NASDAQ Board Diversity Proposal Approved By the SEC

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On August 6, 2021, the SEC approved Nasdaq's board diversity proposal set forth in Rules 5605(f) and 5606 of the Nasdaq Listing Rules.

__Board Diversity Disclosure__. Most Nasdaq-listed companies will be required to disclose the number of their directors who self-identify as diverse. For this purpose, Nasdaq has defined diverse as an individual who self-identifies as one or more of these categories: (i) a woman (regardless of sex designation at birth), (ii) an "Underrepresented Minority" (Black or African American, Hispanic or Latinx, Asian, Native American or Alaskan Native, Native Hawaiian or Pacific Islander, or two or more races or ethnicities (defined as a person who identifies with more than one of these categories: White (not of Hispanic or Latinx origin), Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander)) or (iii) as lesbian, gay, bisexual, transgender or a member of the queer community ("LGBTQ+"), by August 8, 2022 or the date of the company's proxy or information statement for its 2022 annual meeting (if later).

__Board Diversity Standards__. Most Nasdaq-listed companies will also be required to have at least one director who self-identifies as a woman and at least one director who self-identifies as an Underrepresented Minority or LGBTQ+. Smaller reporting companies and foreign issuers may satisfy this standard by having two directors who self-identify as women. Companies with five or fewer directors ("Small Boards") only need to have one director who self-identifies as diverse to meet this standard. A company with a Small Board prior to becoming subject to this standard may also add a sixth director who self-identifies as diverse without becoming subject to having two diverse directors.

To assist its listed companies that do not currently meet these standards, Nasdaq has been approved by the SEC to offer free board recruiting services in partnership with Equilar for one year.

If a Nasdaq-listed company does not meet the applicable standard, it must explain why it does not meet its board diversity standard. Nasdaq will only confirm that the company has provided the required explanation, it will not evaluate the substance of that explanation.

__Transition Timing__. The timing of the date of compliance with these new board diversity standards depends on the company's listing tier and board size:

- Nasdaq Global Select Market and Nasdaq Global Market: These companies must have one diverse director by August 7, 2023 and two diverse directors by August 6, 2025 or explain why they do not by the respective deadlines.
- Nasdaq Capital Market: These companies must have one diverse director by August 7, 2023 and two diverse directors by August 6, 2026 or explain why they do not by the respective deadlines.
- Companies with Small Boards: These companies, regardless of listing tier, must have, or explain why they do not have, one diverse director by August 7, 2023.

The deadlines may be extended if the company files its proxy or information statement for the company's annual meeting of shareholders in the applicable year after the respective deadlines. If the company does not file a proxy/information statement, the disclosure must be included in the company's Form 10-K or Form 20-F.

Location of Disclosure. The diversity disclosures and any explanatory statement must be presented together in the company's (i) annual proxy or information statement, (ii) Annual Report on Form 10-K or 20-F (if it does not file proxy/information statements), or (iii) website. If a company posts the disclosure on its website, it will need to submit the disclosure to the Nasdaq Listing Center, including the URL, within one business day after the posting on its website.

Form of Disclosure. Nasdaq requires its listed companies to use a standardized board diversity matrix. Foreign issuers may use an alternative board diversity matrix if they choose to disclose directors who self-identify as underrepresented persons in the foreign issuer's home country or indicate that the board diversity disclosure is prohibited under its home country law. Companies will need to disclose the board diversity matrix for both the current and immediately preceding year after the first year of implementation.

Failure to Meet the Board Diversity Standards. If a company has a board vacancy and no longer meets the applicable board diversity standard, it will have until the later of (i) one year from the date of the vacancy or (ii) the date the company files its proxy/information statement (or Form 10-K or 20-F if it does not file a proxy/information statement), to meet the applicable standard. If a company fails to provide the diversity disclosures within the required time, it will be subject to delisting proceedings.

Exemptions. While controlled companies do not qualify for an exemption from the board diversity requirements, certain other companies have been provided with such an exemption. For instance, SPACs are not subject to the board diversity requirements until their business combinations. There are also exemptions for asset-backed issuers, cooperatives, limited partnerships, management investment companies, and issuers of non-voting preferred securities, debt securities and derivative securities that do not have equity securities listed on Nasdaq. A company that ceases to be exempt will have until the later of (i) one year from the date it no longer qualifies as an exempt company and (ii) the date it makes its annual meeting filing during the following calendar year to satisfy the board diversity requirements.

SEC Approval. As has often been the case recently, the SEC's approval of Nasdaq's board diversity proposal was not unanimous. Commissioners Roisman and Peirce both voted against the board diversity disclosure proposals, with Commissioner Peirce doing so in the longest dissent in recent memory (13 pages). We expect litigation may be used to challenge this action, which could delay the implementation of these board diversity standards.

Action Steps. Nasdaq-listed companies that do not meet the board diversity standards should begin identifying potential diverse director nominees. Such company's should take advantage of the free recruiting services being offered by Nasdaq over the next year. Nasdaq companies that do not already do so should add diversity questions to their annual director and officer questionnaires and a consent to disclosure from each director or nominee. Listed companies should determine how best to add the Nasdaq board diversity matrix in their proxy/information statement or 10-K/20-F. Consideration should be given to whether privacy needs to be taken into account, particularly by foreign issuers. If a listed company makes changes to its nominating committee's process for identifying and evaluating nominees for director due to these new requirements, it should review its disclosure obligations under Item 407(c)(2)(vi) of Regulation S-K and disclosure interpretations 116.11 and 133.13.

Miscellaneous. While the board diversity disclosure requirement may not be an explicit mandate, we expect most companies will try mightily to avoid having to disclose that they do not meet this requirement and why.

Given the number of other initiatives related to board diversity (i.e., California statutory mandate, proxy advisory firms and institutional investor policies and the potential for further action by the SEC as noted in its most recent flex agenda), all public companies should be monitoring this issue closely.

For questions regarding Nasdaq's new board diversity rules, please contact your GableGotwals attorney or a member of our Corporate & Securities team.

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