vote.[127] Much like in 2021, DEI dominated shareholder proposals.[128] There were forty-four shareholder proposals that related to DEI in 2022, eleven went to a vote, and one passed.[129] Mainly these shareholder proposals were seeking disclosure of data beyond EEO-1 data, such as data on disclosure of recruitment, retention, and promotion of diverse employees.[130] Eighteen proposals addressed board diversity, which was a decline from 2021.[131] Nevertheless, the most successful shareholder proposals addressing DEI were civil rights and racial equity audits.[132] Shareholders submitted eight civil rights audits, eight went to a vote, and five passed.[133] Furthermore, shareholders proposed thirty racial equity audits, sixteen went to a vote, and three passed in the 2022 proxy season.[134]

SBL No. 14L and the 2022 proxy season demonstrate that while DEI shareholder proposals continue to be popular, greater access to shareholder derivative suits does not necessarily translate into greater success for DEI shareholder proposals. On the other hand, the data shows that racial equity and civil rights audits are promising tools for addressing racial disparities on the aggregate but are not a direct path to increasing board diversity.

C. Nasdaq Listing Requirements

In December 2020, the SEC approved a new listing requirement that the Nasdaq submitted for approval.[135] The Nasdaq listing requirement includes two rules.[136] The first, Rule 5606, requires that every listed company disclose every board member's self-identified demographic information (including race, gender, and sexuality) to Nasdaq.[137] The rule further requires the respective

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[126] Brigid Rosati, Kilian Moote, Rajeev Kumar, Michael Maiolo, Georgeson LLC, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE, *A Look Back at the 2022 Proxy Season* (Oct. 23, 2022), https://corpgov.law.harvard.edu/2022/10/23/a-look-back-at-the-2022-proxy-season/

[127] *Id.*

[128] *Id.*

[129] *Id.*

[130] *Id.*

[131] *Id.* (noting that "we believe this decline in proposal volume is not indicative of waning importance of this topic, but rather an indication of progress").

[132] *Id.*

[133] *Id.*

[134] *Id.*

[135] Order Approving Nasdaq Proposed Rule Changes, 86 Fed. Reg. 4424, 4424-25 (Aug. 12, 2021).

[136] *Id.*

[137] *Id.*

company to publish this information on their website or in the company's proxy statement annually.[138] The second rule, Rule 5606(f), adopts a comply or explain approach and requires that the companies that list with Nasdaq have a certain number of women, people of color, or gay directors based on a diversity matrix or the company must disclose the reason for non-compliance.[139] At a minimum, the rule requires that each company have, or explain the lack of at least one director who self-identifies as female and at least one director of a racial minority or who identifies as LGBTQ+.[140] Rule 5606 also states that Nasdaq will cover the financial cost associated with recruitment services if a listed company needs assistance finding diverse candidates.[141] Corporations can opt out of explaining why they did not meet the diversity targets.[142] If they choose not to explain why they did not comply with the diversity matrix, then Nasdaq may de-list the company.[143]

In its rationale for the rule, Nasdaq explained that increasing board diversity results in increased perspectives, better decision-making, and stronger internal monitoring, which benefits shareholders.[144] Nasdaq also emphasized "the recent calls from investors and commissioners alike for more transparency regarding boardroom diversity" and how shareholders invest more confidently in diverse boards.[145] If upheld, the Nasdaq rule would be "one of the most forceful moves yet to bring greater diversity to U.S. corporations," as the rule would affect over three-quarters of Nasdaq-listed companies. [146]

D. International Landscape

European laws that mandate and encourage board diversity preceded American initiatives and regulations aimed at increasing board diversity. Most recently, the European Union ("EU") adopted a directive on gender balance on corporate boards in November of 2022.[147] The directive requires that 33% of board members and 40% of non-executive directors at large-listed EU

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138 *Id.*

139 *Id.*

140 *Id.*

141 *Id.*

142 Id.

143 Id.

144 Notice of Filing of Proposed Rule Change to Adopt Listing Rules Related to Board Diversity, Exchange Act Release No. 90547, 2020 WL 7226158, 2 (Dec. 4, 2020).

145 *Id.*

146 Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1, 59 (2022).

147 *Gender Equality: The EU Is Breaking the Ceiling Thanks to New Gender Balance Targets on Company Boards*, EUROPEAN UNION (Sept. 22, 2022), https://ec.europa.eu/commission/presscorner/detail/en/statement_22_7074.

companies be of the under-represented sex by July 2026.[148] Members of the under-represented sex can be male, female, or non-binary depending on the board's composition.[149] The directive is enforced through a comply or explain approach reminiscent of the Nasdaq rule in that those companies that do not comply with the directive must explain why they could not achieve the EU's gender parity standard.[150] Unlike the Nasdaq rule, the EU permits member states to create their own penalties for noncompliance when those sanctions are "effective, proportionate and dissuasive."[151] For example, the EU lists imposing fines or nullifying contested director appointments as sufficient penalties.[152]

Recognizing that many EU countries already have laws in place aimed at achieving gender parity, the EU directive allows states to mandate different percentages of the under-represented sex based on their preexisting laws.[153] Much like American states, the international landscape consists of varied approaches to board diversity. Norway passed the first mandatory quota law in 2003.[154] In Norway, 40% of board members must identify as female.[155] Norway imposes harsh sanctions for non-compliance, like the corporation dissolution or de-listing from stock exchanges.[156] Four years later, Spain, an EU member, passed a law that requires that 40% of all directors identify as female.[157] Rather than punishment for non-compliance, Spain rewards companies with a board comprised of at least 40% women.[158]

Even though both Spain and Norway require the same percentage of women to serve on the board, how they implement enforcement varies and may explain the drastic difference in compliance. Today, women occupy 44% of all board seats in Norway[159] whereas they only occupy 23.7% in Spain.[160] In 2015, Germany passed the Co-Determination Act and became the largest economy to

148 *Id.*
149 *Id.*
150 *See id.*
151 *Id.*
152 *Id.*
153 *Id.*
154 Sharpless, *supra* note 2, at 191-92.
155 *Id.*
156 *Id.*
157 *Id.* at 192.
158 *Id.*
159 Spencer Stuart, *2020 Nordic Spencer Stuart Board Index*, (last visited Jan. 28, 2023) https://www.spencerstuart.com/research-and-insight/nordic-board-index/diversity.
160 Aida Pelaez-Fernandez, *Women in Senior Management Stagnant in Corporate Spain at Only 16%*, REUTERS (July 8, 2020), https://www.reuters.com/article/us-spain-women-companies/women-in-senior-management-stagnant-in-corporate-spain-at-only-16-idUSKBN2492QF.

mandate a gender quota.[161] Under the Act companies must have 30% of directors from an underrepresented gender.[162] Companies face a € 50,000 fine and election nullification for non-compliance.[163] Other EU member states, including France, Belgium, Italy, and Greece, passed similar laws.[164] The United Kingdom, however, only requires that companies "pay due regard to benefits of diversity on the board, including gender when searching for and appointing directors."[165]

Europe's long history and continuous gender quotas and targets could help America to understand their laws' effectiveness and use it as a model in achieving board diversity. Several independent studies of European countries concluded that boards of directors are more diverse in countries with formal quotas and disclosure requirements, whereas voluntary targets are consistently less effective.[166] Still, "quotas" in the United States face strong Equal Protection challenges unique to the American Constitution and political landscape.

European laws require gender parity while American laws require female membership. The difference may seem semantic; however, requiring female membership as opposed to an underrepresented sex could make these mandates more likely to withstand American constitutional scrutiny.[167] For example, the EU directive is facially gender-neutral, and it can benefit men, women, and non-binary persons, depending on the board's current composition. Adopting the language of the EU directive may unlock the European mandates' effectiveness and withstand an Equal Protection Challenge as such.[168] Hawaii could become the first state to test this theory. In January of 2023, Congresswoman Amy

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161 Sharpless, *supra* note 2, at 192.

162 *Id.*

163 *Id.* at 192-93.

164 *Id.* at 193.

165 Seletha R. Butler, *All on Board! Strategies for Constructing Diverse Boards of Directors*, 7 VA. L. & BUS. REV. 61, 87 (2012) (quotations omitted); *see also id.* at 87 ("In Australia, corporations are required to disclose the company's progress toward board-established gender objectives, including disclosure of the number of females on the board of directors. The Swedish government has threatened to institute gender diversity requirements on companies if companies fail to voluntarily allocate 25% of the board seats to female directors.") (footnote omitted).

166 Houser & Williams, *supra* note 17, at 537-38.

167 *See generally Washington v. Davis*, 426 U.S. 229, 242 (1976) ("Nevertheless, we have not held that a law, neutral on its face and serving ends otherwise within the power of government to pursue, is invalid under the Equal Protection Clause simply because it may affect a greater proportion of one race than of another.").

168 *Id.*, *see Crest v. Padilla*, No. 19STCV2756, slip op. at 9 (Cal. Super. Ct. 2022) (finding § 301.3 to violate the Equal Protection Clause and noting that "S.B. 826's goal was to achieve gender equity or *parity*; its goal was not to boost California's economy, not to improve opportunities for women in the workplace nor not to protect California's taxpayers, public employees, pensions and retirees.") (emphasis added).

Perruso introduced H.B. 1191 to the Hawaii House of Representatives.[169] If enacted, H.B. 1191 would require that all publicly held domestic corporations with principal executive offices in Hawaii have at least three directors from the two groups.[170]

E. Alliance for Fair Board Recruitment v. SEC

In response to the SEC's approval of the Nasdaq rule, both the Alliance for Fair Board Recruitment ("the Alliance") and the National Center for Public Policy Research ("the Center") filed a lawsuit against the SEC challenging its order approving the Nasdaq rule in the Fifth Circuit. Nasdaq later joined the suit as a co-defendant. Oral arguments for the case occurred on August 29, 2022, but the case is still ongoing.[171]

Petitioner, Alliance for Fair Board Recruitment asserts the following three claims against the SEC: (1) the SEC order and the Nasdaq rule violate the Fifth Amendment Equal Protection Clause, (2) the SEC order violates the Free-speech Clause of the First Amendment, and (3) the SEC's approval of the Nasdaq rule violates the Exchange Act.[172]

Before the Fifth Circuit can address the first or second claim, however, the court must find that there was some state action in the case.[173] Petitioners rely on the close regulatory relationship between the SEC and stock exchanges to establish state action. [174] The Alliance relies on *Intercontinental Industries, Inc. v. American Stock Exchange* to argue that Nasdaq's "intimate" involvement and interdependence qualify as state action.[175] The Center, conversely, argues that Nasdaq acts as state actor because the stock exchange is a "creature of federal law, serves federal interests, and is controlled by a federal agency."[176] Petitioners

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169 H.R. No. 1191, 32nd Leg., Reg. Sess. (Haw. 2023).

170 *Id.*

171 *See* Oral Argument, Opening Brief for Petitioner Alliance for Fair Board Recruitment, *All. for Fair Bd. Recruitment & Nat'l Ctr. for Pub. Pol'y Rsch. v. SEC*, No. 21-60626 (5th Cir. Nov. 22, 2021) (No. 21-60626), https://www.ca5.uscourts.gov/OralArgRecordings/21/21-60626_8-29-2022.mp3.

172 *See generally* Opening Brief for Petitioner Alliance for Fair Board Recruitment, *All. for Fair Bd. Recruitment & Nat'l Ctr. for Pub. Pol'y Rsch. v. SEC*, No. 21-60626 (5th Cir. Nov. 22, 2021) [hereinafter *Opening Brief for the Alliance*].

173 *Id.* at 11-17.

174 *Id.* at 21; Opening Brief for Petitioner National Center for Public Policy Research at 18, *All. for Fair Bd. Recruitment & Nat'l Ctr. for Pub. Pol'y Rsch. v. SEC*, No. 21-60626 (5th Cir. Dec. 20, 2021) [hereinafter *Opening Brief for the Center*].

175 *Opening Brief for the Alliance*, *supra* note 172, at 21-22.

176 *Id*. at 18.

argue that, even if the court is unwilling to classify Nasdaq as a state actor, the SEC's approval of the Nasdaq rule qualifies as state action. [177]

Petitioners claim the Nasdaq rule violates due process and equal protection as it pertains to race and gender. [178] Regarding race, petitioners argue that Rule 5606(f) "encourages decisions to be made on the basis of protected classifications" and favors one race over the other thereby triggering strict scrutiny.[179] The Alliance also argues that the Nasdaq rule is a de facto racial mandate because noncompliance with the suggested number of diverse directors' subject companies to reputational harm and litigation risk.[180] Both defendants opposed such a classification. In its brief, the SEC persuasively argues that the Nasdaq rule "do[es] not mandate any particular board composition"; instead, it requires companies that list with the organization comply with the diversity matrix or explain why they did not meet the voluntary goal.[181] In its reply brief, Nasdaq urges the Fifth Circuit to accept its classification of Rule 5606(f) as a "disclosure-based framework, not a mandate or quota."[182]

As the rule pertains to gender classifications, petitioners argue the Nasdaq rule fails both strict scrutiny and intermediate scrutiny.[183] The Alliance argues the rule is not narrowly tailored because of the "inconclusive" nature of the empirical relationship between racial diversity and improved governance. [184] Furthermore, the Alliance argues the Nasdaq rule is overinclusive because it lacks a sunset clause and applies to every Nasdaq-listed company, regardless of if they have a documented history of discrimination.[185]

The Alliance argues the Nasdaq rule violates the First Amendment by compelling speech in that it requires Nasdaq-listed companies to disclose "controversial information in a non-viewpoint neutral manner.[186] The Alliance's argument is twofold.[187] First, the Alliance argue that the "explain" requirement

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[177] *Id.* at18, 22.
[178] *Id.* at 24.
[179] *Id.*
[180] *Id.* at 26.
[181] Brief for Respondent Securities and Exchange Commission at 3, *All. for Fair Bd. Recruitment & Nat'l Ctr. for Pub. Pol'y Rsch. v. SEC*, No. 21-60626 (Feb. 18, 2022).
[182] *Id.* at 12.
[183] *Opening Brief for the Alliance*, *supra* note 172 at 43; *Opening Brief for the Center*, *supra* note 174 at 21.
[184] *Id.*
[185] *Id.*
[186] *Id.* at 42.
[187] *Id.*

of the Nasdaq's comply or explain approach is not viewpoint neutral because only companies who fail to achieve the diversity matrix's requisite number of diverse directors must explain the composition of the board.[188] Second, the Alliance alleges that Rule 5606, which requires every Nasdaq-listed company to disclose the board members' gender, race, ethnicity, and sexual orientation is subject to, and would fail, strict scrutiny.[189] Finally, the Alliance argues the Nasdaq rule exceed the authority of the Exchange Act.[190] The SEC order approving the Nasdaq diversity rule found that the rule was consistent with Section 6(b)(5) and 6(b)(8) of the Exchange Act and that Section 6(b)(4) of the Act permitted the Board Recruiting Service Proposal.[191] Still, the Alliance maintains the SEC order was not "supported by substantial evidence, " which 15 U.S.C. § 78y(a)(4) requires.[192]

Outside of the same issues argued by the Alliance, the Center, in its opening brief, asserted that the SEC's approval of the Nasdaq rule violates the Vestment Clause and is arbitrary and capricious.[193]

First, the Center argues that SEC approval of the Nasdaq rule is a violation of the Vestment Clause.[194] The Center argues SEC approval of diversity quotas or disclosures exceeds the Commission's authority under the Exchange Act and the approval was part of a broader pattern of federal agencies regulate outside of their statutory authority.[195] The Center further argues "the Board Diversity Rules are indisputably an attempt by the SEC and Nasdaq to resolve major policy questions of vast economic and political significance" without Congress[196] and that regulatory resolution of the issue would disturb the balance of federalism since corporations are traditionally "creatures of state law." [197]

Finally, Center, in one last attempt at an appeal, argues that the SEC's order approving the Nasdaq rule was arbitrary and capricious.[198] Their reasoning is

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188 *Id.*
189 *Id.* at 42- 51.
190 *See Opening Brief for the Alliance*, *supra* note 172 at 54-67.
191 Self-Regul. Organizations; the Nasdaq Stock Mkt. LLC; Notice of Filing of Proposed Rule Change to Adopt Listing Rules Related to Bd. Diversity, Release No.34- 90574, at 40 (Dec. 4, 2020).
192 *Opening Brief for the Alliance*, *supra* note 172 at 58; *see also* 15 U.S.C. § 78y(a)(4) ("The findings of the Commission as to the facts, if supported by substantial evidence, are conclusive.").
193 *See Opening Brief for the Center*, *supra* note 174 at 24-30, 47.
194 *See Opening Brief for the Center*, *supra* note 174 at 24-30.
195 *Id.* at 25, 29.
196 *Id.* at 28, 31.
197 *Id.* at 28, 31.
198 *Id.* at 47.

twofold.[199] First, the Center argues the SEC adopted Nasdaq's rationale—that investors invest and vote based on directors' gender, race, and sexual preferences—without any independent analysis.[200] Second, petitioner argues the SEC did not consider important aspects of the Nasdaq recruitment rule such as who will create the list of ready candidates, the criteria for this list, and how Nasdaq defines "board-ready."[201]

II. WHEN THE DUST SETTLES: ANTICIPATING THE IMPACT OF CONSTITUTIONAL CHALLENGES TO BOARD DIVERSITY INITIATIVES

Academic literature views the comply or explain approach as a strong middle-of-the-road approach especially after the gender and racial mandate failures in *Crest v. Padilla I* and *II*,.[202] After all, the comply or explain approach is more effective than voluntary targets or non-binding resolutions, but it faces fewer facial constitutional challenges than the mandatory quota approach.[203] *Alliance for Fair Board Recruitment v. SEC* effectively puts the comply or explain approach on trial, and corporate board diversity advocacy currently stands at an impasse.

The Fifth Circuit upholding the Nasdaq rule on any grounds would be an unequivocal win for board diversity advocates; however, the grounds on which the court rules will have strong implications for future policymaking. For example, if the Fifth Circuit does not find state action, then the precedent would signal other stock exchanges that they may adopt similar listing rules. If the Fifth Circuit finds state action in this case, listing exchanges would likely be less inclined to pass rules that address board diversity or other ESG considerations because of the potential litigation cost.

The grounds by which the court could find state action also have significant implications for policies that address corporate diversity and for ESG investments in general. At oral arguments, the court spent a lot of time on questions about how the Nasdaq rule or SEC order could qualify as state action.[204] Particularly, the judges wanted to understand whether Plaintiffs argued

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199 *See generally id.* at 48-51.

200 *Id.* at 48.

201 *Id.* at 50-51.

202 Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1, 61 (2022).

203 *See* Katherine Sharpless, *California's S.B. 826: Will the Supreme Court Get on Board?*, 42 WOMEN'S RTS. L. REP. 172, 186-91 (2021).

204 *See generally* Oral Argument, Opening Brief for Petitioner Alliance for Fair Board Recruitment, *Alliance for Fair Board Recruitment & National Center for Public Policy Research v. SEC*, No. 21-60626 (5th Cir. Nov. 22, 2021) (No. 21-60626), https://www.ca5.uscourts.gov/OralArgRecordings/21/21-60626_8-29-

that any listing requirement was a state action because of listing exchanges' quasi-governmental relationship with the government, the SEC's approval of the Nasdaq rule made it state action, or SEC commissioners' statements supporting board diversity effectively made the Nasdaq rule state action.[205] If the Fifth Circuit finds the latter, any private action that aligns with a federal agency's regulatory agenda could be state action.[206]

The most unlikely, yet best, outcome for board diversity advocates would be for the Fifth Circuit to find there was state action in this instance but no constitutional violation. The Fifth Circuit is often cited as the most politically conservative circuit court in the country.[207] Therefore, even though *Alliance for Fair Board Recruitment v. SEC* would only bind those in the Fifth Circuit, it would be persuasive precedent for other circuits and signal public and private entities that they could adopt the comply or explain approach.

On the other hand, any Fifth Circuit finding the Nasdaq rule unconstitutional would majorly setback diversity advocates. Still, the grounds for such a holding would create different hurdles for future policymaking. In *Alliance for Fair Board Recruitment*, Petitioners argue the Nasdaq rule is a de facto quota or, in the alternative, the rule operated as a racial target that encouraged diversity.[208] Whether the comply or explain approach operates as a quota or a racial target is an issue of first impression. Regardless of the classification, however, the Nasdaq rule is unlikely to pass strict scrutiny because how it uses racial classifications or even heightened scrutiny regarding gender and sexuality classifications.[209] Furthermore, if the court found that the comply or explain approach operated as a racial target and violated due process, voluntary targets and nonbinding resolutions, like those in Washington, Maryland, and Colorado could be on the chopping block next.

2022.mp3; *see also* Cydney Posner, *Fifth Circuit Hears Oral Argument on Challenge to Nasdaq Board Diversity Rules—Will the Rules Survive?*, JD SUPRA (Sept. 8, 2022), https://www.jdsupra.com/legalnews/fifth-circuit-hears-oral-argument-on-8046591/.

205 *Id.*

206 *See* EPA, *Laws & Regulations*, *Regulatory Agendas & Regulatory Plans*, (explaining the timeline and purposes of federal agencies' regulatory agendas) (last updated Nov. 15, 2022) https://www.epa.gov/laws-regulations/regulatory-agendas-and-regulatory-plans.

207 Ann E. Marimow, *Trump's Lasting Legacy on the Judiciary Is Not Just at the Supreme Court*, THE WASHINGTON POST (Jan. 29, 2023), (noting that the 5th Circuit has historically leaned conservative but has become increasingly so under the Trump administration) https://www.washingtonpost.com/politics/2023/01/29/5th-circuit-court-trump-judges-conservative/.

208 *Opening Brief for the Alliance*, *supra* note 172 at 24.

209 Adam Winkler, *Fatal in Theory and Strict in Fact: An Empirical Analysis of Strict Scrutiny in the Federal Courts*, 59 VAND. L. REV. 793, 815 (2019) (finding that the survival rate of cases in federal court where strict scrutiny is applied to suspect class discrimination is twenty-seven percent).

The Court could find two foreseeable ways in which the Nasdaq rule violated the First Amendment. First, the Court could hold that a requirement that a corporation explain its noncompliance with the Nasdaq diversity matrix is unconstitutional because it is not viewpoint neutral or because it compels speech. Second, the Court could rule that Nasdaq's mandatory disclosure framework violated the First Amendment. The latter would jeopardize every state law that addresses board diversity. As in Section I, every state with a statute or resolution that addresses board diversity requires or encourages diversity disclosures. Additionally, the SEC proposed many ESG disclosures in the past year to "promot[e] consistent, comparable, and reliable information for investors."[210] A Fifth Circuit holding that creates precedent that mandatory disclosures violate the First Amendment would not only impact the most common policy tool to address board diversity at both the state and federal level, but would question the legality of all ESG-related disclosures and prevent shareholders access to standardized information about corporations. Finally, the Fifth Circuit decides whether the Nasdaq rule exceeds the Exchange Act's or Vestment Clause's authority. Such a holding would question any listing exchanges and the SEC's authority to promulgate rules that relate to ESG considerations and present a large, legal barrier to several proposed rules on the SEC's 2023 regulatory agenda.[211]

Alliance for Fair Board Recruitment is a case where future board diversity and potentially ESG investing hangs in the balance because it uses what many scholars thought to be a middle-of-the-road approach that would withstand constitutional challenge. If the court does not uphold the Nasdaq rule, *Alliance for Fair Board Recruitment* may force diversity advocates to leave behind the fight for statutory or regulatory remedies and fully embrace shareholder activism in the fight for board diversity.

III. WALKING THE LINE: BOARD DIVERSITY INITIATIVES THAT ARE BOTH EFFECTIVE & LIKELY TO WITHSTAND CONSTITUTIONAL CHALLENGE

Alliance for Fair Board Recruitment and *Crest v. Padilla I and II* highlight a uniquely American struggle: the more effective the approach to achieve board diversity, the stronger the constitutional challenge. While gender quotas with harsh penalties for noncompliance are effective at achieving board diversity in

[210] *ESG Disclosures for Investment Advisers and Investment Companies*, U.S. SEC. & EXCH. COMM'N, https://www.sec.gov/files/ia-6034-fact-sheet.pdf (last visited Jan. 28, 2023).

[211] David Freed, *SEC Rulemaking Agenda for 2023 Released*, JD SUPRA (Jan. 6, 2023), htttps://www.jdsupra.com/legalnews/sec-rulemaking-agenda-for-2023-released-5522541/.

Europe, they violate the Equal Protection Clause and will likely fare no better after the Supreme Court hands down two decisions regarding affirmative action in *Students for Fair Admissions* v. *UNC* and *SFFA v. Harvard*, both of which are expected in the Summer of 2023.[212]

However, it is important, to ensure that board diversity and other ESG objectives are achieved through constitutionally sound means and are appealing to both sides of the aisle. With those legal limitations and policy goals in mind, the SEC should adopt a rule promulgating an S-K disclosure regarding board diversity. On January 4, 2023, the Office of Information and Regulatory Affairs of the SEC released its Fall 2022 Unified Agenda.[213] The Agenda contains a proposed disclosure addressing board diversity.[214] The only available information regarding the potential rule is as follows: "the Division is considering recommending that the Commission propose rule amendments to enhance registrant disclosures about the diversity of board members and nominees."[215] With the Notice of Proposed Rule Making set to be published in October of 2023,[216] this Comment suggests a framework for an SEC board diversity disclosure.

A. What the SEC Board Diversity Proposal Should Include

Defining diversity is a vexing task and a task that is easy to criticize. If one defines diversity too narrowly, one runs the risk of missing cross-sections of identities that can add value and perspective to the boardroom. If one defines diversity too expansively, one runs the risk of allowing companies to garner the benefits of claiming that they are diverse while one gender or race is overrepresented. While the SEC's definition of "diversity" in Item 407 has faced criticism for its breadth, it would be illogical and confusing for the SEC to adopt two definitions of diversity for the same S-K disclosure. Furthermore, the SEC's definition of diversity in Item 407 aligns with the diversity indica that large investment firms, like BlackRock and State Street Global, use in their proxy voting guidelines.[217] Consequently, the SEC should retain the definition of

212 *See* Valerie Strauss, *The Element of Suspense in Supreme Court 023 Affirmative Action Ruling*, THE WASHINGTON POST (Jan. 16, 2023, 7:00 AM), https://www.washingtonpost.com/education/2023/01/16/suspense-supreme-court-affirmative-action/.

213 Chair Gary Gensler, *Statement on Fall 2022 Regulatory Flexibility Agenda*, U.S. SEC. & EXCH. COMM'N, (Jan. 4, 2023), https://www.sec.gov/news/statement/gensler-fall-2022-reg-flex-agenda-20230104.

214 *Corporate Board Diversity*, RIN: 3235-AL91, OFFICE OF INFORMATION AND REGULATORY AFFAIRS, https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=202210&RIN=3235-AL91.

215 *Id.*

216 *Id.*

217 *See* Section III, Part B, subsection 1.

diversity in Item 407 but structure the disclosure in the following bipartisan system to ensure that data regarding demographic diversity is readily available.

First, the SEC's board diversity rule should require firms to disclose the total number of directors on the firm's board and the self-identified race, ethnicity, and gender of board members and nominees. The rule should also require disaggregated data requiring the company to identify the demographic data of the chair of the board, the chair of the nominating committee, and the chair of the executive compensation committee as well as the members of those committees. Identifying the demographic characteristics of these powerful committees addresses concerns raised regarding "identity capitalism" or the "commodification of the outgroup" by clearly demonstrating if diverse members have membership in positions of influence. [218] There is a difference between having a seat at the table and having a voice at the table.[219] These committees are understood to be those with the most influence on the board and the company as a result.[220] Together, this data will better help shareholders and stakeholders alike understand whether a company's board has reached critical mass or whether diverse directors are placed in positions of power. Such disclosure also recognizes that, historically, underrepresented directors are given access to positions of influence on corporate boards at a much lower rate than their white, male counterparts.[221] Finally, such information would provide a bulwark for activist investors against boards who claim that they have diversified their boards even though their definition of diversity fails to account for demographic diversity.

The second part of the disclosure should be voluntary to allow companies to supplement demographic disclosures with disclosures about broader characteristics of diversity such as age, military service, socioeconomic status, disability, geographic history, or sexuality. As such, companies could supplement demographic data with whatever information they feel is important or representative of the directors' diverse perspectives and experiences. These discretionary disclosures would honor the distinction between demographic and

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[218] *See* Ellen E. Farwell, *A Real Seat at the Table: Identity Capitalism and State Law Efforts to Diversify Corporate Boards*, 56 NEW ENG. L. REV. 141, 151 (2022).
[219] *Id.*
[220] *Id.*
[221] *Id.*

cognitive diversity and give investors a better idea of the diversity, or lack thereof, of directors' lived experiences.[222]

Finally, the SEC should require companies to include these disclosures in their initial filing and in their annual S-K disclosures, which are in turn made public on EDGAR.[223] Together, this bipartite framework mandates the disclosure of demographic data while encouraging companies to outline other unique aspects and experiences of their directors. A board diversity disclosure like this would standardize the data regarding board diversity available to investors, investment advisors, and asset managers.

B. Legal Authority & Justifications for an SEC Board Diversity Disclosure

The SEC promulgating a rule requiring such a disclosure framework is effective both for the above reasons and because it would likely withstand constitutional challenge. The SEC has broad authority to require registrants to disclose information under both the Securities Act of 1933 and the Securities Exchange Act of 1934.[224] Under that statutory authority, the SEC is authorized to require issuers to disclose information regarding "the organization, financial structure, and nature of the business",[225] to promulgate rules "as necessary or appropriate for the proper protection of investors, and to ensure fair dealing in the security."[226]

First, Section 14(a) of the Exchange act vests the SEC with the authority to protect the public interest and investors by regulating the proxy voting process.[227] A mandatory diversity disclosure for all issuers protects shareholders because it gives shareholders the information they want and need to exercise their voting power and unprecedented access to standardized information to compare how companies perform in comparison to their competitors.[228] Such a disclosure is increasingly important because analysts predict the 2023 proxy season will see an increase in overall shareholder proposals and "anti-ESG"

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[222] Allison Reynolds & David Lewis, *Teams Solve Problems Faster When They're More Cognitively Diverse*, HARVARD BUSINESS REVIEW (Mar. 20, 2017), https://hbr.org/2017/03/teams-solve-problems-faster-when-theyre-more-cognitively-diverse.

[223] *See generally About EDGAR,* U.S. SEC. & EXCH. COMM'N, (last updated Oct. 6, 2022) https://www.sec.gov/edgar/about.

[224] Jill E. Fisch, *The SEC's Authority to Pursue Climate-Related Disclosure*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE (June 20, 2022), https://corpgov.law.harvard.edu/2022/06/20/the-secs-authority-to-pursue-climate-related-disclosure/.

[225] Securities Exchange Act of 1934, 15 U.S.C. § 78*l*(b)(1).

[226] *See* Securities Exchange Act of 1934, 15 U.S.C. § 78m(a)(1).

[227] *See* Securities Exchange Act of 1934 § 14(a).

[228] Order Approving Nasdaq Proposed Rule Changes, 86 Fed. Reg. 44424, 44425 (Aug. 12, 2021).

proposals.[229] While "anti-ESG" proposals have been historically unsuccessful,[230] a diversity disclosure would allow those advocating for and against a proposal to make more informed decisions because a diversity disclosure provides access to comparative empirical data regarding board composition and nomination.

Second, the SEC is responsible for promulgating rules that promote competition in investor capital.[231] A board diversity rule achieves that purpose by standardizing the varied diversity disclosures that companies are subjected to under competing state laws.[232] This makes it difficult for investors to compare and for ESG-ranking firms to value.[233] An SEC board diversity disclosure would be published on EDGAR, which would make all issuer data public. [234] In turn, ESG firms would have standardized data from all issuers to accurately rank firms' diversity. Notably, asset managers predict ESG-related assets to be valued at $33.9 trillion annually by 2026.[235] In other words, there is a lot of money up for grabs in ESG investing in the next three years and competition for those investments must be informed and fair. The premise of this proposed disclosure is not the contested empirical relationship between diversity and firm value nor is a value judgment.[236] Rather, the value of the disclosure comes from making

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229 Merel Spierings, *2023 Proxy Season Preview – Comprise and Conflict Ahead*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE (Mar. 9, 2023), https://corpgov.law.harvard.edu/2023/03/09/2023-proxy-season-preview-compromise-and-conflict-ahead/.

230 Clara Hudson, *Conservative Shareholder Proposals Rise Amid Anti-ESG Rumbles*, BLOOMBERG LAW, (Aug. 31, 2022, 5:00 AM), https://news.bloomberglaw.com/securities-law/conservative-shareholder-proposals-rise-amid-anti-esg-rumbles.

231 *Id.*

232 *Id.*

233 *See, e.g.*, U.S. Gov't Accountability Off., Gao-20-530, Public Companies: Disclosure of Environment-Al, Social, and Governance Factors and Options to Enhance Them (2020).

234 U.S. SEC. & EXCH. COMM'N, supra note 223.

235 Ryan Stanton, *ESG-Focused Institutional Investment Seen Soaring 84% to US $33.9 Trillion in 2026, Making Up 21.5% of Assets Under Management: PwC Report*, PWC (Oct. 10, 2022), https://www.pwc.com/gx/en/news-room/press-releases/2022/awm-revolution-2022-report.html.

236 *Compare* Abhilasha Gokulan, *Increasing Board Diversity: A New Perspective Based in Shareholder Primacy and Stakeholder Approach Models of Corporate Governance*, 96 N.Y.U. L. REV. 2136, 2147, 2151-52 (2021) (finding that having a higher percentage of female directors is positively associated with an increase in invested capital, sales, equity, and return on assets in a study of *Fortune* 500 companies), *and* Mary Curtis et al., GENDER DIVERSITY & CORPORATE PERFORMANCE, CREDIT SUSIE, 12 (2012) (stating that several studies have found female representation is correlated with increased stock price when compared to all-male boards), *and* SUNDIATU DIXON-FYLE ET AL., DIVERSITY WINS: HOW INCLUSION MATTERS 8 (3rd ed. 2020), https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters (finding that racially and ethnically diverse companies are consistently more likely to financially outperform peer companies), *with* Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1, 32-33 (2022) (detailing studies that have found a negative or inconclusive relationship between board diversity and firm value).

stock competition more competitive and effective, which the SEC is statutorily required to do.[237]

Finally, even if the Fifth Circuity does not uphold the Nasdaq rule, then a diversity disclosure is even more important because it does not act as a de jure or de facto quota. Furthermore, broader disclosure frameworks have continuously been upheld in the past. Notably,

> no court has invalidated a Commission rule for overstepping the Commission's disclosure authority despite the Commission's active rulemaking spanning close to nine decades and despite the fact, as is often the case with economic regulation, many of the Commission's rules were initially resisted by the regulated entities and other interested parties.[238]

Furthermore, Congress, despite having the ready authority to do so, has never passed a legislative override of an SEC disclosure.[239] These two facts highlight that over time, throughout periods of regulation and deregulation and different political administrations that Congress widely recognizes the SEC's broad power to promulgate rules relating to disclosures. Overall, this is the next step that must be taken to address board diversity in America.

CONCLUSION

To be clear, this Comment in no way suggests that an SEC board diversity disclosure would eradicate disparities on corporate boards. Nor does this Comment suggest such a disclosure is immune from the same legal claims argued *in Alliance for Fair Board Recruitment v. SEC*. However, this comment argues that an SEC board diversity disclosure rule is more likely to withstand constitutional challenge than the "comply or explain" approach because no court has ever overruled an SEC rule nor has Congress ever used its legislative power to moot such a rule.[240] Furthermore, the adoption of such a rule sets a solid foundation for continued shareholder activism through more informed shareholder proposals and ESG investing.

Regardless of the Fifth Circuit or the California Court of Appeals' future rulings, shareholder proposals, proxy disclosures and guidelines, IPO pledges,

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[237] *See* Securities Act of 1934 § 2(b).

[238] Jill E. Fisch, *The SEC's Authority to Pursue Climate-Related Disclosure*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE, (Jun. 20, 2022), https://corpgov.law.harvard.edu/2022/06/20/the-secs-authority-to-pursue-climate-related-disclosure/.

[239] *Id.*

[240] *Id.*

and ESG investing are predicted to become more popular tools and should be immune from constitutional challenges as they do not require state action. To supplement those efforts, a board diversity disclosure is necessary to provide clear, publicly accessible, and standardized information about board composition, which would promote fair competition and protect investors.

A diversity disclosure also could aid state governments in responding to legal challenges. In *Crest v. Padilla II*, the California Secretary of State did not provide convincing evidence of discrimination in corporate board selection for remediation.[241] However, the court noted that state could have proven discrimination by "a properly established statistical disparity" or a "properly traced statistical history."[242] § 301.3 and § 301.4 may have faced a different fate if the California Secretary of State could wield SEC data to prove discrimination. As such, an SEC board diversity rule would create data which could better equip states to implement board diversity legislation to respond to any constitutional challenges successfully. Regardless, a board diversity disclosure framework promotes a free market, encourages fair competition, and provides better support for private and public actors to advocate for board diversity in the future.

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241 *Crest v. Padilla*, No. 20 STCV 37513, 2022 WL 1073294, at 11, 15 (Cal. Super. Ct 2022).
242 *Id. at 15.*