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The Future (Public Company Boardroom) is Female: From California SB 826 to a Gender Diversity Listing Standard

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THE FUTURE (PUBLIC COMPANY BOARDROOM) IS FEMALE: FROM CALIFORNIA SB 826 TO A GENDER DIVERSITY LISTING STANDARD

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I. INTRODUCTION

The issue of board diversity has received an unusual amount of attention in recent years as corporations face an increasing amount of pressure to add

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more women to their boards.¹ In 2017, State Street Corporation, the world's third-largest asset manager, made headlines when it announced its board gender diversity campaign by placing a statue of the Fearless Girl staring down the Charging Bull of Wall Street in New York City's Financial District.² At the beginning of 2020, Goldman Sachs announced that it would require companies it helps take public to have at least one diverse board member, with a focus on women. Both Twitter and Facebook experienced social media shaming after going public without any women on their boards. More recently, the office-sharing company WeWork was in the news for announcing its plans to go public with an all-male board.³ In 2018, California also made headlines when it became the first state in the country to enact a landmark board diversity law, Senate Bill (SB) 826, which requires public corporations headquartered in the state to have a minimum number of female directors on their boards.⁴ Other states are already following

1. While there are many other forms of diversity that are relevant in this context, this Article focuses on gender diversity because board diversity efforts from investors and legislators have overwhelmingly focused on gender diversity. This Article does not address well-documented racial and ethnic diversity issues facing corporate America.

2. Institutional investors now own 70% of U.S. public companies, and they have become more vocal about what they want from boards. Institutional investors like State Street Global Advisors and Black Rock Inc. are putting pressure on companies with all-male boards to add women. In some cases, they are withholding votes for directors at companies that do not nominate a slate of diverse directors. *The Evolving Boardroom: Signs of Change: PWC's 2018 Annual Corporate Directors Survey*, PWC, <https://www.pwc.es/es/publicaciones/consejos-y-buen-gobierno/pwc-annual-corporate-directors-survey-2018.pdf>.

3. See Leslie Picker & Deirdre Bosa, *WeWork Doesn't Have a Single Woman Director, According to IPO Filing*, CNBC (Aug. 14, 2019), <https://www.cnbc.com/2019/08/14/wework-doesnt-have-a-single-woman-director-according-to-ipo-filing.html>. Following public outrage, WeWork announced plans to add one woman to its all-male, seven-member board. Joshua Franklin, *IPO Hopeful WeWork Adds Woman to Board, CEO Returns \$5.9 Million, After Backlash*, REUTERS (Sep. 4, 2019), <https://www.reuters.com/article/us-wework-ipo/wework-adds-woman-to-its-board-ahead-of-ipo-after-backlash-idUSKCN1VP1ES>.

4. SB 826 adds two sections to the California Corporations Code and only applies to publicly traded corporations in the state. It requires publicly traded domestic corporations and publicly traded corporations that have their principal executive offices in California, regardless of the state in which they are incorporated, have a minimum of one woman on their board of directors by the end of 2019. By the end of 2021, corporations with five directors must have at least two women directors, while corporations with six or more directors must have at least three women directors. S.B. 826, Reg. Sess. (Cal. 2018); Ca. Corp. Code § 301.3 (West 2018). According to the Harvard Law School Forum on Corporate Governance and Financial Regulation, shortly before the law was enacted, 79% of California companies did not meet the 2021 standards. See Howard Dicker, Lyuba Golster & Erika Kaneko, *Mandated Gender*

California's lead; Illinois, New Jersey, Massachusetts and Michigan are either considering or have passed similar legislation.⁵

In addition to states and investor groups, federal legislators, regulators, and national securities exchanges are also pushing board diversity initiatives. Several disclosure-based proposals are currently under consideration by the U.S. House Committee on Financial Services,⁶ and Representative Carolyn Maloney, Chair of the U.S. House Subcommittee on Investor Protection, Entrepreneurship, and Capital Markets, introduced the Diversity in Corporate Leadership Act of 2019.⁷ In February 2019, the U.S. Securities and Exchange Commission (SEC) released new Compliance and Disclosure Interpretations, requiring companies to explain how they factor diversity into

Diversity for California Boards, HARV. L. SCH. F. CORP. GOVERNANCE (Oct. 18, 2018), <https://corpgov.law.harvard.edu/2018/10/18/mandated-gender-diversity-for-california-boards/>.

5. In May 2019, the Illinois House passed a bill based on California SB 826 that would require all publicly held boards to have a woman, a Latino person, and an African American person on their boards by the end of 2020. See Kathy Gurchiek, *Report: Diversity on Boards Growing Slowly but Steadily*, SOC'Y FOR HUM. RESOURCE MGMT. (Jun. 13, 2019), <https://www.shrm.org/resourcesandtools/hr-topics/behavioral-competencies/global-and-cultural-effectiveness/pages/report-diversity-on-boards-growing-slowly-but-steadily.aspx>. The Illinois Senate subsequently revised the bill by removing the requirement for minority and female representation and instead replaced it with a diversity disclosure requirement. H.B. 3394, 101th Gen. Assemb., Reg. Sess. (Ill. 2019). In May 2019, Maryland signed legislation effective Oct. 1, 2019 that urges nonprofits and privately held and publicly traded corporations doing business in the state to have a minimum of 30% female directors on their Boards by the end of 2022. S.B. 911, 439th Gen. Assemb., Reg. Sess. (Md. 2019). A new bill was introduced in New Jersey at the beginning of 2019 that would require many public companies based in the state to have at least three women on the board by 2021. S. 3469, 218th Leg., Reg. Sess. (N.J. 2019). The Massachusetts bill would require that by the end of 2021, all publicly held corporations with principal executive offices in Massachusetts have at least one female director on their boards, and by the end of 2023, depending on the size of the board it must have two or three women. S. 1879, 191th Gen. Ct., Reg. Sess. (Mass. 2019). A bill introduced in the Michigan Senate would require publicly held corporations with their principal executive offices in Michigan to have a minimum number of female directors. S.B. 115, 100th Leg., Reg. Sess. (Mich. 2019).

6. See *Diversity in the Boardroom: Examining Proposals to Increase the Diversity of America's Boards: Hearing on H.R. 281, H.R. 1018, and H.R. 3279 Before the H. Comm. on Fin. Servs.*, 116th Cong. (2019). [hereinafter *Diversity in the Boardroom Hearing*]

7. See H.R. 3279, 116th Cong. (2019). The proposed legislation would, in part, require the U.S. Securities and Exchange Commission (SEC) to establish a Diversity Advisory Group to study and make recommendations on strategies to increase gender, racial, and ethnic diversity among the members of the board of directors of issuers of public securities.

nomination decisions and other company policies.⁸ In June 2019, the New York Stock Exchange (NYSE) announced the launch of the NYSE Board Advisory Council, which is tasked with connecting diverse candidates with companies seeking new directors.

The push for improved gender diversity in the boardroom is part of a broader, reinvigorated women's movement of the past several years. Women are driving a renewed movement for equality and leading a transformation in American civic life that challenges the patriarchal culture in the workplace and in leadership generally.⁹ In particular, the 2010s have birthed several powerful female-led movements that advocate for equal opportunities and a greater representation of women in leadership across industries and sectors.¹⁰ The cultural ripple effects of #MeToo-fueled

8. See SEC Advisory Comm. on Small & Emerging Companies, *Recommendation Regarding Disclosure of Board Diversity* (Feb. 16, 2017), <https://www.sec.gov/info/smallbus/acsec/acsec-recommendation-021617-corporate-board-diversity.pdf>.

9. Some historians and advocates have termed this evolution of the feminist movement as "Fourth-Wave Feminism." See Kira Cochrane, *The Fourth Wave of Feminism: Meet the Rebel Women*, THE GUARDIAN (Dec. 10, 2013), <https://www.theguardian.com/world/2013/dec/10/fourth-wave-feminism-rebel-women>.

10. In 2013, Sheryl Sandberg's book *Lean In* encouraged women to "lean in" to claim their place as C-suite business leaders. It became a best-seller and launched a movement for workplace equality. See SHERYL SANDBERG, *LEAN IN: WOMEN, WORK, AND THE WILL TO LEAD* (2013). In 2016, Hillary Clinton became the first female presidential nominee of a major U.S. political party and by doing so, carved a path for the record number of women running for the 2020 Democratic nomination. See Carrie Dann, *Hillary Clinton Becomes First Female Nominee of Major U.S. Political Party*, NBC NEWS (Jul. 26, 2016), <https://www.nbcnews.com/storyline/2016-conventions/hillary-clinton-becomes-first-female-nominee-major-u-s-political-n617406>. In 2017, millions of people stormed the streets following the inauguration of Donald J. Trump as part of The Women's March, the largest single-day protest in American history. See *Women's March*, HISTORY (Jan. 21, 2017), <https://www.history.com/this-day-in-history/womens-march>. The #MeToo movement went viral in late 2017 and sparked a national conversation about workplace sexual harassment. See Mary Pflum, *A Year Ago, Alyssa Milano Started a Conversation About #MeToo. These Women Replied*, NBC NEWS (Oct. 15, 2018), <https://www.nbcnews.com/news/us-news/year-ago-alyssa-milano-started-conversation-about-metoo-these-women-n920246>. At least two hundred prominent men lost their jobs following #MeToo allegations, and *Time* magazine named "The Silence Breakers" as the 2017 "Person of the Year." See Audrey Carlsen et al., *The Men Who Have Been Replaced*, N.Y. TIMES (Oct. 24, 2018), <https://www.nytimes.com/newsgraphics/2019/04/05/metoo/metoo-A14.pdf>; see also Stephanie Zacharek, Eliana Dockterman & Haley Sweetland Edwards, *The Silence Breakers*, TIME (2017), <https://time.com/time-person-of-the-year-2017-silence-breakers/>. In 2018, women ran for political office in unheard-of numbers and won a record number of seats in the U.S. Congress. See Heather Caygle, *Record-breaking*

uprisings and the record number of women winning in the midterm elections compelled many commentators to call 2018 another “Year of the Woman.”¹¹ Female empowerment movements are changing societal norms, shifting workplace power dynamics, and laying the groundwork for greater gender equity both inside and outside of the boardroom.

Board diversity initiatives and laws are being enacted at a time when men still outnumber women in the most prestigious leadership positions in corporate America.¹² Nationally, women only make up 22% of C-Suite

Number of Women Run for Office, POLITICO (Mar. 8, 2018), <https://www.politico.com/story/2018/03/08/women-rule-midterms-443267>. In 2019, the U.S. Women’s National Team won the Women’s World Cup soccer championship game, which gave rise to widespread public support for the team’s equal pay demand and for female athletes generally. See Anna North, *What’s Next for the US Women’s Soccer Team and Their Fight for Equal Pay*, VOX (Jul. 10, 2019), <https://www.vox.com/2019/7/10/20686692/us-womens-soccer-team-parade-equal-pay>.

11. The first “Year of the Woman” was in 1992 when twenty-eight women were elected to Congress, nearly doubling the number of women in the House of Representatives. See *The Year of the Woman, 1992*, US HOUSE OF REPRESENTATIVES: HIST., ART & ARCHIVES (last visited May 22, 2020), <https://history.house.gov/Exhibitions-and-Publications/WIC/Historical-Essays/Assembling-Amplifying-Ascending/Women-Decade/>; see also Adam Clymer, *The 1992 Elections: Congress – The New Congress; Democrats Promise Quick Action on a Clinton Plan*, N.Y. TIMES (Nov. 5, 1992). Many commentators cite Anita Hill’s 1991 appearance at the confirmation hearing of then-Supreme Court nominee Clarence Thomas as the triggering event. See Sarah Pruitt, *How Anita Hill’s Testimony Made America Cringe—And Change*, HISTORY (Apr. 2, 2019), <https://www.history.com/news/anita-hill-confirmation-hearings-impact>.

12. Note that the underrepresentation of women in leadership positions is not limited to the corporate sector. In the legal profession, women are 45% of associates but only 22.7% of partners and 19% of equity partners. In academia, women are only 32% of full professors and 30% of college presidents. Women represent only 24% of members of Congress. Women accounted for just 18% of all the directors, executive producers, producers, writers, cinematographers, and editors who worked on the top-grossing 250 domestic films of 2017. See Comm’n on Women in the Profession, AM. BAR ASS’N, *A Current Glance at Women in the Law* (2018), <https://www.americanbar.org/content/dam/aba/administrative/women/a-current-glance-at-women-in-the-law-jan-2018.authcheckdam.pdf>; Heather L. Johnson, Am. Council on Educ., *Pipelines, Pathways, and Institutional Leadership: An Update on the Status of Women in Higher Education 2017*, <https://www.acenet.edu/Documents/HES-Pipelines-Pathways-and-Institutional-Leadership-2017.pdf>; *Results: Women Candidates in the 2018 Elections*, RUTGERS CTR. FOR AM. WOMAN AND POL. (Nov. 29, 2018), http://cawp.rutgers.edu/sites/default/files/resources/results_release_5bletterhead5d_1.pdf; Martha M. Lauzen, *The Celluloid Ceiling: Behind-the-Scenes Employment of Women on the Top 100, 250, and 500 Films of 2017* (2018), https://womenintvfilm.sdsu.edu/wp-content/uploads/2018/01/2017_Celluloid_Ceiling_Report.pdf.

executives,¹³ and women account for about one-fifth of board directors in the country.¹⁴ In other words, a staggering 99% of boards are majority male. At the start of 2018, 585 companies in the Russell 3000 still had all-male boards,¹⁵ and only 28% of Russell 3000 companies have women holding at least one-fifth of their board seats.¹⁶ Board diversity is also a problem among newly public companies. Nearly 40% of recent IPO companies had no women on their boards at the time they went public.¹⁷ Representatives on both sides of the political aisle seem to agree that the underrepresentation of women in corporate America is a problem that needs to be addressed.¹⁸

The underrepresentation of women in these positions is not due to a lack of educational attainment. Today, women comprise more of the college-educated workforce and since the 1980s, have been earning a higher percentage of advanced degrees than men, but the leadership gender gap persists.¹⁹ In fact, men and women enter the workforce in roughly equal

13. Rachel Thomas et al., *Women in the Workplace 2018* at 5, McKinsey & Co. Company (2018), https://wiw-assets-production.s3.us-east-1.amazonaws.com/pdfs/women_in_the_workplace_2018_print.pdf.

14. Bonnie Marcus, *What Role Does Political Correctness Play In Corporate Board Diversity?*, FORBES (Oct. 29, 2018), <https://www.forbes.com/sites/bonnie-marcus/2018/10/29/what-role-does-political-correctness-play-in-corporate-board-diversity/#374f4d5a5556>.

15. Amit Batish, *Equilar Gender Diversity Index: Q1 2018*, EQUILAR (May 9, 2018), <https://www.equilar.com/reports/55-gender-diversity-index-q1-2018.html>. The Russell 3000 Index tracks the performance of 3,000 of the largest U.S.-traded stocks, which represent about 98% of all U.S. incorporated equity securities. James Chen, *Russell 3000 Index*, INVESTOPEDIA (Jun. 22, 2019), https://www.investopedia.com/terms/r/russell_3000.asp.

16. Inst. Shareholder Servs., Inc., *Gender Parity on Boards Around the World*, HARV. L. SCH. F. CORP. GOVERNANCE (Jan. 5, 2017), <https://corpgov.law.harvard.edu/2017/01/05/gender-parity-on-boards-around-the-world/>.

17. James Cheap, *Board Classification and Diversity in Recent IPOs*, HARV. L. SCH. F. CORP. GOVERNANCE (Apr. 24, 2018), <https://corpgov.law.harvard.edu/2018/04/24/board-classification-and-diversity-in-recent-ipos/>.

18. See, e.g., *Diversity in the Boardroom Hearing*, *supra* note 6 (statement of Rep. Patrick McHenry) (“Pursuing diverse boards is the right thing to do as a matter of economic interest.”); *id.* (statement of Rep. Maxine Waters) (“Strong diversity in the boardroom is critical to continued U. S. competitiveness and to ensuring that consumers of all backgrounds are served and not excluded”).

19. Women earn more than 57% of bachelor’s degrees, over 59% of master’s degrees, and 53% of doctorate degrees. *Degrees Conferred by Degree-Granting Institutions, by Level of Degree and Sex of Student: Selected Years, 1869-70 Through 2021-22*, NAT’L CTR. FOR EDUC. STAT. (June 2012), https://nces.ed.gov/programs/digest/d12/tables/dt12_310.asp?campaign_id=10&instance_id=10628&segment_id=14853&user_id=9057472ac769b04e9b634aa2632c5970®i_id=86995897. Women 25

numbers, but data shows that at the senior-management level, men outnumber women two to one.²⁰ Even in industries such as healthcare and retail, where women significantly outnumber men in the workforce, men still dominate the senior-level positions.²¹ Where men and women are equally qualified, the low percentage of women on boards and in senior-management positions represents an enormous loss of talent and educational investment.

The presence of women on America's corporate boards has undoubtedly increased over the last decade.²² While the traditional obstacles faced by women going up the corporate ladder have become surmountable for some women, the route to the boardroom still contains a variety of barriers for most women.²³ In fact, corporate governance experts predict that at the current rate of change, it could take nearly four decades before corporate boardrooms match the approximately half-female workforce.²⁴

years and older make up 50.2% of the college-educated work force. Richard Fry, *U.S. Women Near Milestone in the College-Educated Labor Force*, PEW RES. CTR. (June 20, 2019), <https://www.pewresearch.org/fact-tank/2019/06/20/u-s-women-near-milestone-in-the-college-educated-labor-force/>.

20. *Pyramid: Women in S&P 500 Companies*, CATALYST (May 1, 2019), <https://www.catalyst.org/research/women-in-sp-500-companies/>.

21. Michelle Stohlmeyer Russell et al., *Women Dominate Health Care – Just Not in the Executive Suite*, BOSTON CONSULTING GROUP (Jan. 7, 2019), <https://www.bcg.com/publications/2019/women-dominate-health-care-not-in-executive-suite>.

22. See HEIDRICK & STRUGGLES INT'L, INC., *Board Monitor US 2019* at 4 (2019), https://www.heidrick.com/-/media/Publications-and-Reports/Board_Monitor_US_2019.ashx (stating that in 2009, women filled 18% of new board seats, while in 2018, women filled 40% of new board seats); Lisa M. Fairfax, *Clogs in the Pipeline: The Mixed Data on Women Directors and Continued Barriers to Their Advancement*, 65 MD. L. REV. 579, 582 (2006) (stating that from 1994 to 2004, there was a 20% increase in companies in the Fortune 1000 reporting at least one woman on their board); Deb DeHaas et al., *Missing Pieces Report: The 2018 Board Diversity Census of Women and Minorities on Fortune 500 Boards*, HARV. L. SCH. F. CORP. GOVERNANCE (Feb. 5, 2019), <https://corpgov.law.harvard.edu/2019/02/05/missing-pieces-report-the-2018-board-diversity-census-of-women-and-minorities-on-fortune-500-boards/> (finding that women and minorities have made more progress in board representation for the *Fortune* 500 between 2016 and 2018 than between 2012 and 2016).

23. There are significant racial and ethnic differences in the rate of women's advancement. For example, there are just two women of color CEOs of Fortune 500 companies. Julia Carpenter, *Forget the 'Glass Ceiling.' Women of Color Face a 'Concrete Ceiling'*, CNN MONEY (Aug. 8, 2018), <https://money.cnn.com/2018/08/06/pf/women-of-color-ceos/index.html>. Women of color are only 4.7% of executive- or senior-level officials and managers in S&P 500 companies. Judith Warner et al., *The Women's Leadership Gap*, CTR. FOR AM. PROGRESS (Nov. 20, 2018), <https://cdn.americanprogress.org/content/uploads/2018/11/19121654/WomensLeadershipFactSheet.pdf>.

24. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-16-30, CORPORATE BOARDS:

Research clearly shows that laws mandating a minimum level of female board representation are effective at causing companies to add female directors to their boards at the rate required by those laws.²⁵ On the other hand, countries without board gender diversity mandates tend to have less gender-diverse boards than countries with such laws.²⁶ Recognizing the success of such mandates in many European countries,²⁷ California and other legislatures considering board diversity legislation seek to use the same approach to diversify America's corporate boardrooms. However, these so-called "gender quotas" face considerable criticism and legal challenges in the United States.²⁸

SB 826's quota mechanism faces a serious equal protection constitutional hurdle to its implementation in the United States.²⁹ The first of – what

STRATEGIES TO ADDRESS REPRESENTATION OF WOMEN INCLUDE FEDERAL DISCLOSURE REQUIREMENTS (2015); *Boards Will Reach Gender Parity in 2055 at Current Pace*, EQUILAR (Jan. 31, 2017), <https://www.equilar.com/blogs/212-boards-will-reach-gender-parity-in-2055.html>.

25. Following the passage of SB 826, the percentage of female directors per firm affected by the law rose by 3.4%. Green et. al. *Do Board Gender Quotas Affect Firm Value? Evidence from California Senate Bill No. 826* (2019). In countries that have an average of three women on large company boards, all but one country also have government-mandated quotas. See Jeff Green, *Women Get Board Seats Mostly When It's Required by Law*, BLOOMBERG (Dec. 11, 2018), <https://www.bloomberg.com/news/articles/2018-12-11/women-get-corporate-board-seats-mostly-when-it-s-required-by-law>. See also *infra* Part V.

26. A notable exception is Sweden, whose public companies average more than 30% female directors but do not operate under a quota system. See Zineb Raji, *Gender Diversity in Corporate Senior Management: Glass Ceiling Yet to be Cracked*, VIGEO EIRIS (Mar. 2018), <https://30percentclub.org/assets/uploads/UK/ThirdPartyResearch/Gender-diversity-in-senior-corporate-managment.pdf>.

27. The use of gender quotas for boards has been implemented in at least eighteen countries for certain companies: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, India, Ireland, Israel, Italy, Malaysia, Netherlands, Norway, Spain, Switzerland, and South Africa. Susan Franceschet & Jenifer M. Piscopo, *Equality, Democracy, and the Broadening and Deepening of Gender Quotas*, 9 POL. & GENDER 310, 311 (2013). See Vanessa Fuhrmans & Alejandro Lazo, *California Moves to Mandate Female Board Directors*, WALL ST. J. (Aug. 29, 2018), <https://www.wsj.com/articles/california-moves-to-mandate-female-board-directors-1535571904> (noting that the number of women on boards in Italy, Germany and several other European nations has tripled and, in some cases, quadrupled in recent years); *Gender Parity on Boards Around the World*, *supra* note 16 (finding that the mandate in Norway has resulted in an average of 42% of seats on Norwegian boards being held by women in 2016).

28. See Darren Rosenblum, *California Dreaming*, 99 B.U. L. REV. 1435, 1445-1447 (2019) (summarizing the critiques of California's quota).

29. See Joseph A. Grundfest, *Mandating Gender Diversity in the Corporate Boardroom: The Inevitable Failure of California's SB 826* 1 (Rock Ctr. for Corp.

commentators predict will be many – legal challenges to SB 826 have already been filed.³⁰ This Article does not analyze the merits of the equal protection concerns raised by other commentators, but it instead aims to address such concerns by putting forth a different strategic approach to instituting a gender diversity mandate.

This Article proposes taking gender diversity mandates out of the hands of state regulators and into the realm of the national securities exchanges. Specifically, this Article proposes the implementation of gender diversity listing standards by the major national securities exchanges that would require publicly traded companies to have a minimum number of women on their boards.³¹ Mandatory gender diversity measures via listing standards is

Governance at Stan. U. Working Paper Series No. 232, Sept. 12, 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3248791; Stephen M. Bainbridge, *California Corporate-Board Quota Law Unlikely to Survive a Constitutional Challenge*, WASH. LEGAL FOUND. (Oct. 2, 2018), <https://www.wlf.org/2018/10/02/wlf-legal-pulse/california-corporate-board-quota-law-unlikely-to-survive-a-constitutional-challenge/>; Kimberly D. Krawiec, *Board Diversity in the News Again*, Kimberlydkrawiec.org (Sept. 1, 2018), <http://kimberlydkrawiec.org/board-diversity-in-the-news-again>; *CalChamber Bill Positions*, CAL. CHAMBER OF COM., <http://ctweb.capitoltrack.com/public/search.aspx?t=bill&s=SB826&go=Search&session=17&id=1dae9efb-651d-4a02-a05d-360ca7965b14> (last visited Sept. 3, 2019). Some have also questioned the legality of SB 826 under the Commerce Clause. See Vikram David Amar & Jason Mazzone, *Part Three on California's Mandate That Women Be Placed on Corporate Boards: Dormant Commerce Clause and Improper Government Purpose Questions*, VERDICT (Nov. 1, 2018), <https://verdict.justia.com/2018/11/01/part-three-on-californias-mandate-that-women-be-placed-on-corporate-boards>.

30. Notably not a single corporation that was compelled to comply with SB 826 has filed suit. On August 6, 2019, the conservative government watchdog Judicial Watch filed a lawsuit in Los Angeles County Superior Court on behalf of three California taxpayers to block California from implementing SB 826, alleging that the gender-based quota is unconstitutional under the California Constitution. Complaint at 1-2, *Crest v. Padilla*, No. 19ST-CV-27561 (Cal. Super. Ct. Aug. 6, 2019). The second lawsuit was filed on November 13, 2019 by a shareholder of OSI Systems, Inc., a publicly traded company that is incorporated in Delaware and headquartered in California. Complaint at 1-2, *Meland v. Padilla*, No. 19-cv-02288 (E.D. Cal. Nov. 13, 2019). The court dismissed the complaint for lack of standing on April 20, 2020.

31. A listing standard is a requirement for listed securities established by a stock exchange in order to promote liquidity and transferability of shares by increasing investor confidence in both the markets and listed issuers. Listing standards are typically quantitative standards focused on indicators such as total number of stockholders, average monthly trading volume, aggregate market value, and annual revenue. See *Equity Rules Manual*, NASDAQ (2019), <https://listingcenter.nasdaq.com/rulebook/nasdaq/rules>; see also *Listed Company Manual*, NYSE (2019), <https://nyseguide.srorules.com/listed-company-manual/document?treeNodeId=csh-da-filter!WKUS-TAL-DOCS-PHC-%7B0588BF4A-D3B5-4B91-94EA->

the most effective and constitutionally feasible way to increase the number of women directors in this country. The proposed listing standards would be based on best practices guidelines, formulated with input from various stakeholders, and allow for differences among listed companies.

Part II of this Article describes how the governance of publicly traded companies is regulated, and specifically, the unique role securities exchanges play in regulating corporate governance matters. Listing standards adopted by exchanges impose a layer of regulation on public companies beyond state corporate law and federal securities law. The exchanges also offer certain benefits over state and federal regulation of public companies. The stock exchanges are capable of moving more quickly than state or federal regulators should the business environment change or if adjustments to the exchanges' listing standards are required. Listing standards also allow for flexibility and experimentation across a wide variety of corporate boards and avoid a one-size-fits-all approach to regulating public company boards. Finally, listing standards offer public companies predictability and consistency over a patchwork of state corporate laws.

Part II also discusses the important influence of norms on the development of corporate law. It details the new norms that are emerging around greater gender equity inside the boardroom as a result of the efforts of various investor groups and gender diversity advocacy groups. This Article's listing standard proposal aims to bring regulation of board governance in line with this new reality.

Part III of this Article examines the economic justification for gender diversity on corporate boards. Public companies have accumulated significant power and influence in our economy and society relative to other stakeholders. They are the largest drivers of wealth creation in our economy; they yield considerable influence over our country's elections; the location of their operations determines the vitality of our country's cities and towns; and they create products and technologies that have revolutionized our day-to-day lives. Good governance is central to healthy companies and in turn, a healthy economy and society. Diverse boards are more effective and perform better than homogenous boards. From an economic perspective, there simply is no business case for a homogenous board.³²

BE9F17057DF0%7D--WKUS_TAL_5667%23teid-0. Other listing standards focus on corporate governance matters such as the number of independent directors on a board and the mandate for an audit committee comprised of independent directors. Listing standards are subject to SEC authorization.

32. Multiple studies have shown that women provide different values and bring different professional experiences than men, which can enhance board decision-making and performance. They engage in better decision-making processes, provide better

Part IV explores two primary reasons why gender diversity efforts to date have not resulted in significantly more women on corporate boards. First, there is low turnover among corporate directors, and as a result, boards have few vacancies in any given year for new directors.³³ When a seat opens, companies prioritize prior board experience in the election of new directors and find candidates from within current board members' largely male-dominated networks.³⁴ Since women have historically been excluded from boardrooms in large numbers, the number of women who have prior board experience or are within the necessary networks is limited. Second, women continue to face structural barriers and discrimination in the workplace, hindering their ability to reach leadership positions. Gender stereotypes and implicit biases are hard to overcome through voluntary efforts. In fact, voluntary diversity measures and increased transparency efforts have proven to not be strong enough to considerably improve the gender diversity of corporate boards.

The issue of defining the most effective approach to improving gender diversity on corporate boards is squarely presented at this time given changing societal norms around gender equality in the workplace and in leadership positions. Part V of this Article analyzes the proposed gender diversity listing standard, addresses potential legal challenges it may face, and concludes that it is the most appropriate response to current governance needs articulated by various corporate stakeholders. A gender diversity listing standard would promote good governance among issuers and signal corporate responsibility and accountability to shareholders.

Ultimately, this Article's listing standard proposal aims to formalize the

oversight, and drive better corporate outcomes. *See, e.g.*, Catherine M. Daily & Dan R. Dalton, *Women in the Boardroom: A Business Imperative*, J. BUS. STRATEGY 8, 9 (2003); Sabina Nielsen & Morten Huse, *The Contribution of Women on Boards of Directors: Going Beyond the Surface*, 18 CORP. GOVERNANCE 136, 143 (2010); Amy J. Hillman et al., *Women and Racial Minorities in the Boardroom: How Do Directors Differ?*, 28 J. MGMT. 747, 758-59 (2002); Val Singh et al., *Newly Appointed Directors in the Boardroom: How Do Women and Men Differ?*, 26 EUR. MGMT. J. 48, 49, 59-7 (2008); Stephen Bear et al., *The Impact of Board Diversity and Gender Composition on Corporate Social Responsibility and Firm Reputation*, 97 J. BUS. ETHICS 207, 217 (2010).

33. *See* Anne Stych, *Low Turnover Slows Diversity on Corporate Boards*, BIZWOMEN (Apr. 29, 2019), <https://www.bizjournals.com/bizwomen/news/latest-news/2019/04/low-turnover-slows-diversity-on-corporate-boards.html?page=all>.

34. According to research from the Boardlist, a company that facilitates the placement of women on boards, 95% of board placements are the result of networking. *See* Marcus, *supra* note 14; Rosenblum, *supra* note 28, at 1449 (noting that the nominating committees of company boards are dominated by men, making it difficult for purely private action to generate structural transformation in corporate leadership).

country's changing norms around gender parity in leadership while avoiding the legal challenges faced by California's state-level gender diversity mandate (and other state legislation modeled after it). Further, the proposal would expedite the pace at which public companies increase board participation by women compared with efforts to date by Congress, the SEC, investor groups, trade associations, other stakeholders, and the exchanges themselves. In order to achieve gender parity in boardrooms across America, it must be mandated.

II. REGULATION OF CORPORATE GOVERNANCE

Corporate governance broadly describes the structure, processes, and procedures by which companies are directed and controlled.³⁵ Regulators and investors care about corporate governance because it impacts corporate performance, which in turn, affects the health of the economy.³⁶ Public companies in this country control billions of dollars, and they are capitalized in large part by the contributions of middle-class investors to retirement accounts, pension funds, college-savings plans, and mutual funds.³⁷ Corporations rely on their reputations with respect to corporate governance in part to induce investors to capitalize their enterprises.

In the United States, publicly traded corporations maintain a system of governance characterized by the separation of ownership and control. The three primary constituencies involved in corporate governance are shareholders, directors, and officers.³⁸ Under the prevailing view of

35. See The Fin. Aspects of Corp. Governance (Cadbury Comm.), *Report Comm. on the Fin. Aspects of Corp. Governance* 1, 16 (1992), <https://ecgi.global/sites/default/files/codes/documents/cadbury.pdf> (noting that the responsibility of a board includes determining a company's strategic aims, as well as the leadership to execute them, and supervising the management of the business and reporting to shareholders on their stewardship).

36. See Ellen Florian, *One Bright Spot in the WeWork Debacle: Turns out Investors Actually Care About Corporate Governance*, FORTUNE (Sept. 25, 2019) <https://fortune.com/2019/09/25/wework-adam-neumann-we-co-corporate-governance-investors/> (describing how the market has suffered due to poor decisions in governance).

37. A Federal Reserve Board study found that in 2016, 51.9% of families owned stocks, either directly or as part of a fund. The study also found that about one-third of families in the lower half of the income scale had stock holdings. In the next 40% of the income scale, about 70% of households held stocks, while households in the top 10% of the income scale had stock ownership rates above 90%. See Jesse Bricker et al., *Changes in U.S. Family Finances from 2013 to 2016: Evidence from the Survey of Consumer Finances*, 103 FED. RES. BULL. no. 3 (Sept. 2017), <https://www.federalreserve.gov/publications/2017-September-changes-in-us-family-finances-from-2013-to-2016.htm>.

38. Control blocks of stock owned by families, corporate groups, banks, and the government are more common in Europe and Asia.

corporate governance in the United States, a corporation should be governed for the benefit of shareholders.³⁹

Shareholders are owners of the corporation, but they do not have any right to manage the day-to-day business of the corporation. Shareholders rely on corporate governance mechanisms to bridge the gap between their ownership of and lack of control over large public companies. Shareholders holding stock with voting rights have the right to elect directors to the board.⁴⁰

The board of directors is the highest governing body within a corporation and serves both a monitoring role and a leadership role.⁴¹ As monitors, the board provides oversight over management and corporate activities. As leaders, the board acts on behalf of shareholders to make corporate policy decisions and advise on strategic and operational issues facing the corporation. Board directors have fiduciary duties to protect shareholders' assets and ensure that the corporation maximizes shareholder value.⁴² The

39. In other countries, especially those in Europe, other stakeholders such as workers, customers, suppliers, and communities are central to corporate governance norms. Note that the shareholder-centric norm in the United States may be starting to shift to a broader stakeholder group. One of the U.S.'s most powerful business lobbying groups, The Business Roundtable, released a statement in August 2019 signed by more than 180 chief executives of the largest American companies titled "Business Roundtable Redefines the Purpose of a Corporation to Promote an Economy that Serves All Americans." It is the first time in its nearly fifty-year history that the group has said shareholder value is not the first priority. *See Business Roundtable Redefines the Purpose of a Corporation to Promote "An Economy That Serves All Americans"*, BUS. ROUNDTABLE (Aug. 19, 2019), <https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans> (stating that the CEOs commit to lead their companies for the benefit of all stakeholders – customers, employees, suppliers, communities and shareholders).

40. Typically, the nominating committee of the board of directors recommends the election of a director for each open board seat. Both the NYSE and NASDAQ require that the nominating committee be comprised of independent directors. The nominated directors are listed on a proxy statement that is sent to each shareholder. At the annual shareholder meeting, shareholders may either vote for the nominated director or abstain from voting. Alternately, shareholders may nominate their own candidates to the board via a process known as a proxy contest. Shareholders are responsible for preparing and distributing their own proxy materials. *See Equity Rules Manual*, *supra* note 31; *Listed Company Manual*, *supra* note 31.

41. State corporation codes generally provide that a corporation's business and affairs be managed by or under the direction of a board of directors. *See, e.g.*, DEL. CODE. ANN. tit. 8, § 141(a) (2019); MODEL BUS. CORP. ACT § 8.01(b) (AM. BAR ASS'N 2016) (stating that "all corporate powers shall be exercised by or under the authority of the board of directors, and the business and affairs of the corporation shall be managed by or under the direction, and subject to the oversight, of the board of directors.").

42. The purpose or goal of the corporate form is almost universally conceived as profit maximization. *But see* Lynn A. Stout, *Lecture and Commentary on the Social*

board also appoints the chief executive officer, who, together with other officers, runs the daily operations of the corporation. When people think about who leads a company, they typically focus on the chief executive officer (CEO), but the CEO serves at the pleasure of the board and is an agent of the corporation whose duties are defined by the board. Accordingly, the board plays a critical role in the leadership of the corporation.

The governance of a public company is guided by a complex framework of legal and non-legal factors⁴³ that determine how decisions are made, how power is exercised, and the extent to which interests of various corporate stakeholders are considered. State corporate law, federal securities law, listing standards, and norms are the major pieces of the corporate governance framework for public companies.

State corporate law is the primary source of corporate governance rules and supplies the basic scaffolding for decision-making that occurs within a corporation. State corporate codes, the common law, and the governance documents of each company provide for the allocation of corporate power among the three groups of internal constituents described above: shareholders, directors, and officers.⁴⁴ Because corporations are generally free to incorporate in any state without limiting their ability to do business in other states, corporations ultimately choose what state corporate law will govern their internal affairs.⁴⁵ State corporate law does not focus upon the

Responsibility of Corporate Entities: Bad and Not-So-Bad Arguments for Shareholder Primacy, 75 S. CAL. L. REV. 1189, 1195-99 (2002) (noting that the obligation to maximize shareholder value is the subject of considerable debate among corporate scholars).

43. See Robert B. Thompson, *Collaborative Corporate Governance: Listing Standards, State Law, and Federal Regulation*, 38 WAKE FOREST L. REV. 961, 966 (2003) (listing the many non-legal factors that influence corporate governance: the various markets, including the market for shares, the products market, the market for executives, and the market for corporate control; private ordering such as incentive contracts for various participants or monitoring, including that provided by directors and independent accountants; and norms, including the collective impact of business culture and groups that promote best corporate practices).

44. Delaware places all corporate power in the board of directors. See DEL. CODE ANN. tit. 8 § 141(a) (stating that all corporate power should be exercised by or under the direction of the board of directors).

45. The internal affairs doctrine asserts that only the state in which a corporation is incorporated, as opposed to the state in which a corporation primarily operates or holds its assets, should have the authority to regulate a corporation's internal affairs. Delaware is the most popular state for corporate charters largely based on reliance on the internal affairs doctrine and the perceived desirability of its corporate governance laws. Corporate scholars have questioned the legality of SB 826 under the internal affairs doctrine and argue that SB 826 is invalid as applied to corporations not incorporated in

public market for securities and its related needs, interests, and issues.

Federal securities laws provide a separate layer of corporate governance regulation over public companies and regulate the issuance of securities.⁴⁶ The SEC was created in the aftermath of the Great Crash of 1929 and during the ensuing Great Depression, as a way to restore public confidence in the capital markets and thereby promote economic recovery. The SEC is also the federal agency that has oversight authority over stock exchanges.⁴⁷ The primary sources of federal securities laws include the Securities Act of 1933, the Securities Exchange Act of 1934 (Exchange Act), and regulations promulgated by the SEC under those acts. The Sarbanes-Oxley Act of 2002 and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 also impose a variety of substantive corporate governance requirements.

Because this Article's proposal primarily concerns the other two legs of the corporate governance framework—listing standards and norms—they are discussed in turn below.

A. U.S. Exchange-Established Listing Standards

Even before there were federal securities laws, stock exchanges regulated the corporate governance of public companies.⁴⁸ Stock exchanges operate

California under the internal affairs doctrine. *See, e.g.,* Grundfest, *supra* note 29, at 1-4.

46. Note that state statutes known as “blue sky laws” also regulate securities. The blue sky laws vary from state to state, but each state’s blue sky laws contain a registration requirement for securities that will be sold in that state. The National Securities Markets Improvement Act of 1996 preempts state regulation of securities registration and offering process for securities listed on NYSE or NASDAQ. *See* National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, § 18(a)(1B) 110 Stat. 3416.

47. The SEC is primarily responsible for administering six major securities laws: Securities Act of 1933, 15 U.S.C.A. §§ 77a-77aa (2019); Securities Exchange Act of 1934, 15 U.S.C.A. §§ 78a-78qq (2019); Trust Indenture Act of 1939, 15 U.S.C.A. §§ 77aaa-77bbbb (2019); Investment Company Act of 1940, 15 U.S.C.A. §§ 80a-1 to -64 (2019); Investment Advisers Act of 1940, 15 U.S.C.A. §§ 80b-1 to -18 (2019); and Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002) (codified as amended at 15 U.S.C.A. §§ 7201-65 and in scattered sections of 18 U.S.C.A. (2019)). Through the Securities Act of 1933 and the Exchange Act of 1934, the SEC has primary responsibility for implementing the disclosure obligations of listed companies in the SEC. *See* SEC What We Do (June. 10, 2013), <https://www.sec.gov/Article/whatwedo.html>.

48. *See, e.g.,* NYSE: CORPORATE GOVERNANCE GUIDE (Steven A. Rosenblum et al. eds. 2014), https://www.nyse.com/publicdocs/nyse/listing/NYSE_Corporate_Governance_Guide.pdf (describing how in 1895, the NYSE recommended that listed companies issue a full report of their annual operations at least fifteen days before the shareholder meeting. In 1899, it began requiring regular financial statements of all listed companies.

as markets for the purchase and sale of an issuer's shares and serve as regulators of the markets they create.⁴⁹ The two predominant and most prestigious U.S. financial securities markets are the NYSE and the National Association of Securities Dealers Automated Quotation System (NASDAQ). The NYSE is the oldest and largest stock exchange in the world by market capitalization.⁵⁰ Over 3,100 companies are traded on the NYSE, including some of America's largest companies such as Target, Disney, Coca-Cola, and McDonald's. NASDAQ is the second-largest stock exchange⁵¹ in the world by market capitalization, with over 3,500 companies listed on the exchange. In addition to a variety of consumer goods companies and health care companies, many of America's largest technology companies, such as Apple, Facebook, Microsoft, and Amazon are traded on NASDAQ. Together, NYSE and NASDAQ account for the majority of the securities listed for trading on U.S. stock exchanges and thus hold considerable power over the governance standards of public companies in this country.

Because the operation of successful securities markets depends on the integrity of the listed companies and the equitable treatment of shareholders, each of the security exchanges establishes a set of contractual rules or "listing standards" that regulate the issuers of securities traded on those exchanges and the securities that are listed for trading.⁵² Listing standards are designed

It urged listed companies to have at least two outside directors on their boards starting in 1956. In 1977, NYSE required that listed companies have independent audit committees comprised of outside directors.) Over the last decade, the exchanges have worked jointly to issue new corporate governance standards.

49. Stock exchanges are commonly referred to as self-regulatory organizations (SROs). All securities transactions that do not take place on the stock exchange occur in the over-the-counter (OTC) market. The exchanges offer listed securities greater liquidity and prestige than the OTC market. *See* Special Study Grp. of the Comm. on Fed. Regulation of Sec., *Special Study on Market Structure, Listing Standards and Corporate Governance*, 57 BUS. LAW. 1487, 1491, 1502, 1531 (2002).

50. The NYSE began as a member-owned SRO, but it demutualized in 2006. Demutualization is the process by which a stock exchange converts from a nonprofit, member-owned entity into a for-profit corporation owned by shareholders. The sources of revenue for a stock exchange include listing fees, trading transaction fees, and sale of information services and market data. *See* Andreas M. Fleckner, *Stock Exchanges at Crossroads*, 74 FORDHAM L. REV. 2550, 2554 (2006).

51. NASDAQ initially operated as a quotation service and was a wholly owned for-profit subsidiary of the nonprofit National Association of Securities Dealers, Inc. It spun off in 2000 and converted into a shareholder-owned market. It began issuing public stock in 2002.

52. Under the Exchange Act, stock exchanges are required to self-regulate by establishing rules that regulate listed companies, brokers, dealers, and other market participants. Note that the SEC is also authorized to impose listing standards, but the

to promote share liquidity and market stability by increasing investor confidence in both the exchange market and the companies that are listed.⁵³ Exchanges have strong incentives to adopt listing standards that benefit investors because their incomes rise when more investors purchase securities listed on their exchanges. Companies that are seeking access to the public markets are incentivized to list with an exchange that attracts the most investors.⁵⁴ Some of the listing standards are prerequisites to listing a security on the exchange and others are rules applicable after an issuer's shares are already listed. An exchange may remove or de-list the company's stock from the exchange if the company fails to meet the exchange's listing standards.⁵⁵

The listing standards vary by exchange, but they are generally categorized as (i) quantitative standards such as minimum numerical thresholds for market capitalization, revenue, and number of shares, and (ii) internal structure standards such as the requirement for an audit committee comprised of independent directors. The latter requirements are considered corporate governance listing standards, and they effectively mandate that listed companies meet a baseline level of "corporate responsibility, integrity and accountability to shareholders."⁵⁶ Corporate governance listing standards reflect the exchanges' conception of good governance practices and serve as quality indicators to investors.⁵⁷ By assuring investors that its issuers are

scope of SEC authority to directly impose listing standards is limited to matters in furtherance of the Exchange Act. *See* *Bus. Roundtable v. SEC*, 905 F.2d 406, 414 (D.C. Cir. 1990). Some commentators have argued that listing standards are not designed to protect shareholders and markets but instead function as marketing campaigns by the exchanges. *See* Douglas C. Michael, *The Untenable Status of Corporate Governance Listing Standards under the Securities Exchange Act*, 47 *BUS. LAW.* 1461, 1462 (1992).

53. *See* Fleckner, *supra* note 50 at 2546 (providing liquidity is one of the critical functions of a stock exchange).

54. *See* Paul G. Mahoney, *The Exchange as Regulator*, 83 *VA. L. REV.* 1453, 1457-1458 (1997) (stating "[a]s a provider of liquidity, an exchange competes with other exchanges and over-the-counter markets, both to attract companies to list and to induce investors to purchase listed securities").

55. *See Special Study on Market Structure, Listing Standards and Corporate Governance*, *supra* note 49, at 1516 (noting that delisting for noncompliance is rare, so exchanges tend to encourage compliance through negotiation with listed companies or by imposing sanctions, including fines).

56. *See Listed Company Manual*, *supra* note 31.

57. Some commentators have argued that in the competitive market for listings, exchanges have considerable incentives to under-regulate issuers to attract more firms. Regulation imposes costs on companies, and if the costs are high enough, companies may choose to list on another exchange. *See, e.g.,* Jonathan R. Macey & Maureen O'Hara, *From Markets to Venues: Securities Regulation in an Evolving World*, 58 *STAN.*

practicing proper governance, exchanges are, in a way, mitigating the financial risk to investors purchasing shares on their exchanges and making the exchanges more attractive to investors.

Although listing standards are enforced through a private contract between a listed company and an exchange, the process of developing a listing standard involves a public discussion. Corporate governance listing standards are considered “rules” for purposes of the Exchange Act. Accordingly, they must be adopted pursuant to Section 19 of the Exchange Act and are subject to SEC approval.⁵⁸ In particular, Section 19(b) outlines the process by which an exchange can propose a new listing standard. First, the exchange must file a copy of the proposed listing standard with the SEC for publication.⁵⁹ The SEC will then solicit comments from the public on the proposed listing standard. Following the comment period, the SEC must approve the proposed listing standard if it finds that the proposed listing standard is “consistent with the requirements of” the Exchange Act.⁶⁰ On the other hand, the SEC must disapprove a proposed listing standard if it is unable to find that such standard is consistent with the Exchange Act.⁶¹

The “consistency” standard provides exchanges with substantial autonomy to adopt corporate governance listing standards.⁶² *Business Roundtable v. SEC*⁶³ is the sole judicial interpretation of SEC authority over corporate governance listing standards.⁶⁴ The court reviewed a voting rights

L. REV. 563, 580 (2005).

58. Section 19 of the Securities Exchange Act of 1934, as amended (Exchange Act) describes the process for the adoption of exchange listing standards. Section 19(b) outlines the process by which exchanges can propose new rules or amend existing rules, and Section 19(c) provides the SEC with certain direct authority to unilaterally amend, delete, or add to the listing standards of an exchange. *See* Securities Exchange Act of 1934, 15 U.S.C.A. § 19 (2019) [hereinafter Exchange Act].

59. *See id.* at § 19(c)(1).

60. *See id.* at § 78s(b)(2) (emphasis added).

61. *See id.*

62. Nothing in the Exchange Act prohibits an exchange from regulating corporate governance through its listing standards, nor does the Exchange Act contemplate the SEC performing a merit review of the proposed listing standards. *See* Stephen M. Bainbridge, *Revisiting the One Share/One Vote Controversy: The Exchange’s Uniform Voting Rights Policy*, 22 SEC. REG. L.J. 175, 183 (1994) (concluding that “the SEC effectively must rubberstamp” listing standard proposals).

63. 905 F.2d. 406 (D.C. Cir. 1990).

64. The issue in *Business Roundtable* was whether the SEC had exceeded its jurisdiction when it promulgated a regulation impacting the rules of SROs under Exchange Act Rule 19(c)-4. *See id.* at 409. While the Article’s proposal is focused on an exchange-established rule under Exchange Act Rule 19(b), court dicta on the scope of SEC authority over invalidating listing standards promulgated by an exchange is

standard promulgated by the SEC and invalidated it because it was not consistent with the purposes of the Exchange Act. In the opinion, the court specifically found the scope of SEC authority to be “quite limited” with respect to disapproving proposed listing standards related to corporate governance matters.⁶⁵ The consistency standard has been interpreted to mean the requirement that proposed corporate governance listing standards not be “designed to permit unfair discrimination” among issuers.⁶⁶ In other words, the SEC must approve proposed corporate governance listing standards as long as it is satisfied that any differences in the application of the listing standards are based on meaningful distinctions between issuers and are not unfairly discriminatory.

Exchange-established corporate governance listing standards have long served as an alternative to government regulation of public companies⁶⁷ and

relevant.

65. See Special Study Grp. of the Comm. on Fed. Regulation of Sec., *Special Study on Market Structure, Listing Standards and Corporate Governance*, 57 BUS. LAW. 1487, 1524 (2002) (citing *Bus. Roundtable*, 905 F.2d. at 414). The report also noted that the SEC’s authority to approve a governance standard is limited, but the limitations are not defined. See *id.* at 1554. See generally *Silver v. New York Stock Exch.*, 373 U.S. 341, 351 (1963) (commenting that Congress did not intend for The Exchange Act to displace “the exchanges’ traditional process of self-regulation. The intention was rather, . . . one of ‘letting the exchanges take the leadership with Government playing a residual role. Government would keep the shotgun, so to speak, behind the door, loaded, well-oiled, cleaned, ready for use but with the hope it would never have to be used’”).

66. Note that consistency standard has not been judicially interpreted with respect to corporate governance listing standards, but a Task Force for the American Bar Association found the nondiscrimination standard to be the only restriction on an exchange’s authority to adopt corporate governance listing standards under the consistency standard. See *Special Study on Market Structure Listing Standards and Corporate Governance*, *supra* note 65 at 1520 n.160 (stating that “[([S]tructure and content of listing agreements between exchanges and issuers are, except for questions of ‘unfair discrimination’ among issuers, outside the scope of the [SEC’s] oversight and regulatory jurisdiction” (citing Comment Letter from the ABA Section of Corporation, Banking and Business Law, Federal Regulation of Securities Committee, Task Force on New York Stock Exchange Listing Requirements, to Jonathan G. Katz, Secretary, SEC, at 4 (Dec. 31, 1986)))). The report also described how courts have interpreted the consistency standard and how the standard applies to corporate governance listing standards. Sections 6(b)(5) and 15(b)(6) generally require that rules of an exchange be designed “to prevent fraudulent and manipulative acts and practices” and “to protect investors and the public interest.” See Securities Exchange Act of 1934, 15 U.S.C.A. § 78f(b)(5) (2019); see also *Special Study on Market Structure, Listing Standards and Corporate Governance*, *supra* note 65 at 1518-1520, n.158.

67. The efficacy and appropriateness of the exchange-method of regulation is a source of great debate among scholars. See Paul G. Mahoney, *The Exchange as Regulator*, 83 VA. L. REV. 1453, 1455 (1997); Douglas C. Michael, *Untenable Status of*

in the context of this Article's proposal, are preferable to direct federal or state regulation of corporate governance in the following ways.

Jurisdiction—While exchanges are subject to SEC oversight, they are ultimately private entities. As private entities, exchanges are able to develop rules in areas where government entities lack jurisdiction as long as they comply with applicable securities laws. For example, the SEC cannot directly regulate the corporate governance of listed companies,⁶⁸ but the exchanges can mandate compliance with its rules.⁶⁹ Most relevant to this Article's proposal, the exchanges are also able to regulate in areas where state entities may face constitutional restrictions.⁷⁰

Coordination—American corporate law is comprised of the statutes and judicial decisions of fifty-one separate jurisdictions. States have not voluntarily coalesced around a single approach to matters concerning the internal affairs of a corporation.⁷¹ Publicly traded companies typically

Corporate Governance Listing Standards under the Securities Exchange Act, 47 BUS. LAW. 1461, 1462 (1992); A.C. Pritchard, *Markets as Monitors: A Proposal to Replace Class Actions with Exchanges as Securities Fraud Enforcers*, 85 VA. L. REV. 925, 964-65 (1999); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359, 2399-401 (1998).

68. See *Bus. Roundtable*, 905 F.2d at 412 (finding that corporate governance regulation is beyond the purview of the Exchange Act). But see Jeffrey Y. Wu, *Revisiting Business Roundtable and Section 19(c) in The Wake of the Sarbanes-Oxley Act*, 23 YALE J. ON REG. 249, 250 (2006) (arguing that Sarbanes-Oxley has implicitly expanded the SEC's rulemaking authority under Section 19(c) of the Exchange Act).

69. See Kerry Shannon Burke, *Regulating Corporate Governance through the Market: Comparing the Approaches of the United States, Canada and the United Kingdom*, 27 J. CORP. L. 341, 360 (2002) (stating that "The NYSE closes this gap in the federal law by mandating compliance with its corporate governance standards."). See also *Special Study on Market Structure, Listing Standards and Corporate Governance*, *supra* note 65, at 1490 (stating that "Corporate governance listing standards fill, at least in part, the sizeable gap between state corporate law and the federal securities laws").

70. See *infra* Part V.A.

71. See Jill E. Fisch & Steven Davidoff Solomon, *Centros, California's "Women on Boards" Statute and the Scope of Regulatory Competition*, EUR. BUS. ORG. L. REV. 8 n. 51 (forthcoming 2019), https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=3077&context=faculty_scholarship. Note that California and Delaware hold differing views on the scope of the internal affairs doctrine. Notably, the U.S. Supreme Court has never found that the internal affairs doctrine is constitutionally mandated. See ERIN A. O'HARA & LARRY E. RIBSTEIN, *THE LAW MARKET* (Oxford Univ. Press, 2009) (asserting that the doctrine does not have "special constitutional status"); Jeb Rubenfeld, *State Takeover Legislation and the Commerce Clause: The "Foreign" Corporations Problem*, 36 CLEV. ST. L. REV. 355, 357 (1988) (analyzing and rejecting arguments that the internal affairs doctrine is compelled by the Commerce Clause); Faith Stevelman, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law*, 34 DEL. J.

operate in multiple states, engage in substantial interstate commerce, and have geographically dispersed shareholders. As a result, the laws applicable in one state may affect the corporation's activities in other states.⁷² Listing standards satisfy the need to coordinate applicable governing law to facilitate interstate markets and provide clear guidance to corporations where state law diverges or does not address a governance matter applicable to listed companies.⁷³ In the context of the Article's proposal, without a single mandate, publicly traded corporations might be forced to comply with the board diversity laws of all potentially relevant states, which can increase the cost of conducting interstate commerce and effectively limit new entrants into the market.⁷⁴

Flexibility—Compared with state or federal regulation, listing standards are more flexible, allow for more experimentation, and avoid a one-size-fits-all approach to regulating corporate governance. Corporations do not have uniform needs or abilities with respect to implementing corporate governance standards. Through listing standards, exchanges may establish special rules, exempt smaller companies, or offer a phased-in approach as needed.

Speed—The exchanges can implement regulations more quickly than state or federal regulators. Demutualized, or for-profit, exchanges are run as

CORP. L. 57, 75 (2009) (stating that “[u]nder modern law the [internal affairs doctrine] is best understood merely as a choice of law regime”).

72. Examples where one state's laws impact corporate activity in other states include state anti-takeover statutes, state “corporate outreach” statutes, and the internal affairs doctrine.

73. Even if federal legislation did not explicitly preempt state law in this area, corporations would adapt in the way they have done with respect to director independence standards. The standards under Sarbanes-Oxley, NASDAQ, and NYSE to determine whether a director is independent differ from Delaware law, and it is possible for a director to be independent under one standard and not under Delaware law. While these director independence rules regulate a corporation's internal affairs and could conflict with the state of incorporation's law on the same issue, the corporations to which these requirements apply have responded by changing their structure to reflect these rules. See Fisch & Solomon, *supra* note 71, at 14 n.90. This response has positive implications for a corporation's ability to comply with a gender diversity listing standard in the face of state gender diversity mandates. Unlike the director independence rules, there is no conflicting standard under Delaware law with which publicly traded corporations based in California would have to contend.

74. Scholars refer to this issue as a regulatory spillover problem. See Erin O'Hara O'Connor & Larry E. Ribstein, *Preemption and Choice-of-Law Coordination*, 111 MICH. L. REV. 647, 660 (2013) (explaining the “spillover” problem and its costs). Note that the enforceability of the internal affairs doctrine in this context has been the subject of recent debate.

businesses and can make decisions quickly through their board of directors and officers. While the implementation of new listing standards is subject to SEC approval, the comment period prior to approval is relatively short.⁷⁵

Expertise—The exchanges have the industry experience and proximity to market actors necessary to proactively anticipate challenges and potential impacts of corporate governance regulation on the marketplace. Their expertise in this area is an asset to designing and implementing corporate governance rules that are effective and tailored to market participants.⁷⁶

B. Norms

Norms such as prevailing industry and community standards play an important role in shaping corporate governance practices and influencing how business are run.⁷⁷ Norms are a reflection of the views held by most people and often serve as the basis for formalizing those views into law and regulation.⁷⁸ Professor Melvin A. Eisenberg explained the influence of

75. All rule proposals are subject to a thirty-five day comment period prior to approval though the SEC has the ability to extend the comment period to ninety days. At the end of the comment period, the SEC must either approve the proposed rule or initiate proceedings to evaluate whether the rule should be disapproved. *See* Securities Exchange Act of 1934, 15 U.S.C.A. § 78s (2019).

76. *See* Kerry Shannon Burke, *Regulating Corporate Governance through the Market: Comparing the Approaches of the United States, Canada and the United Kingdom*, 27 J. CORP. L. 341, 349 (2002) (stating that “Many governmental regulators are experts in shaping regulatory policy, but may lack the industry experience necessary to appreciate the true impact of a new law on the marketplace.”).

77. *See* Melvin A. Eisenberg, *Corporate Law and Social Norms*, 99 COLUM. L. REV. 1253, 1269 (1999) (stating that “while social norms differ from legal rules, there is often a symbiotic relationship between legal rules and social norms . . . legal rules are often based on social norms . . . adoption of a legal rule that is based on a social norm sends a message that the community regards the norm as especially important”); Inst. Shareholder Servs. Inc., *Gender Parity on Boards Around the World*, HARV. L. SCH. F. CORP. GOVERNANCE (Jan. 5, 2017), <https://corpgov.law.harvard.edu/2017/01/05/gender-parity-on-boards-around-the-world/> (discussing how social norms in various markets often drive the regulatory framework, and how that regulatory framework is fulfilled). Examples of corporate norms shaping corporate governance practices include reports from The Business Roundtable, The Conference Board, and ABA Task Force. *See, e.g.*, Business Roundtable, *Principles of Corporate Governance*, <https://www.businessroundtable.org/policy-perspectives/corporate-governance/principles-of-corporate-governance> (last visited Mar. 31, 2020); Conference Board Commission on Public Trust and Private Enterprise, *Findings and Recommendations*, https://www.conference-board.org/pdf_free/SR-03-04.pdf (last visited Feb. 8, 2020).

78. JONATHAN R. MACEY, *CORPORATE GOVERNANCE: PROMISES KEPT, PROMISES BROKEN* 33 (2008) (“Norms are important because they are often the source of actual legal rules”). *See* Eisenberg, *supra* note 77 at 1265 (noting that some corporate law

norms on corporate law especially well:

“Adoption of a legal rule that is based on a social norm sends a message that the community regards the norm as especially important. This message increases both the likelihood that the norm will be internalized and the reputational penalties for violating the norm. Furthermore, legal rules add, to the force of a specific obligational norm, the force of the general norm of obedience to law, which is one of the most powerful norms of our society. Legal rules may also serve to clarify social norms by providing focal points for their meaning.”⁷⁹

The sources of new norms are primarily found outside of the courts;⁸⁰ in many cases, new norms are a result of campaigns of civil society groups that work to change public opinion and practice.⁸¹ As Professor David Cole outlines in his book *Engines of Liberty*, the public acceptance of marriage equality was incubated by activists long before the Supreme Court declared it a constitutional right, as was the recognition of the individual right to bear arms and the human rights of foreign prisoners of war in the war on terror.⁸² A similar process is now occurring with respect to women’s fight for equality in the workplace.⁸³

doctrines explicitly incorporate social norms such as ALI’s Principles of Corporate Governance); Burke, *supra* note 76 at 371-73 (comparing the differing cultural factors between the U.S., Canada, and U.K. and how such factors result in various approaches toward regulated entities in each country); DUNCAN GREEN, *HOW CHANGE HAPPENS* 49 (2016) (noting that norms set “standards that national movements can use to rally for change in legislation and in public attitudes on everything from whether bribery is acceptable or parents have the right to beat their children, to discrimination against migrant workers . . .”).

79. See Eisenberg, *supra* note 77 at 1269-70.

80. See Eisenberg, *supra* note 77 at 1264 (“social norms may shift when, and because, enough actors change their behavior that a tipping-point is crossed”); Green, *supra* note 78 at 52 (“‘Critical junctures’, such as wars or political and economic crises, can help shift norms, when an upheaval in traditional routines opens the door to new thinking. In the US, the experience of blacks and whites fighting alongside each other in the Second World War helped galvanize the civil rights movement. Increased attention to inequality in recent years suggests that the 2008 financial crisis may have changed attitudes.”).

81. See DAVID COLE, *ENGINES OF LIBERTY: THE POWER OF CITIZEN ACTIVISTS TO MAKE CONSTITUTIONAL LAW* 9 (2016) (“Look behind any significant judicial development of constitutional law, and you will nearly always find sustained advocacy by multiple groups of citizens, usually over many years and in a wide array of venues.”).

82. See *id.* at 81 (examining the role civil society groups such as Freedom to Marry, the National Rifle Association, and the Center for Constitutional Rights have played in transforming public opinion on these issues from provoking outrage to being broadly accepted rights).

83. See David A. Katz et al., *Corporate Governance Update: Shareholder Activism*

Throughout history, women's movements have translated mass collective action into political, social, and economic change. Most recently, the 2017 Women's March, the largest single-day demonstration in U.S. history, heralded a new wave of women's activism that has been sustained by the #MeToo movement and the political organizing that resulted in historic wins for women in the 2018 mid-term elections. Galvanized women are recognizing their power to change norms.

The normative expectations of women's roles in corporate America have undergone extraordinary change over the last century, largely thanks to women's movements and the work of civil society groups. Today, several grassroots campaigns and advocacy organizations are helping shift norms inside corporate boardrooms from male-dominated to gender-diverse. For instance, 2020 Women on Boards is a national campaign to increase the percentage of women on U.S. company boards to at least 20% by the year 2020,⁸⁴ and the Thirty Percent Coalition is a national organization that is committed to the goal of women holding 30% of board seats across public companies.⁸⁵ Another private sector initiative, Every Other One, is backed by the Committee for Economic Development and aims to increase gender diversity on U.S. boards by getting companies to appoint a woman to every other vacant board seat.⁸⁶

The effectiveness of these groups' efforts is evidenced by the broader and growing support of gender diverse boards among the country's largest investors.⁸⁷ In 2017, State Street Corporation issued proxy voting guidelines

Is the Next Phase of #MeToo, Harv. L. Sch. F. on Corp. Governance and Fin. Reg., (Sept. 28, 2018), <https://corpgov.law.harvard.edu/2018/09/28/corporate-governance-update-shareholder-activism-is-the-next-phase-of-metoo/> (explaining that "[a]s the #MeToo movement continues to make itself felt in all facets of American life . . . many boards have overseen the addition of anti-harassment policies to corporate codes of conduct, the establishment of procedures for addressing allegations, and the enhancement of employee training at all levels. Directors are taking proactive steps toward educating themselves and looking deeply into issues involved, and many have highlighted it as a priority for the senior management team. Boards that have successfully installed . . . good governance in this area can now . . . consider the larger project of gender equality in corporate America, in which sexual harassment, corporate culture, gender pay equity, and gender diversity are related issues.").

84. See 2020 WOMEN ON BOARDS, <https://2020wob.com/about/> (last visited Sept. 4, 2019).

85. See THIRTY PERCENT COALITION, *Who We Are*, <https://www.30percentcoalition.org/who-we-are> (last visited Sept. 4, 2019).

86. See Comm. for Econ. Dev., *CED Unveils "Every Other One" Initiative*, PR NEWswire (Nov. 13, 2014), <https://www.prnewswire.com/news-releases/ced-unveils-every-other-one-initiative-282556071.html>.

87. According to proxy advisory firm ISS's Governance Principles Survey, the

designed to diversify the boards of companies in which it invests.⁸⁸ BlackRock, the world's largest asset manager, released new proxy voting guidelines in 2019, stating that it expects to see at least two women directors on each of its portfolio companies' boards.⁸⁹ California Public Employees' Retirement System (CalPERS), one of the largest pension funds in the country, launched a board diversity plan in 2017, announcing it would withhold votes against existing directors who sit on U.S. company boards without diverse board members.⁹⁰ More recently, the Midwest Investor Diversity Initiative, a group of eleven pension and union funds with a collective \$750 billion in assets, launched an effort to persuade small and mid-sized companies in the Midwest to adopt diverse board candidate search policies with the goal of having such companies add more women and people of color to their boards.⁹¹ The views of institutional investors are particularly influential as a source of governance norms, given that such investors make up the majority of the shareholder base of most publicly traded companies.⁹²

majority of investors (61%) and non-investors (55%) agree that board gender diversity is an essential attribute of effective board governance regardless of the company or of its market. Effective for annual meetings on or after February 1, 2020, ISS will recommend against the election of the nominating committee chair at Russell 3000 and S&P 500 companies where there are no women on the board. Lyuba Goltser & Elisabeth McMorris, *Heads Up for the 2020 Proxy Season: ISS Survey Results May Signal Policy Changes*, JD SUPRA (Sept. 13, 2019), <https://www.jdsupra.com/legalnews/heads-up-for-the-2020-proxy-season-iss-65833/>. See also Michal Barzuza et al., *Shareholder Value(s): Index Fund Activism and the New Millennial Corporate Governance*, 93 S. CAL. L.R. 101, 121 (Forthcoming 2020). Available at SSRN: <https://ssrn.com/abstract=3439516> or <http://dx.doi.org/10.2139/ssrn.3439516> (arguing that index funds have demanded gender diversity on the boards of large companies in large part to attract the assets of Millennials, a generation that places a premium on social values in their investments).

88. See State Street Global Advisors, *2017 Global Proxy Voting and Engagement Guidelines* (Mar. 18, 2017), <https://www.ssga.com/investment-topics/environmental-social-governance/2018/07/annual-stewardship-report-2017.pdf>.

89. See *Corporate Governance and Proxy Voting Guidelines for U.S. Securities*, BLACKROCK (Jan. 2020), <https://www.blackrock.com/corporate/literature/fact-sheet/blk-responsible-investment-guidelines-us.pdf>.

90. See Arleen Jacobius, *CalPERS turns Focus to board diversity in proxy Board Diversity in Proxy Voting*, PENSIONS & INVESTMENTS, (Sept. 17, 2018), <https://www.pionline.com/article/20180917/ONLINE/19091861/calpers-turns-focus-to-board-diversity-in-proxy-voting>.

91. See Jeff Green, *A \$750 Billion Midwest Fund Group Pushes for Board Diversity*, BLOOMBERG (Aug. 13, 2019), <https://www.bloomberg.com/news/articles/2019-08-13/a-750-billion-fund-group-targets-midwest-s-white-male-boards>.

92. See Charles McGrath, *80% of Equity Market Cap Held by Institutions*, PENSIONS & INVESTMENTS, (Apr. 25, 2017), <https://www.pionline.com/article/20170425>

In this context, we are seeing a shift in workplace power dynamics, and new norms are emerging around greater gender equity inside the boardroom.⁹³ When stock exchanges formulate corporate governance listing standards, they look to prevailing industry and community norms as their primary reference point.⁹⁴ As discussed in Part V, listing standards should reflect such changes in corporate norms and reinforce emerging norms around gender equity in the boardroom.

III. THE BUSINESS CASE AGAINST HOMOGENEITY

There are three main normative justifications for imposing a gender diversity mandate on corporate boards: economic, individual fairness, and societal public interest. The economic justification is that increasing the number of women directors will improve corporate governance, which will lead to better corporate performance. The individual fairness justification is that as a matter of fairness, equally qualified women should have the same access as men to opportunities that yield economic power. The societal public interest justification relies on the argument that more gender-balanced boards are important for democratic legitimacy, achieving equality, and creating a fairer society. This Article focuses on economic justifications because they appear more prominently in the U.S. conversations on board gender diversity, where shareholder primacy is still the dominant model.

Effective corporate governance plays a central role in the proper functioning of companies and hinges to a large degree on the strength of the board. Since the early 2000s, and following a series of major corporate scandals and the financial crisis, prevailing views about the characteristics of a strong board have changed dramatically.⁹⁵ Congress passed the

/INTERACTIVE/170429926/80-of-equity-market-cap-held-by-institutions (noting that institutions own about 78% of the market value of the Russell 3000 index and 80% of the large-cap S&P 500 index).

93. See Claire A. Hill, *#MeToo and the Convergence of CSR and Profit Maximization*, 69 CASE W. RES. L. REV. 895, 895-96 (2019) (observing that shareholder activism is increasingly focused on “boys club” cultures at workplaces and companies are beginning to address issues salient to gender equality in corporate America such as gender diversity on boards).

94. See MACEY, *supra* note 78, at 33.

95. In the wake of the highly publicized Enron and WorldCom corporate scandals in the early 2000s, exchanges have come to play a central role in promulgating the corporate governance requirements of public companies. Congress and the exchanges focused their attention on the corporate governance practices of public companies to maintain investor confidence in the markets. Sarbanes-Oxley Act of 2002 focused on strengthening the requirements for director and auditor independence. See Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 116 Stat. 745 (2002).

Sarbanes-Oxley Act of 2002,⁹⁶ and the exchanges issued a new set of corporate governance listing standards aimed at improving the board's oversight function, decision-making, and overall performance.⁹⁷ The reforms did not include any diversity mandates despite research showing more diverse boards are more effective at reducing risk, monitoring the management team, and decision-making.⁹⁸ Research also shows that more gender-diverse boards in particular outperform predominantly male boards on a range of board functions and corporate performance indicators.⁹⁹ The remainder of Part III summarizes the research on the effects of board diversity on corporate performance and board function.

For decades, gender-diversity advocates have argued that gender diversity is good for business and by increasing diversity, a corporation's bottom line would improve. In fact, many empirical studies show a correlation between greater gender diversity and business performance.¹⁰⁰ For example, the

96. *See id.*

97. New NYSE listing standards required a majority of independent directors and the audit, compensation and nominating governance committees only be comprised of independent directors. Sarbanes-Oxley defined a new broader responsibility for corporate officers, including requiring them to certify financial statements and that the company has a system in place to fairly present its results. *See id.* at § 401(a)(i); *see also* Report of the New York Stock Exchange Corporate Accountability and Listing Standards Committee (June 6, 2002), <http://www.iasplus.com/en/binary/resource/nysegovf.pdf> (citing "increase the quality of board oversight and lessen the possibility of damaging conflicts of interest" as the justifications for the reforms).

98. *See infra* discussion and text accompanying notes 111-115.

99. *See infra* discussion and text accompanying notes 104-115.

100. *See* Thomas Lee Hazen, *Diversity on Corporate Boards: Limits of the Business Case and the Connection Between Supporting Rationales and the Appropriate Response of the Law*, 89 N.C. L. REV. 887, 888 (2011); Lisa M. Fairfax, *Board Diversity Revisited: New Rationale, Same Old Story?*, 89 N.C. L. REV. 855, 858 (2011) (outlining the various empirical studies establishing a positive relationship between board diversity and improved financial performance along a variety of financial metrics). A study of the boards of FTSE-listed companies found that operational performance and share prices were both higher in the case of companies where women made up over 20% of board members than those companies with lower female representation. Yilmaz Arguden, *Why Boards Need More Women*, HARV. BUS. REV. (June 7, 2012), <https://hbr.org/2012/06/why-boards-need-more-women>. Gender-balanced leadership teams were 21% more likely to experience above-average profitability than companies with the least gender-balanced teams, according to a McKinsey Report. *See Delivering Through Diversity*, MCKINSEY & COMPANY (Jan. 2018), https://www.mckinsey.com/~media/McKinsey/Business%20Functions/Organization/Our%20Insights/Delivering%20through%20diversity/Delivering-through-diversity_full-report.ashx. Companies with the highest representation of women on their senior teams reap 34% more profits than companies with the lowest female representation according to study by Catalyst. *The Bottom Line: Connecting Corporate Performance and Gender Diversity*, CATALYST

Credit Suisse Research Institute found that from 2005 to 2011, the shares of companies with at least one woman on the board outperformed those without any women.¹⁰¹ Analysis from Harvard's School of Public Health ranked Fortune 500 companies by the number of women directors present on their boards and found those in the highest quartile had a 42% greater return on sales.¹⁰² Federal reserve economists analyzing the performance of 90 U.S. bank holding companies found that banks with more gender diversity on their boards perform better.¹⁰³

However, critics attack the adequacy of such studies, noting that correlation does not establish causation and also cite studies showing negative correlations.¹⁰⁴ There is also a body of research finding no causation between greater gender diversity and improved profitability and stock performance.¹⁰⁵ What this research and critics of mandatory board diversity efforts fail to address are the potential negative effects of homogeneity on board performance. The sense of comfort that people feel in a homogenous group comes at a cost; homogenous groups have less objective judgment and more blind spots in their decision-making.¹⁰⁶

(2004), https://www.catalyst.org/wp-content/uploads/2019/01/The_Bottom_Line_Connecting_Corporate_Performance_and_Gender_Diversity.pdf/.

101. See *Gender Diversity and Corporate Performance*, CREDIT SUISSE RES. INST. (Jul. 31, 2012), <https://www.credit-suisse.com/about-us-news/en/articles/media-releases/42035-201207.html>.

102. See Lois Joy et al., *The Bottom Line: Corporate Performance and Women's Representation on Boards*, CATALYST (Oct. 15, 2007), https://www.catalyst.org/wp-content/uploads/2019/01/The_Bottom_Line_Corporate_Performance_and_Womens_Representation_on_Boards.pdf.

103. See Ann L. Owen & Judit Temesvary, *Gender Diversity on Bank Board of Directors and Performance*, FED. RES. (Feb. 12, 2019), <https://www.federalreserve.gov/econres/notes/feds-notes/gender-diversity-on-bank-board-of-directors-and-performance-20190212.htm>.

104. See Fairfax, *supra* note 100, at 862 (highlighting studies showing negative correlation between board diversity and firm value).

105. See Lisa M. Fairfax, *The Bottom Line on Board Diversity: A Cost-Benefit Analysis of the Business Rationales for Diversity on Corporate Boards*, 2005 WIS. L. REV. 795, 810 (2005).

106. The effects associated with homogeneity include lack of accuracy in processing information and an absence of objectivity in making decisions. Psychologists call this phenomenon "groupthink." See Frances J. Milliken & Luis L. Martins, *Searching for Common Threads: Understanding the Multiple Effects of Diversity in Organization Groups*, 21 ACAD. MGMT. REV. 402, 414 (1996). One study revealed that all-white juries made more factually inaccurate statements and considered a narrower range of information during jury deliberations than did racially diverse juries. See Samuel R. Sommers, *On Racial Diversity and Group Decision Making: Identifying Multiple Effects of Racial Composition on Jury Deliberations*, 90 J.

Decades of social science research shows that diverse groups are more innovative at solving complex, non-routine problems—the exact types of problems that boards are tasked with providing strategic input on—than homogeneous groups.¹⁰⁷

Gender diversity on boards changes behaviors, decisions, and director interactions. The presence of women directors on boards can improve how boards function and enhance the quality of discussions.¹⁰⁸ Research suggests that women exercise more due diligence,¹⁰⁹ are more reflective,¹¹⁰ and may be more effective at dealing with risk, a key function of a corporation's board.¹¹¹ Another study found that public companies with more women on their boards have fewer governance-related scandals and have higher

PERSONALITY & SOC. PSYCHOL. 597, 606-07 (2006). In another study, researchers asked traders to price stocks in simulated markets. The participants were placed in either ethnically diverse or homogenous teams. Traders who were part of the diverse teams were 58% more likely to price stocks correctly, whereas those in homogenous groups were more prone to pricing errors. David Rock & Heidi Grant, *Why Diverse Teams Are Smarter*, HARV. BUS. REV. (Nov. 4, 2016), <https://leadersforgood.net/wp-content/uploads/2016/01/H038YZ-PDF-ENG.pdf> (citing Sheen S. Levine et al., *Ethnic Diversity Deflates Price Bubbles*, 111 PNAS 18,524 (2014)).

107. This is not only because people with different backgrounds bring new information, but simply interacting with individuals who are different forces groups to prepare better, anticipate alternative viewpoints, and expect that reaching consensus will require effort. See Katherine W. Philips, *How Does Diversity Make Us Smarter*, SCI. AM. (Oct. 1, 2014), <https://www.scientificamerican.com/article/how-diversity-makes-us-smarter/>.

108. A 2010 study published in *Science* provides evidence that “collective intelligence” generally increased when women made up a greater proportion of the group. See Joan MacLeod Heminway & Sarah White, *Wanted: Female Corporate Directors*, 29 PACE L. REV. 249, 287-88 (2009) (summarizing findings by social psychologists that women “communicate and make decisions differently than men in ways that may be more compatible with the complexity and uncertainty inherent in turbulent environments”).

109. Boards with a higher number of female directors are more likely to ask top-ranked financial advisers for help in assessing the price at which their companies will sell in a takeover offer. See Maurice Levi et al., *Are Women More Likely to Seek Advice than Men? Evidence from the Boardroom*, 8 J. RISK FIN. MGMT. 127, 134 (2015).

110. See Jennifer Miner Knippen & Trevor A. Foulk, Univ. Va., *Ruminating at the Top: Exploring the Effects of Gender Bias on Strategic Choice*, Academy of Management Conference (Nov. 30, 2014).

111. See Linda-Eling Lee et al., *Women on Boards: Global Trends in Gender Diversity on Corporate Boards*, MSCI (Nov. 2015), <https://www.msci.com/documents/10199/04b6f646-d638-4878-9c61-4eb91748a82b> (showing that companies with more than the average numbers of female directors score higher on MSCI's metric for management of environmental, social and governance risks).

meeting attendance rates.¹¹²

Studies also suggest that other corporate stakeholders benefit from board gender diversity. Companies with more gender diverse boards have more women in their management ranks and a smaller gender wage gap.¹¹³ In other words, boards with more female members have positive effects on the career development of women at lower levels of the corporation, ultimately helping to create a wider pipeline of female talent.¹¹⁴

Given the number of studies showing the benefits of board diversity on board performance along several metrics, the business case against homogeneity is becoming harder for corporations and investors alike to ignore.

IV. STALLED PROGRESS: WHY VOLUNTARY DIVERSITY EFFORTS HAVE FAILED

Part IV explains two predominant obstacles to women reaching the boardroom, despite the business case for improving the gender diversity of corporate boards.

A. Low Board Turnover & Overemphasis on Prior Board Experience

One reason that has been cited by corporate governance experts for slow progress is the low turnover among corporate directors. With low turnover, opportunities for increasing board diversity are limited. A study by the Conference Board found that about half of companies in the S&P 500 and Russell 3000 disclosed no change in their board makeup in 2018, similar to

112. See Lee, *supra* note 111, at 6 (showing that public companies with more women on their boards are less likely to be hit by scandals such as bribery, fraud or shareholder contests).

113. Higher levels of women on corporate boards correlate with higher levels of women in management jobs and with lower levels of gender inequalities in pay. See Siri Terjesen & Val. Singh, *Female Presence on Corporate Boards: A Multi-Country Study on Environmental Context*, 83 J. BUS ETHICS 55, 59 (2008). When boardrooms and executive suites represent the demographics of the workforce, employees are more likely to stay with the organization, and female and minority potential employees are more likely to see the organization as an attractive employer. See Amy J. Hillman et al., *Organizational Predictors of Women on Corporate Boards*, 50 ACAD. OF MGMT. J., 941, 945 (2007); Mary C. Mattis, *Women Directors: Progress and Opportunities for the Future*, 5 BUS. CONTEMP. WORLD, 140, 148 (1993).

114. See Catherine H. Tinsley & Kate Purmal, *Helping More Women Get CEO Jobs*, HARV. BUS. REV. (July 29, 2019), https://hbr.org/2019/07/research-board-experience-is-helping-more-women-get-ceo-jobs?utm_medium=social&utm_source=linkedin&utm_campaign=hbr (finding that board experience is helping more women get CEO jobs).

the turnover rate in 2016.¹¹⁵ In other words, these companies neither added a new director nor replaced an existing director. Further, one-fourth of Russell 3000 directors stay in their positions for more than 15 years, and the average tenure of an S&P 500 director is 12.7 years.¹¹⁶

When a seat did become available, only one-quarter of corporations elected a first-time director who had never previously served on a public company board. Corporations primarily look to candidates who have C-suite experience or have previously served on a public company board when filling a board seat vacancy, largely out of custom and not because of any legal requirement or evidence to support the practice. There are no studies indicating that such experience is linked to better corporate performance. On the other hand, there are studies indicating that directors with prior managerial experience may have biases in favor of management that could undermine their ability to be independent and objective, which are key qualities of an effective director.¹¹⁷ Qualified candidates may need to have a solid understanding of corporate affairs and financial matters in order to effectively participate on a board, but candidates do not solely develop these skills by sitting on boards or by serving as a CEO. The emphasis on prior board experience acts as a barrier to women being considered for board vacancies because few women have this experience on their resumes.

The low turnover of board positions coupled with the Catch-22 emphasis on prior board experience as a qualification to board service cannot be easily overcome without a gender diversity mandate that forces corporations to stop using the “lack of qualified” women excuse.¹¹⁸

115. See *Despite Demand for More Diversity and Refreshment, Half of Russell 3000 Companies Report No Change in Board Composition*, CONF. BD. (Apr. 24, 2019), https://www.conference-board.org/press/news/index.cfm?id=49831&mod=article_incline.

116. See Matteo Tonello, *Corporate Board Practices in the Russell 3000 and S&P 500*, CONF. BD. (2019), <https://www.russellreynolds.com/en/Insights/thought-leadership/Documents/TCB-Corporate-Board-Practices-2019.pdf>.

117. See Fairfax, *supra* note 105, at 881 (citing Lucian Bebchuk & Jesse Fried, *Pay Without Performance: The Unfulfilled Promise of Executive Compensation*, 33-34 (2004)) (noting that directors who are executives or former executives may have biases in favor of management).

118. See Fairfax, *supra* note 105, at 858 (examining the “pool problem” and finding that the problem may be exaggerated.); See also Emily Chasan, *BlackRock Is Sick of Excuses for Corporate Boards Lacking Women*, BLOOMBERG (Nov. 2, 2018), <https://www.bloomberg.com/news/articles/2018-11-03/blackrock-is-sick-of-excuses-for-corporate-boards-lacking-women>. (quoting Michelle Edkins, BlackRock’s global head of stewardship, “Every man was a first-time director once. If someone took a bet on an untrained director who happened to be a man, you can take a bet on an untrained director who happens to be a woman.”).

B. Unconscious Gender Bias

Federal legislation did not guarantee equal employment opportunities for women until the 1960s. Prior to the passage of Title VII, private employers were free to discriminate against women in every aspect of the workplace. More than forty years after its passage, women still face significant barriers with each step up the corporate hierarchy.

Numerous studies confirm that deeply entrenched stereotypes, discriminatory attitudes, and subconscious gender biases remain significant barriers to women breaking through the “glass ceiling” and reaching the upper echelons of corporate America.¹¹⁹ Some scholars describe this as “unconscious gender bias,” which is the unintentional and automatic mental associations based on gender, stemming from traditions, norms, values, cultures and/or experiences.¹²⁰

Research shows that both men and women overestimate male performance and underestimate female performance. One Yale University study found that both male and female scientists were more likely to hire men, consider them more competent than women, and pay them \$4,000 more per year than women.¹²¹ Another study of employees of a large service organization found even when there are no differences in performance appraisals, more men than women received promotions.¹²² A study of business school graduates found that women with an MBA degree from a top-twenty business school earned 12% less in her first year of employment than her male counterpart.¹²³ Separately, a 2018 Georgetown University study found that men with bachelor’s degrees make an average of \$26,000 more per year than women

119. See Deborah L. Rhode, *The Subtle Side of Sexism*, 16 COLUM. J. GENDER & L. 613, 618 (2007) (detailing the social science data showing that subconscious biases lead to women being held to higher standards, female resumes being evaluated less favorably, and women internalizing the stereotypes and viewing themselves less qualified for promotions and leadership positions); Jayne W. Barnard, *More Women on Corporate Boards? Not So Fast*, 13 WM. & MARY J. WOMEN & L. 703, 713-14 (2007).

120. See Int’l Labour Org., *ACT/EMP Research Note: Breaking Barriers: Unconscious Gender Bias in the Workplace* 3 (Aug. 2017), https://www.ilo.org/wcmsp5/groups/public/---ed_dialogue/---act_emp/documents/publication/wcms_601276.pdf.

121. See Margaretta Midura, *John vs. Jennifer: A Battle of the Sexes*, YALE SCI. (Feb. 19, 2013), <http://www.yalescientific.org/2013/02/john-vs-jennifer-a-battle-of-the-sexes/>.

122. See IRIS BOHNET, *WHAT WORKS: GENDER EQUALITY BY DESIGN* (2016).

123. See Christina Settini, *Tackling the MBA Gender Pay Gap*, FORBES (Sept. 25, 2017), <https://www.forbes.com/sites/christinasettimi/2017/09/25/tackling-the-mba-gender-pay-gap/#4c7653791f2d>.

with the same credentials.¹²⁴

Shareholder activism is also not immune from unconscious gender bias. A 2017 study investigated the reasons that hedge fund activists seemingly ignore evidence for gender-diverse boards in their choices for director nominees and disproportionately target female chief executive officers.¹²⁵ The authors suggest that hedge funds may be subconsciously biased against women leaders due to perceptions, cultural attitudes, and beliefs about the attributes of leaders in our society. Activists may view female CEOs as weak and may be more willing to second-guess and criticize the corporate strategic plans put forth by women leaders. Indeed, one academic study found that the persistent mention of a female CEO in media coverage leads to a 96% probability that activists will target her company.¹²⁶

Research shows that when directors are looking to fill open positions on their board, they tend to favor people like themselves.¹²⁷ So when the majority of directors are white men, they are likely to favor, mentor, and invest more in other white men.

Unconscious gender bias is entrenched in our culture. It is a significant barrier to the advancement of women in corporate America and into leadership roles more broadly. Unconscious gender bias is also difficult to minimize and prevent without a strong regulatory framework. A gender diversity mandate is an effective way to overcome unconscious gender bias where other less stringent efforts have failed.¹²⁸

124. See Anthony P. Carnevale et al., *Women Can't Win: Despite Making Educational Gains and Pursuing High-Wage Majors, Women Still Earn Less Than Men* (2018), CTR. ON EDUC. & THE WORKFORCE, https://cew.georgetown.edu/wp-content/uploads/Women_FR_Web.pdf.

125. See David A. Katz & Laura A. McIntosh, *Activism and Board Diversity*, HARV. L. SCH. F. CORP. GOVERNANCE & FIN. REG. (Sept. 29, 2017), <https://corpgov.law.harvard.edu/2017/09/29/activism-and-board-diversity/>.

126. See *id.*

127. See *Diversity in the Boardroom: Perspectives and Practices*, DELOITTE 13 (2015), https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_Board_Diversity_Full_Article.PDF (noting that an overwhelming majority of companies turn to their own directors for board member recommendations).

128. See Siri Terjesen, *Why Some Board Gender Quotas Don't Work*, CATALYST (Feb. 12, 2019), <https://www.catalyst.org/2019/02/12/why-some-board-gender-quotas-dont-work/> (noting that a large body of research suggests that governments enact a board gender quota if other soft measures such as target-setting fail to increase female representation in the boardroom).

V. A GENDER DIVERSITY LISTING STANDARD APPROACH

Globally, board gender diversity mandates are not new,¹²⁹ but they have become of more immediate import in the United States in light of the recent transformative women's movements.¹³⁰ Nations that are more successful at nearing gender parity on corporate boards provide some guidance about what would transform America's boardrooms. One of the greatest predictors of a more gender-diverse board appears to be the strength of any regulation mandating a minimum level of such diversity. Countries with the strongest regulatory and enforcement regimes, paired with the most stringent and binding quotas, are the most effective at increasing the representation of women on corporate boards.¹³¹ For example, Norway and France, countries with the highest percentage of female directors in the world, have strong laws with strict gender quota mandates.¹³² The regulatory approach in California

129. See *supra* discussion and text accompanying note 27. Norway was the first country to enforce a board gender quota in 2006, which required 40% female representation. Iceland, France, and Spain also mandate 40%. Belgium, Italy, Germany, and the Netherlands have lower gender quotas. See Inst. Shareholder Servs., Inc., *Gender Parity on Boards Around the World*, HARV. L. SCH. F. CORP. GOVERNANCE & FIN. REG. (Jan. 5, 2017), <https://corpgov.law.harvard.edu/2017/01/05/gender-parity-on-boards-around-the-world/>; Alison Smale & Claire Cain Miller, *Germany Sets Gender Quota in Boardrooms*, N.Y. Times (Mar. 6, 2015) <https://www.nytimes.com/2015/03/07/world/europe/german-law-requires-more-women-on-corporate-boards.html>; Rosenblum, *supra* note 28, at 1441-1442 (detailing corporate diversity quotas that have been established abroad).

130. See *supra* Part II.B.

131. On the other hand, countries with the fewest percentage of female directors do not have any gender diversity regulation. Countries with the lowest percentage of female directors in the world include South Korea (2.3%), Japan (5%), Russia (5.4%), and Greece (8.8%). See Inst. Shareholder Servs., Inc., *Gender Parity on Boards Around the World*, HARV. L. SCH. F. CORP. GOVERNANCE & FIN. REG. (Jan. 5, 2017), <https://corpgov.law.harvard.edu/2017/01/05/gender-parity-on-boards-around-the-world/>.

132. Norway's percentage of female directors is 42.1% and France's is 36.8%. Norwegian law mandates strict quotas that depend on the size of the board: (i) if the board of directors has two or three members, both sexes shall be represented; (ii) if the board of directors has four or five members, each sex shall be represented by at least two members; (iii) if the board of directors has six to eight members, each sex shall be represented by at least three members; (iv) if the board of directors has nine members, each sex shall be represented by at least four members, and if the board of directors has more members, each sex shall represent at least 40% of the members of the board; and (v) the rules apply correspondingly for elections of deputy members of the board of directors. See Norwegian Public Limited Liability Companies Act, § 6-11a (Act No. 45/June 13, 1997) (Nor.); Inst. Shareholder Servs., Inc., *Gender Parity on Boards Around the World*, HARV. L. SCH. F. CORP. GOVERNANCE & FIN. REG. (Jan. 5, 2017), <https://corpgov.law.harvard.edu/2017/01/05/gender-parity-on-boards-around-the->

SB 826 is modeled after the quota-based approaches in Norway and France.

In the U.S., states are recognizing that a mandate approach may be required because progress has been slow, and voluntary self-regulation approaches have not proven to be sufficiently effective at achieving gender-balanced boards. The question then becomes how to implement a mandate in the U.S. that will pass constitutional muster and fit within the country's political, economic, and cultural preferences for corporate freedom and market-based approaches. The stock exchanges are best positioned to impose a gender diversity mandate on publicly traded corporations through new corporate governance listing standards.

Under this proposal, the major U.S. stock exchanges would develop listing standards, subject to SEC approval,¹³³ that would mandate a minimum number of women directors on the boards of the companies listed on their exchanges.¹³⁴ The listing standards would be based on best practice

world/. The French law requires listed companies or non-listed companies (with revenues or total assets of over EUR fifty million and employing at least 500 persons for the last three years) to have a proportion of men or women that is at least 40%. *See* Loi 2011-103 du 27 janvier 2011 relative à représentation équilibrée des femmes et des hommes au sein des conseils d'administration et de surveillance et à l'égalité professionnelle [Law 2011-103 of January 27, 2011 on Equal Representation of Women and Men on Corporate Boards and on Equality in the Workplace], JOURNAL OFFICIEL DE LA REPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], Jan. 28, 2011, at 1680. Finland does not have specific quotas but instead has in place "softer" laws that mandate the presence of women on corporate boards, and Sweden uses a public disclosure approach. Since 2016, the Finnish corporate code stipulates that both women and men be represented on listed company boards, and listed companies are required to report on their objectives and initiatives to ensure that both women and men are represented. *See* FIN. SEC. MKT. ASS'N, *Finnish Corporate Governance Code* (2015), <https://cgfinland.fi/wp-content/uploads/sites/6/2015/10/hallinnointikoodi-2015eng.pdf>. Since 2015, Sweden's corporate code requires that board nomination committees strive for gender balance in their proposals regarding board composition and provide the public with explanations of their proposals. *See* SWED. CORP. GOVERNANCE Bd., *The Swedish Corporate Governance Code* (2016), http://www.corporategovernanceboard.se/UserFiles/Archive/496/The_Swedish_Corporate_Governance_Code_1_December_2016.pdf.

133. Under Sections 19(b) and 19(c) of the Exchange Act, the SEC would need to find consistency with the requirements of the Exchange Act in order to approve of an exchange-established gender diversity listing standard. *See* Securities Exchange Act of 1934, 15 U.S.C.A. § 78s (2019).

134. By setting a minimum number, companies would have flexibility to choose the total number of women on their board and decide whether to expand the total number of board seats to allow for the addition of women board members. Importantly though, gender parity requires a critical mass of women on a board. Studies have shown that the inclusion of one or two women as token minority representatives was both ineffective and harmful to equality and inclusion efforts.

guidelines and be formulated with input from various stakeholders such as investors, listed companies, corporate governance experts, and advocacy groups. The listing standards would also be tailored to allow for corporate control and to accommodate differences between companies, yet still be effective at increasing the number of women on publicly traded corporate boards by virtue of being a mandate. The listing standards would be strictly enforced by the exchanges through fines and threats of delisting. The exchanges would also require periodic public disclosure of board diversity figures to ensure compliance. This proposal aims to address the board gender diversity problem while taking advantage of the strengths and expertise of the exchanges.

Critics of a gender diversity listing standard approach may argue that it adds to the cost of becoming or remaining a public company.¹³⁵ As we have seen with any new regulation of private markets, there will always be upfront concerns about regulating corporations because the costs are more direct and easier to calculate than the benefits. It is also likely that the regulation becomes cost effective over time as more women reach senior positions.¹³⁶ Notably, the overall cost of underrepresentation of women to the economy is difficult to quantify because the costs are likely indirect.¹³⁷ Finally, the cost burden involved in recruiting women directors is not articulated with any specificity relative to the costs associated with ongoing disclosure requirements or enhanced governance duties currently required of listed companies.¹³⁸

135. SEC Commissioner Hester M. Peirce made this argument with respect to board diversity mandates generally in her remarks before the Society for Corporate Governance National Conference. See Hester M. Pierce, *Baby on Board: Remarks Before the Society for Corporate Governance National Conference*, SEC (June 28, 2019), <https://www.sec.gov/news/speech/baby-board-remarks-corporate-governance-national-conference-062819>.

136. Recruiting costs may decrease as more women enter the leadership pipeline and corporations invest in developing such pipeline. *Ten years on from Norway's quota for women on corporate boards*, THE ECONOMIST (Feb. 17, 2018), <https://www.economist.com/business/2018/02/17/ten-years-on-from-norways-quota-for-women-on-corporate-boards> (showing numbers of women on boards have increased since Norway's mandate).

137. But see Kweilin Ellingrud et al., *How Reducing Gender Inequality Could Boost U.S. GDP by \$2.1 Trillion*, Harv. Bus. Rev. (Apr. 12, 2016), <https://hbr.org/2016/04/how-reducing-gender-inequality-could-boost-u-s-gdp-by-2-1-trillion> (finding that if there was parity between the sexes in the workplace, the United States economy would earn approximately \$4.3 trillion more between 2016 and 2025).

138. See Henry N. Butler & Larry E. Ribstein, *The Sarbanes-Oxley Debacle: What We've Learned and How to Fix It*, 1, 40 (2006) (detailing cost data of complying with Sarbanes-Oxley).

Critics of a gender diversity listing standard approach may also argue that it interferes with private contracting rights of corporations and its shareholders. Some corporate scholars assert that corporate governance arrangements are matters of private ordering, and shareholders and directors can arrange their governance structure more efficiently than regulators.¹³⁹ This argument relies on the premise that shareholders are providing actual consent to the corporation's directors, but as others have argued, shareholders' consent is often coerced or ignorant.¹⁴⁰ This argument also ignores the exchanges' self-identified role in encouraging "high standards of corporate democracy."¹⁴¹ From time to time, exchanges step in to adjust for market inefficiencies, externalities, and obstacles.

Putting these critiques aside, the proposal raises two legal issues with respect to the exchanges' authority to adopt gender diversity listing standards under Section 19(b) of the Exchange Act and under the equal protection clause of the U.S. Constitution.

A. Section 19(b) Exchange Act Analysis

As discussed at Part II.A., corporate governance listing standards require approval by the SEC before they can become effective. Under Section 19(b) of the Exchange Act, in order to approve an exchange-established listing standard, the SEC needs to find consistency with the requirements of the Exchange Act. When the exchanges have made the most dramatic changes to their corporate governance listing standards, they have typically followed a strong push from the SEC and a negotiation with the SEC over the new requirements until both parties are satisfied. However, the proposal here would not follow this protocol.

Given the limited case law in this area, it is difficult to define with precision the authority of the exchanges with respect to corporate governance matters.¹⁴² However, from a governance perspective, the proposal is

139. See, e.g., Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416, 1442 (1989).

140. See, e.g., Melvin A. Eisenberg, *The Conception that the Corporation is a Nexus of Contracts, and the Dual Nature of the Firm*, 24 J. CORP. L. 819, 824 (1999).

141. See NYSE, *Listed Company Manual* (2019), https://nyseguide.srorules.com/listed-company-manual/document?treeNodeId=csh-da-filter!WKUS-TAL-DOCS-PHC-%7B0588BF4A-D3B5-4B91-94EA-BE9F17057DF0%7D--WKUS_TAL_5667%23teid-0 (noting that listing standards are aimed at "maintaining appropriate standards of corporate responsibility, integrity and accountability to shareholders").

142. The *Business Roundtable* decision limited the scope of SEC authority with respect to disapproving proposed listing standards as long as it is satisfied that any differences in the application of the listing standards are based on meaningful distinctions

analogous to the independent director listing standards for which the NASDAQ and NYSE received SEC approval and implemented following the corporate accounting scandals in the early 2000s.¹⁴³ The SEC approved the independent director listing standards and found the listing standards to meet the consistency standard.¹⁴⁴ The governance goal of the proposed listing standards is similar to that of the independent director listing standards; both change the composition of a listed company's board in order to improve the board's oversight function, decision-making, and overall performance. The proposal, like that of the independence standards, relates to the maintenance of integrity of the securities markets and fairness to investors by promoting investor confidence in the monitoring role of the board and by providing reliability in the level of diversity mandated. Gender diversity listings standards fall within the right of the exchanges to establish quantitative standards for their respective markets.

B. Equal Protection Clause Analysis

1. Justiciability

Before reaching the merits of an equal protection challenge and assuming the court has jurisdiction, claimants must show they have a justiciable claim. Claimants other than the companies themselves will have barriers to standing.¹⁴⁵ The Constitution requires a claimant to have suffered an "injury-in-fact" that was caused by the allegedly unconstitutional government action.¹⁴⁶ A shareholder plaintiff would have to argue that encroachment on shareholder voting rights is the "injury-in-fact," while a potential male board member plaintiff would have to argue that he was deprived of the opportunity to sit on the company's board because of his gender. Neither of these arguments is likely to overcome the barriers to standing because the listing

between issuers and are not unfairly discriminatory. *See supra* Part II.A.

143. *See supra* discussion and text accompanying notes 100-101.

144. *See Order Approving Proposed Rule Change by the New York Stock Exchange Related to its Audit Committee Requirements*, 64 Fed. Reg. 71,529 (Dec. 21, 1999); *Order Approving Proposed Rule Change by the National Association of Securities Dealers Related to its Audit Committee Requirements*, 64 Fed. Reg. 71,523 (Dec. 21, 1999).

145. Corporations affected by the law likely will not have the appetite to sue over the gender diversity listing standards given the potential public-relations challenge of being seen as a company that does not support gender diversity. This has proven to be the case in California; to date, no corporation has challenged SB 826.

146. *Valley Forge Christian College v. Americans United For Separation of Church and State*, 454 U.S. 464, 472 (1982).

standard imposes obligations on the company, not its shareholders.¹⁴⁷ Further, the impact of the listing standard on male board members likely amounts to benign differential treatment.¹⁴⁸

2. Government Action

Another threshold matter claimants must meet is the government action requirement. The equal protection clause only applies to the government, so the conduct giving rise to an alleged violation of the equal protection clause must be considered government action. The implementation of gender diversity listing standards by the securities exchanges could face a viable equal protection challenge if the actions of the exchanges are attributed to the government,¹⁴⁹ but there likely is not sufficient state action to mount a successful case.

The securities exchanges began as private membership organizations, but have since become integrated into the administration of the Exchange Act and are subject to SEC oversight. They are treated as private entities under certain circumstances and as quasi-government entities under other circumstances. However, constitutional restraints on private action depend on the link between the private entity and the government.¹⁵⁰ Restrictions on private action based on constitutional guarantees are only valid if there is a

147. The U.S. District Court for the Eastern District of California dismissed Meland's challenge to SB 826 in *Meland v. Padilla* based on a failure to show an "injury in fact." The shareholder plaintiff's argument was that he was being forced to vote for directors in a gender conscious way, but the district court concluded that the shareholders had no standing to bring suit. The court ruled that the shareholder could cast his votes for any board nominee so his voting rights were not impaired.

148. Courts have encouraged benign discrimination to overcome past discrimination and exclusion. *See Swann v. Charlotte-Mecklenburg Board of Education*, 402 U.S. 1 (1971); *Green v. County School Board*, 391 U.S. 430 (1968).

149. Note that when parties have challenged the actions of an SRO on constitutional grounds, the focus of their disputes have been on illegal seizures in violation of the Fourth Amendment and denials of due process or compelled testimony in violation of the Fifth Amendment. *See Steven J. Cleveland, The NYSE as State Actor: Rational Actors, Behavioral Insights & Joint Investigations*, 55 AM. U. L. REV. 1, 4 (2005).

150. The state action doctrine requires action on the part of a state actor to affect a constitutional violation. *See, e.g., United States v. Morrison*, 529 U.S. 598, 621 (2000) ("action inhibited by the first section of the Fourteenth Amendment is only such action as may fairly be said to be that of the States. That Amendment erects no shield against merely private conduct, however discriminatory or wrongful." (quoting *Shelley v. Kraemer*, 334 U.S. 1, 13 (1948)) (internal quotation mark omitted)); *Edmonson v. Leesville Concrete Co.*, 500 U.S. 614, 619 (1991) ("With a few exceptions, such as the provisions of the Thirteenth Amendment, constitutional guarantees of individual liberty and equal protection do not apply to the actions of private entities.").

sufficiently close nexus between the government and the challenged action such that the behavior of the private entity may be fairly attributed to the government.¹⁵¹ While the state action cases have been contradictory and fact-specific, in making such a determination of whether quasi-private behavior constitutes state action, the U.S. Supreme Court has considered the extent of the government's coercion or encouragement, willful and joint participation, delegation of a public function, and entwinement in the management or control of the private actor to achieve governmental objectives.¹⁵²

Relevant to this inquiry is the relative independence of the exchanges from government interference.¹⁵³ Importantly, governmental regulation by itself does not turn a private actor's actions into those of the state.¹⁵⁴ The securities exchanges have a well-established tradition of self-regulation. It was not until the Great Depression that Congress imposed government supervision

151. *See* *Brentwood Acad. v. Tenn. Secondary Sch. Athletic Ass'n*, 531 U.S. 288, 295 (2001) (finding that state action may only be found if the actions of a private organization are appropriately treated as having been caused by the state itself); *Jackson v. Metro. Edison Co.*, 419 U.S. 345, 351 (1974) (finding that whether the entity and state are sufficiently intertwined may require a detailed inquiry because the nature of the state's involvement may not be readily apparent).

152. *See* *Brentwood Acad.*, 531 U.S. at 296. *But see id.* at 295 ("What [private actions are] fairly attributable [to the government] is a matter of normative judgment, and the criteria lack rigid simplicity."); *Edmonson v. Leesville Concrete Co.*, 500 U.S. 614, 632 (1991) (O'Connor J., dissenting) ("[O]ur cases deciding when private action might be deemed that of the state have not been a model of consistency."). *See also* Cass R. Sunstein, *Lochner's Legacy*, 87 COLUM. L. REV. 873, 886 (1987) ("[H]ow does one decide whether government is acting? The legal test could in theory depend on whether government agents are involved in the process. But . . . such a test would be inadequate. State officials are involved in the enforcement of private contract, tort, and property law every day, and their involvement does not subject all private arrangements to constitutional constraints.") (internal quotation mark omitted).

153. *See* *Brentwood Acad.*, 531 U.S. at 288 (finding the actions of a private association with 84% of its members state employees acting in their official capacity and controlling the board of directors to be sufficient for a finding of state action).

154. *See* *Jackson v. Metro. Edison Co.*, 419 U.S. 345, 351–58 (1974) (finding no such nexus between the state and a public utility's action in terminating service to a customer despite the facts that the utility was subject to state regulation, the state had conferred in effect a monopoly status upon the utility, and in reviewing the company's tariff schedules the regulatory commission had in effect approved the termination provision); *Moose Lodge No. 107 v. Irvis*, 407 U.S. 163, 179 (1972) (finding no state action where a liquor license was issued to a private club that refused to serve African Americans). *See also* *Blum v. Yaretsky*, 457 U.S. 991, 1004 (1982) (noting that state action may be found if "[the State] has exercised such significant encouragement, either overt or covert, that the choice must . . . be deemed to be that of the State.").

over the exchanges through the Exchange Act. Further, the Exchange Act emphasizes self-regulation as the primary means of controlling the securities industry.

While early court decisions classified the actions of self-regulatory organizations (SROs), such as the stock exchanges, as state action, since the 1960s, courts have routinely concluded that the actions of stock exchanges should not be attributed to the government.¹⁵⁵ Further, no recent decisions have attributed the actions of a securities exchange to the government.

Under this Article's proposal, state action likely does not exist because the extent of the SEC's action would be allowing the exchanges to establish the listing standards under applicable law. Under the proposal, exchanges would establish the listing standards on their own accord, in pursuit of their own interests to account for the preferences and concerns of the companies whose securities are traded and the investors that are trading those securities, not through any coercion or encouragement by the SEC or other state actor. Since exchanges generate revenue on listings and trades executed on the exchange, they should seek to attract issuers and investors by responding to the expressed preferences and concerns of the public regarding gender diversity.

Further, as was noted in *Business Roundtable*, the SEC's role in approving corporate governance listing standards is limited.¹⁵⁶ The Exchange Act establishes the SEC's approval process, and the exchanges would merely be seeking approval of the SEC pursuant to the statute. Regulatory schemes and requirements do not automatically impose constitutional restraints on private action. Given the SEC's limited role in the development and approval of exchange-established listing standards, the proposal cannot face

155. See Cleveland, *supra* note 149, at 20-22 (summarizing the development of the state action jurisprudence with respect to SROs); Roberta S. Karmel, *Should Securities Industry Self-Regulatory Organizations be Considered Government Agencies*, 14 STAN. J.L. BUS. & FIN. 151, 171-183 (2008) (discussing cases addressing the NASD's and NYSE's immunity from suit, Fifth Amendment claims, and compulsory arbitration); see, e.g., *Desiderio v. National Ass'n of Securities Dealers, Inc.*, 191 F.3d 198, 206 (2d. Cir. 1999); see also *Gold v. SEC*, 48 F.3d 987, 991 (7th Cir. 1995) (concluding comprehensive regulation of securities exchanges by the federal government by itself does not turn exchanges into governmental actors); *U.S. v. Solomon*, 509 F.2d 863, 868-69 (2d Cir. 1975) (rejecting the argument that the NYSE was "in effect the arm of the Government in administering portions of the Securities Exchange Act."); but see *Rooms v. SEC*, 444 F.3d 1208, 1214 (10th Cir. 2006) (finding that due process requirements apply to enforcement actions of the National Association of Securities Dealers, a SRO). Note that the U.S. Supreme Court has not reviewed the issue of state action in the context of a SRO.

156. See *supra* notes 64-69 and accompanying text.

a successful equal protection challenge without a finding of state action. Failure to satisfy the government action requirement normally results in dismissal without reaching the merits of the equal protection claim.

3. *Merits of an Equal Protection Clause Violation*

If the claimants can show that the government harmed them enough to create a justiciable claim, a court could then proceed to the merits of an equal protection challenge. Facial classifications such as the mandate proposed in the gender diversity listing standard are subject to the equal protection clause. Classifications based on gender must meet intermediate scrutiny, or be substantially related to an important government interest.¹⁵⁷ The Court has recognized remedying the effects of past discrimination as a sufficiently important interest to satisfy intermediate scrutiny.¹⁵⁸ Thanks to the #MeToo movement, sex discrimination in corporate America has never been more visible. Women remain underrepresented on corporate boards in proportion to their percentage of the general population because of systemic bias, structural impediments and gendered norms.¹⁵⁹ A gender diversity listing standard should be viewed as a way to combat the entrenched prejudice and systemic barriers women face as they attempt to advance within companies. The government's justification of equity, proportional representation and balanced power would be considered important in the context of reversing systemic inequity in corporate leadership.

With respect to satisfying the substantial relation test, the Court requires the means to be substantially effective and narrowly tailored. The Court has not found facial quotas in the context of race narrowly tailored, and thus are unconstitutional under U.S. jurisprudence.¹⁶⁰ The same reasoning could be used as a rationale to strike down a gender diversity listing standard. Quotas in affirmative action cases are often considered in the public university context based on racial and ethnic classifications.¹⁶¹ However, the case law

157. See *Craig v. Boren*, 429 U.S. 190 (1976); cf. *Mississippi Univ. for Women v. Hogan*, 458 U.S. 718 (1982).

158. See *Mississippi Univ. for Women v. Hogan*, 458 U.S. 718, 724 (1982); *Califano v. Webster*, 430 U.S. 313 (1977). See also *United States v. Virginia*, 518 U.S. 515, 533 (1996) (quoting *Califano v. Webster*, 430 U.S. 313, 320 (1977) (per curiam)) (stating that “sex classifications may be used to compensate women ‘for particular economic disabilities suffered,’ to ‘promote equal employment opportunity,’ and to advance full development of the talent and capacities of our Nation’s people.”).

159. See *supra*, notes 12-24 and accompanying text.

160. See *Grutter v. Bollinger*, 539 U.S. 306, 309, 334 (2003) (reaffirming that quotas are unconstitutional and violate the Fifth and Fourteenth Amendments).

161. See, e.g., *Regents of the Univ. of Cal. v. Bakke*, 438 U.S. 265 (1978); *Gratz v. Bollinger*, 539 U.S. 224 (2003); *Fisher v. Univ. of Texas at Austin*, 570 U.S. 297 (2013),

on quotas in the affirmative action context is not directly applicable to the mandate proposed in the gender diversity listing standard.

First, the constitutional standard of review for race-based classifications is strict scrutiny while intermediate scrutiny is used for sex-based classifications.¹⁶² This could mean a greater tolerance for gender-based quotas than race-based quotas. Further, the election of directors to corporate boards differs substantially from the admissions policies used by universities. Universities typically have a set number of seats available for an incoming class. Common affirmative action programs are ones that set aside a set number of seats for minority groups or ones that use a point system to evaluate students, where minority students are preferentially awarded a set number of points.¹⁶³ Setting aside admissions seats for one group could result in an equally qualified member of another group being denied admission on account of race. On the other hand, corporate boards are able to expand the number of their board seats such that adding a women director does not necessarily foreclose the opportunity of a male director to sit on the board, nor does it provide an absolute bar to his appointment to the board.¹⁶⁴ While the Court has not directly addressed the constitutionality of facial quotas in the gender context, it has shown openness to gender-based classifications that are remedial in nature and aimed at reversing systemic inequality.

A gender diversity listing standard as proposed in this Article would likely sustain a constitutional challenge when analyzed under intermediate scrutiny and when found to be a remedy for the rampant inequities, harmful gender norms, and pervasive sexual harassment and discrimination found in the power structures of America's corporations.

VI. CONCLUSION

Recent political and cultural developments in the United States have renewed interest in corporate board diversity initiatives. However, the

aff'd, 136 S.Ct. 2198 (2016); *Students for Fair Admissions, Inc. v. Pres. & Fellows of Harvard Coll.*, 308 F.R.D. 39 (D. Mass. 2015), aff'd, 807 F.3d 472 (1st Cir. 2015).

162. *But see* *Frontiero v. Richardson*, 411 U.S. 677, 688-91 (1973) (plurality preferring to apply strict scrutiny to sex-based classifications).

163. These were the programs at issue in *Regents of the University of California v. Bakke* and in *Gratz v. Bollinger*, respectively. *Regents of the Univ. of Cal. v. Bakke*, 438 U.S. 265 (1978); *Gratz v. Bollinger*, 539 U.S. 244 (2003).

164. Indeed, the Court has shown a willingness to consider gender quotas to achieve gender parity. It upheld an employer's affirmative action plan with gender preferences in *Johnson v. Transportation Agency*. *Johnson v. Transportation Agency*, 480 U.S. 616, 641-62 (1987).

boardroom gender gap has proven to be systemic and persistent despite the mobilization of shareholders and stakeholders. Simply asking companies to diversify their boards has resulted in companies paying lip service to diversity instead of forcing systemic change. Boardroom gender mandates are necessary to create faster and sustained increases in gender diversity of public company boards.

Boardroom gender mandates have proven to be transformative with respect to gender parity in European countries, but the judicial fate of such mandates in the United States remains in question. The national securities exchanges, operating as private regulators, offer an avenue around the constitutional hurdles raised by SB 826 and are best positioned to address the gender diversity problem in America's boardrooms.