BOARD REFRESHMENT AND DIVERSITY MANDATE

The business imperative for diversity is widely known and well documented but has yet to take hold in public company C-suites, much less the boardroom. **BY SHELLY HOGANS, CMA, CPA**

NASDAQ'S NEW LISTING RULES SURROUNDING board diversity composition were approved by the U.S. Securities & Exchange Commission on August 6, 2021. According to the board diversity rule, companies listed on Nasdaq's U.S. stock exchange must "publicly disclose board-level diversity statistics using a standardized template; and have or explain why they do not have at least two diverse directors" (bit.ly/3B2EKPy). The rule requires at least one director on the board be a woman and at least one member be from an underrepresented group.

But it provides flexibility in compliance by smaller reporting companies and foreign issuers, which are granted the latitude to meet this mandate by including two female directors and allowing companies with five directors or fewer "to meet the diversity objective by including one diverse director."

The time frame to comply is based on the company's listing tier with Nasdaq and ranges between two and five years from August 2021. In addition, any special purpose acquisition company listed under Nasdaq Rule IM-5101-2 is exempt from the disclosure requirement until completion of its business combination. Although the board diversity rule is a well-intentioned rule, designed to promote inclusivity and advance diversity among the board, we've yet to see if it will be met with enthusiastic acceptance or if it will face executional resistance or, worse, performative implementation, meaning it will only be followed to meet the Nasdaq requirements, without any additional efforts for the overarching goal of diversity, equity, and inclusion.

BOARD REFRESHMENT

How will companies comply with the rule given current board composition and board terms, as well as lack of information to "identify" the existing board relative to the new mandate? For companies without an existing board refreshment and succession planning process that addresses board tenure and retirement, implementation of the new rule may prove to be disruptive. In such sce-

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narios, board refreshment could include an assessment of directors' skills, gaps, tenure, anticipated time horizon for departures, succession plans, and candidate profiles, including a diversity component made evident in the board application process.

The 2020 proxy season provided an opportunity for companies to collect potentially sensitive diversity data from board members by altering directors' and officers' questionnaires, allowing board members to self-identify.

SEARCHING FOR DIVERSE TALENT

Will existing board members choose to give up seats to make room for more diverse representation, or will companies amend their bylaws or articles of incorporation to address board structure, perhaps through a board expansion? In cases of noncompliance, what reasons will companies cite in their human capital disclosures regarding their inability to fill board seats with diverse candidates? If the mandate isn't met, will those from underrepresented populations continue to hear the all too familiar "We can't find diverse talent"?

Herschel Frierson, chair of the board of directors of the National Association of Black Accountants (NABA) and principal at Crowe LLP, commented: "If you go to the same pond, you will get the same fish. Companies need to expand their outreach to organizations like ourselves, NABA. We have the talent in our membership who can meet the needs around the board table; we just need the opportunity. I encourage companies to reach out to NABA to help fill board positions and work with us to build a pipeline for the next generation of board members." To boost company search efforts and enrich "the supply of diverse and qualified board candidates," Nasdaq has also partnered with Athena Alliance, Equilar, and theBoardlist to provide complimentary tools to assist companies in sourcing board candidates (bit.ly/2Zajl9S).

Another way is for nominating and governance committees to focus on board competencies rather than just job titles to "find" the talent. That isn't a lowering of standards or board qualifications. It is, however, an acknowledgment that diversity is similarly lacking among the population of individuals holding traditional C-suite titles, previously seen as the treasure trove for obtaining board talent. Nominating committees must expand their search and network to diverse populations. It's important that companies comply with the rule as they would with any other corporate initiative—what gets measured and allocated resources simply gets done.

RAMIFICATIONS OF NONCOMPLIANCE

Will there be repercussions for companies that opt for explaining the lack of diversity on their boards? Some proxy advisory service firms, like Institutional Shareholder Services Inc., the Vanguard Group, and Glass Lewis, have signaled via their policies that they will recommend an "against" or "withhold" vote for the nominating committee chair for degrees of noncompliance with the diversity rule (bit.ly/3jHvUkn). Goldman Sachs announced in 2020 that it wouldn't help a company go public unless the company's board included at least one board member from an underrepresented group, and starting July 2021, the bank increased this requirement to two such board members, one of whom must be a woman (bit.ly/3E37Pwl).

Will shareholders, investors, or other third parties clamor for greater transparency? William Poudrier, president of The Proxy Advisory Group LLC, a corporate proxy advisory/solicitation firm, said, "For the 2022 proxy season, we anticipate that for the first time, several prominent institutional investors will be submitting protest votes against the reelection of those directors who chair nominating/governance committees at companies where the board lacks any racial or ethnic representation. This institutional stockholder protest trend seems bound to grow and extend for the foreseeable future."

Egon Zehnder, a global leadership advisory, management consulting, and executive recruitment firm, states in its 2020 Global Board Diversity Tracker that it "takes three underrepresented voices in a boardroom to truly change internal dynamics" (bit.ly/2Z5y7P7). Once these voices are included on the board, it isn't just about having a seat at the table but also about being a valued member and being able to fully contribute and bring one's authentic self to the boardroom. Moreover, the board diversity rule should also give a company's board an impetus to hold its senior management accountable for diversity traction or lack thereof beyond board composition, as part of the company's operations.

Until companies voluntarily choose to fill board seats in a manner that's representative of the diversity of talent, the Nasdaq mandate is a step in the right direction. Hopefully, one day we won't need a governing body like Nasdaq to mandate diversity in board composition, but rather, companies will voluntarily choose to fill board seats reflective of diverse talent everywhere. **SF**

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