Nasdaq's Board Diversity Rule Still a Mistake

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On Friday the Securities and Exchange Commission (SEC) approved a new rule from Nasdaq that will require firms listed on that exchange to comply with a board diversity goal or provide a public explanation for why they do not have the prescribed demographic profile. The rule calls for all firms to have "at least two members of its board of directors who are Diverse, including at least one director who self-identifies as female and at least one director who self-identifies as an Underrepresented Minority or LGBTQ+." Listed firms will also be required to disclose "information on the voluntary self-identified gender and racial characteristics and LGBTQ+ status" of the entire board.

The Competitive Enterprise Institute opposed this new rule, and I filed a comment with the SEC to that effect in March of this year. While comments in opposition to the proposal covered a lot of territory, my statement covered the following topics:

- Empirical evidence undermines Nasdaq's case
- Danger of tokenism and backlash
- Women have different career priorities than men
- Impact on potential LGBTQ+ directors
- Cumulative regulatory burden

Sen. Pat Toomey (R-PA), as ranking member of the Senate Banking Committee, has been outspoken in opposition to the rule as well. In a short statement on Friday, he said:

Corporate board rooms, like all organizations, can benefit from a diversity of perspectives, but NASDAQ's one-size-fits-all quota misses the mark. By defining diversity by race, gender, and sexual orientation, NASDAQ's mandate will inevitably pressure companies to subordinate crucial factors such as knowledge, experience, and expertise when selecting board members. … I'm disappointed Chairman Gensler is turning a financial regulator into a laboratory for progressive social engineering.

Friday's statement covered some of the same territory as the SEC comment co-signed by the Republican members of the Banking Committee in February, which advanced three major arguments. Specifically, it states that NASDAQ's proposal:

- Runs contrary to a corporation's duty to nominate to its board of directors individuals who will serve the best interests of the corporation and its shareholders;
- Violates the concept of materiality; and
- Would harm economic growth.

An even more in-depth refutation (28 pages) was published by the Heritage Foundation's David Burton in March. The key takeaways with this study were that the proposed rule:

- Would impose quotas on the basis of sex, sexual orientation, race, and ethnicity;
- Is a major step backwards morally—and is inconsistent with the equal protection principles of the Constitution and the Civil Rights Act of 1964; and
- Is inconsistent with the SEC's statutory mission.

One more interesting comment in opposition to the rule came from the chairman of an actual Nasdaq-listed company, Joe Shoen of Amerco, the parent company of U-Haul:

If AMERCO were to select Board Members based TO ANY DEGREE on race, gender identification or sexual orientation, as an investor, I would be greatly distressed. The proposed rule would clearly encourage such behavior although it would be well masked.

I have witnessed the country struggle for decades to not sort people by race, gender, and sexual orientation. This has become the law of the land. Why now under the guise of social good should the SEC participate in stepping backwards?

In addition to these arguments, there is also the question of why such rules are necessary in the first place. Advocates tell us that many companies are already moving toward making their boards more diverse and that there is academic validation for the premise that firms with more diverse boards enjoy a range of advantages, including being more profitable. But if those things are so clearly established, why would such a policy need to be required? Are the nation's infamously rapacious capitalists, who allegedly care about *nothing* but profit, just leaving valuable advantages on the table because they detest the idea of female directors? Are we to believe business leaders in American are motivated solely by greed and misogyny in equal parts, with only the SEC able to break the tie?

Finally, we are supposed to be reassured that such a rule will be welcomed because, as with many other environmental, social, and governance (ESG) topics, this information on board diversity is being demanded by investors. But is it? The Cato Institute's Jennifer Schulp recently found that, unlike the traditional economic definition, demand for policy change and ESG disclosure is not so easy to measure.