

CLIENT ALERT

Navigating Compensation Governance

Federal Appeals Court Upholds Nasdaq Board Diversity Rule

Nasdaq's board diversity rule survives legal challenge.

The diversity rule requires Nasdaq listed companies to disclose board diversity statistics and to include at least two diverse directors on their boards or explain why this requirement is not met.

The court ruling contrasts with the judicial rulings striking down California's board diversity mandates as unconstitutional. Unlike the state of California, Nasdaq is not a state actor and therefore, not subject to constitutional constraints.

Background on Nasdaq Board Diversity Rule

In August 2021, the Securities and Exchange Commission approved Nasdaq's proposed rule which requires each Nasdaq-listed company (subject to certain exceptions) to meet the following requirements:

- Publicly disclose board-level diversity statistics in a prescribed format in the company's annual proxy statement (or similar filing) or on the company's website; and
- Include at least two diverse directors by a specified date, based on the company's listing tier, or publicly disclose and explain its noncompliance with the board diversity requirement.

Generally, a listed company would meet the diversity requirement if its board includes both: (i) a director who self-identifies as female, and (ii) a director who self-identifies as either an underrepresented minority or LGBTQ+ (see [Meridian Client Update dated August 19, 2021](#) for more details on the Nasdaq board diversity rule).

Legal Challenge and Ruling

The Alliance for Fair Board Recruitment (AFBR) and National Center for Public Policy Research claimed in a federal court lawsuit against Nasdaq that the diversity rule violated the First and Fourteenth Amendment of the U.S. Constitution and the SEC's approval of the diversity rule exceeded the Commission's authority under the Securities Exchange Act.

On October 18, 2023, a three-judge panel on the Fifth Circuit of the U.S. Court of Appeals ruled against AFBR and National Center for Public Policy Research. The Court found the following:

- As a private entity, Nasdaq is not subject to constitutional constraints under the First or the Fourteenth Amendments because Nasdaq is neither: (i) a “state actor”, nor (ii) so entangled with the SEC through the rule approval process that it should be treated as a state actor.
- The SEC’s approval of the Nasdaq board diversity rule did not exceed its authority under the Securities Exchange Act.

Implications of Ruling on Compliance with Diversity Requirements

Unless a court issues a stay order, each Nasdaq-listed company must meet the following diversity requirements (or alternatively explain why the diversity requirements have not been met) according to the following timeline:

- By December 31, 2023, each Nasdaq-listed company must have one diverse director.
- By December 31, 2025, each company listed on the Nasdaq Global Select or Nasdaq Global Markets must have two diverse directors.
- By December 31, 2026, each company listed on the Nasdaq Capital Market must have two diverse directors.

In addition, Nasdaq-listed companies must disclose board diversity statistics each year no later than December 31, with the first disclosure due by December 31, 2023.

For those companies first listed on Nasdaq after December 31, 2022, the above deadlines may differ depending on the date of listing.

Meridian comment. While the federal appeals court ruling is a win for the SEC and Nasdaq, it may not be the final word on the matter. On October 25, 2023, AFBR and National Center for Public Policy Research filed a petition requesting a rehearing by the entire Fifth Circuit. When the Fifth Circuit will take up the case is not known at this time.

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The [Client Update](#) is prepared by Meridian Compensation Partners’ Governance and Regulatory Team led by Donald Kalfen. Questions regarding this Client Update or executive compensation technical issues may be directed to Donald Kalfen at 847-347-2524 or dkalfen@meridiancp.com.

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