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BACKGROUNDER

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Nasdaq's Proposed Board-Diversity Rule Is Immoral and Has No Basis in Economics

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KEY TAKEAWAYS

Nasdaq's proposed board diversity rule would impose quotas on the basis of sex, sexual orientation, race, and ethnicity.

This rule, which must be approved by the Securities and Exchange Commission, is inconsistent with the SEC's statutory mission.

The proposed rule is a major step backwards morally—and is inconsistent with the equal protection principles of the Constitution and the Civil Rights Act of 1964.

The Nasdaq Stock Exchange (Nasdaq)[1] is the second-largest stock exchange in the world.[2] Approximately 2,900 U.S. companies and 600 foreign companies list their stock on Nasdaq.[3] It is also a so-called self-regulatory organization (SRO) that has been delegated regulatory authority by Congress and by the U.S. Securities and Exchange Commission (Commission, or SEC).[4] Nasdaq imposes and enforces detailed rules on the companies it lists,[5] but these rules must be approved by the SEC.[6] Invoking the imperatives of the "social justice movement"[7] and the "benefits to stakeholders of increased diversity,"[8] Nasdaq is seeking SEC approval to impose a corporate governance rule that would require all listed companies to appoint directors based on sex. Many of these companies would also have to appoint directors on the basis of race, ethnicity, or sexual orientation.[9]

This paper, in its entirety, can be found at **http://report.heritage.org/bg3591**

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Specifically, Nasdaq is proposing to require each of its listed companies, subject to certain exceptions, to provide statistical information regarding "diversity" among the members of its board, and to either have, or explain why it does not have, at least two "diverse" directors on its board.[10] "Diverse" would mean a director who self-identifies as female (without regard to the individual's designated sex at birth), an under-represented minority, or LGBTQ+. Nasdaq defines an underrepresented minority as black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, or two or more races or ethnicities.[11]

The Securities and Exchange Commission should disapprove this proposed Nasdaq rule change. If it does not disapprove the proposed rule, it should institute proceedings regarding the proposed rule.[12] If the commission does not disapprove the rule, then Congress should prohibit securities regulations, including those promulgated by SROs, that discriminate on the basis of race, ethnicity, or sex.

Nasdaq's Cloaked Intentions

Nasdaq's submission to the commission is a façade designed to cloak its political "social justice" objectives in the language of economics and securities regulation. Nasdaq's presentation of the empirical literature blatantly misrepresents that literature. Many of the "studies" or statements it selectively cites rely on nothing more than unsubstantiated political preferences. The actual empirical, peer-reviewed economics literature is highly inconclusive—with most studies showing little or no discernable effect on financial performance due to the sexual, racial, or ethnic composition of corporate boards. All serious surveys of the literature reach this conclusion.

This should be unsurprising since sex, race, and ethnicity have nothing to do with competence. There are a few studies that find either positive or negative effects, but the effects are small. A thorough examination of the literature and of the materials cited in Nasdaq's submission shows that its empirical assertions have virtually no basis in the literature. Furthermore, it misrepresents the content of some of the few supporting studies that are peer reviewed. Its submission is deeply misleading.

Stakeholder Theory. Nasdaq also embraces the stakeholder theory of business purpose in which shareholders, rather than being treated as the owners of the business, are reduced to just one more corporate interest group to be placated by a powerful and largely unaccountable management.

The proposed rule is inconsistent with the Commission's statutory mission.[13] The proposed rule neither protects investors, nor promotes the maintenance of fair, orderly, and efficient markets, nor facilitates capital formation.

Civil Rights and Equal Protection. The proposed rule is inconsistent with the principles underpinning the Civil Rights Act of 1964[14] which makes it an unlawful employment practice for an employer to "limit, segregate, or classify his employees...because of such individual's race, color, religion, sex, or national origin." It is also a violation of the equal protection principles of the United States Constitution.[15] Quotas, such as those instituted by the rule, are particularly suspect constitutionally.[16]

The discussion below does not aspire to be an exhaustive discussion of the complex Supreme Court jurisprudence regarding equal protection under the Fifth and Fourteenth Amendments, disparate impact, or the Civil Rights Act. It should, however, give policymakers pause regarding three things.

- The legal issues raised by the proposed rule are far outside the Commission's technical competence or its mission.
- The ethical issues raised by the proposed rule—which would affirmatively discriminate on the basis of sex, race, and ethnicity—are profound.
- Although the outcome of potential litigation is unclear, the proposed rule may well be successfully challenged in court on both constitutional and Civil Rights Act grounds. As discussed below, this will turn on whether Nasdaq as a regulator is deemed a state actor and whether directors are deemed employees for purposes of the Civil Rights Act. If either of these determinations are made, the rule will likely be held invalid. Moreover, there is no doubt that the Commission is subject to the equal protection provisions of the constitution.

Altering the Narrative. Many, perhaps most, of the proponents of diversity, inclusion, social justice, critical race theory, multiculturism, and identity politics reject (in their words) "the very foundations of the liberal order, including equality theory, legal reasoning, Enlightenment rationalism, and neutral principles of constitutional law."[17] They are engaged in a systematic and sustained effort to effectively change our national ethos from *E Pluribus Unum* to *De Uno, Multis*.[18]

They seek to alter the "narrative" and to make sex, race, ethnicity, and sexual orientation central to law, public policy, and our self-understanding instead of individual achievement, merit, talent, and the content of our character. They actively seek to discriminate on the basis of sex, race, ethnicity, or sexual orientation rather than achieve a society in which such discrimination is unlawful and rare. They seek a *faux* diversity measured by group identity, determined largely by immutable characteristics—rather than true diversity that accounts for the rich tapestry of human experience. They seek to subordinate individual merit to group identity. The SEC should not go down this dubious path.

The Nasdaq proposed rule rests on a faulty premise. Nasdaq falsely asserts that shareholders are demanding the corporations that they own to discriminate on the basis of sex, race, ethnicity, or sexual orientation. Shareholders are free to instruct management to do so or to pursue other environmental, social, or governance (ESG) or social justice objectives via shareholder resolutions. When afforded the opportunity to do so, however, they rarely do. According to *Proxy Review*, "None of the seven proposals on the subject [board diversity] that went to votes last year [2019] earned more than 3 percent" of the votes cast.[19]

NASDAQ's reliance on self-identification for board-diversity disclosures raises liability concerns with respect to misrepresentations under the anti-fraud and reporting provisions of the federal securities laws. A person who is a Caucasian male is objectively not a female Native American, whether he "self-identifies" as a female Native American or not.

Redefining the Purpose of Business. The true agenda of social justice advocates, apparently including Nasdaq management, is to remake the purpose of business. Traditionally, the purpose of a business has been to earn a return for its owners by cost-effectively combining the capital and entrepreneurial spirit of its founders and owners with the labor and talent of its employees in a competitive environment to satisfy the wants and needs of its customers. The relationship between owners, management, workers, suppliers, and customers are (subject to certain broad constraints imposed by law) privately decided and voluntary.

With increasing stridency, there is a major effort under way to redefine the purpose of businesses to achieve various social or political objectives unrelated to earning a return, satisfying customers, or treating workers or suppliers fairly. This is being done under the banner of social justice; corporate social responsibility (CSR); stakeholder theory; environmental, social and governance (ESG) criteria; socially responsible investing (SRI); sustainability; diversity; business ethics;

common-good capitalism; or corporate actual responsibility.[20] These new objectives would be enforced by various means, including, as is the case here, regulation.

If successful, these attempts to redefine the purpose of business would have marked adverse social consequences. To wit:

- Management would be even less accountable to anyone since the metrics of success will become highly amorphous and constantly changing.
- Businesses would become less productive and less competitive. Jobs would be lost, and wages would grow more slowly.
- The social welfare cost of going down this road would be considerable.[21]
- It is also one more major step toward the federalization of corporate governance.
- Last, if the SEC chooses to countenance diversity statistical reporting, it should require reporting of types of diversity that are more relevant to business success than the immutable racial, ethnic, or sexual characteristics of its directors.

The Purpose of the Commission and the Securities Laws

The mission of the SEC is to "protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation."[22] The proposed rule does not further these objectives. The proposed rule is beyond the scope of the Commission's statutory charge.[23]

Protecting Investors. The proposed rule does not protect investors in any sense. It does not increase their returns or protect them from losses. It does not protect them from fraud or misrepresentation. It does not protect them from an unaccountable management or board of directors acting in its own interest or pursuing political or social objectives at the expense of investors. Investors may require management and the board to implement board diversity (as defined by the proposed rule or in a similar fashion), but when afforded the opportunity to do so, they do not.[24] Moreover, a very high percentage of the shareholder proposals submitted are submitted by government pension funds in their capacity as shareholders for political reasons.[25] Neither does the rule further fair, orderly, and efficient markets nor facilitate capital formation.

As discussed in detail below, the empirical literature has been misrepresented by Nasdaq. Moreover, if, as Nasdaq claims, diversity requirements (as defined by Nasdaq) are such an obvious and simple way to increase returns, then boards, management, and shareholders require no regulatory mandate to adopt them because it would be in their own financial interest to do so. The fact that Nasdaq feels compelled to mandate diversity, as it defines it, belies the argument that it is in investors' best interest. The rule represents an attempt to pursue political or social objectives unrelated to the Commission mission and likely to be detrimental to investor interests.

To date, the Commission has only required diversity reporting in a responsible fashion.[26] It has not mandated quotas; has acknowledged that there are many kinds of diversity that may be relevant in selecting directors; and has only required diversity reporting (in the Nasdaq sense) to the extent a reporting company has actually relied on these criteria. It should not go down the path that Nasdaq is asking it to take.

Anti-Fraud and Reporting. NASDAQ's reliance on self-identification for board diversity disclosures raises liability concerns with respect to misrepresentations under the anti-fraud and reporting provisions of the federal securities laws. A person who is a Caucasian male is objectively not a female Native American, whether he "self-identifies" as a female Native American or not.

Nasdaq Misrepresents the Economics Literature

There are strong theoretical reasons to doubt that a general mandate of a particular board composition by sex, race ethnicity, or sexual orientation would improve financial performance.

1. Most importantly, to the extent that a particular board composition is likely to improve financial performance, a company is likely to pursue that composition on its own initiative without any mandate. A company that purposely does not take advantage of talented, qualified women and minorities places itself at a competitive disadvantage and also risks anti-discrimination lawsuits, enforcement actions, and reputational damage.[27]

2. It is highly implausible that regulators will select a mandated board composition that is best for all reporting companies.[28] For example, it is highly implausible that the board composition of a retailer focusing on women's fashion or food products directed at minorities should

have the same board composition as, for example, an oil and gas exploration company or a pharmaceutical company.

This *Backgrounder* does not take a position on whether, as an empirical matter, a particular board composition measured by the sex, race, ethnicity, or sexual orientation improves or degrades corporate financial performance. Nor does it take a position on whether a particular board composition measured by other kinds of diversity (such as a director's expertise, experience, approach to business, or business philosophy, educational background, socio-economic background, ethical views, political views, integrity, geographic location, and so on) improves or degrades corporate financial performance. The empirical literature allows no such conclusion. Given the complexity and heterogeneity of modern business, it probably never will. It is, in the author's judgment, virtually certain that the proper board composition varies depending on the business—and that this decision is best left to the private sector.

Misrepresentation of the Economics Literature. Nasdaq's presentation of the empirical literature blatantly misrepresents the literature. Many of the "studies" or statements it selectively cites really rely on nothing more than unsubstantiated political preferences. The actual empirical economics literature is highly inconclusive—with most showing little or no discernable effect based on sexual, racial, or ethnic board composition. Virtually all serious surveys of the literature reach this conclusion. This should be unsurprising since sex, race, and ethnicity have nothing to do with competence.

There are a few studies that find either positive or negative effects. A thorough examination of the literature and of the materials cited in Nasdaq's submission shows that its empirical assertions have virtually no basis in the literature. Furthermore, it misrepresents the content of some of the few peer-reviewed supporting studies. Its submission to the Commission is deeply misleading.

W. Gary Simpson, David A. Carter, and Frank D'Souza found that the evidence for the business case for women directors is mixed and tends to support the view that the ability of women directors to influence profitability and shareholder value is contingent on the specific circumstances of each company.[29] Deborah L. Rhode and Amanda K. Packel, in an article sympathetic to diversity requirements, conducted a reasonably comprehensive review of the literature up to 2014 and found that "[i]n sum, the empirical research on the effect of board diversity on firm performance is inconclusive, and the results are highly dependent on methodology."[30] The

Government Accountability Office study cited by Nasdaq did a very limited survey of the research and found that "[s]ome research has found that gender diverse boards may have a positive impact on a company's financial performance, but other research has not. These mixed results depend, in part, on differences in how financial performance was defined and what methodologies were used."[31]

A 2015 systematic literature search by Jan Luca Pletzer, Romina Nikolova, Karina Karolina Kedzior, and Sven Constantin Voelpel, involving data from 20 studies on 3,097 companies published in peer-reviewed academic journals found that "the mere representation of females on corporate boards is not related to firm financial performance if other factors are not considered."[32] Alice H. Eagly in her article "When Passionate Advocates Meet Research on Diversity, Does the Honest Broker Stand a Chance?" wrote:

> To illustrate the chasm that can develop between research findings and advocates' claims, this article addresses two areas: (a) the effects of the gender diversity of corporate boards of directors on firms' financial performance[,] and (b) the effects of the gender and racial diversity of workgroups on group performance. Despite advocates' insistence that women on boards enhance corporate performance and that diversity of task groups enhances their performance, research findings are mixed, and repeated meta-analyses have yielded average correlational findings that are null or extremely small.[33]

Researchers David A. Carter, Frank P. D'Souza, Betty J. Simkins, and W. Gary Simpson did not find "a significant relationship between the gender or ethnic diversity of the board, or important board committees, and financial performance for a sample of major US corporations."[34] Jens Hagendorff and Kevin Keasey found:

> [P]ositive announcement returns to mergers approved by boards whose members are diverse in terms of their occupational background. By contrast, age and tenure diversity are associated with wealth losses surrounding acquisition announcements, while gender diversity does not lead to measurable value effects.[35]

Nuria Reguera Alvarado, Joaquina Laffarga Briones, and Pilar de Fuentes Ruiz found that "[g]ender diversity and business success are not related."[36]

Renée B. Adams and Daniel Ferreira found that "the average effect of gender diversity on firm performance is negative" and that their results suggest that mandating gender quotas for directors can reduce firm value for well-governed firms.[37] Kenneth Robinson Ahern and Amy Dittmar found

that the 2003 mandate that 40 percent of Norwegian firms' directors be women caused a significant drop in the stock price at the announcement of the law and a large decline in Tobin's Q over the following years. (Tobin's Q is, generally, the market value of a company divided by its assets' replacement cost.) The quota led to younger and less experienced boards, increases in leverage and acquisitions, and deterioration in operating performance.[38] Harald Dale-Olsen, Pal Schone, and Mette Verner published a paper in *Feminist Economics* arguing that the "impact of the [Norwegian] reform on firm performance is negligible."[39]

Daehyun Kim and Laura T. Starks found that "gender diversity in corporate boards could improve firm value because of the contributions that women make to the board by offering specific functional expertise, often missing from corporate boards. The additional expertise increases board heterogeneity," which can increase firm value.[40] Maelia Bianchi and George Latridis "found that companies with a higher proportion of women on their boards outperform those with a lower proportion in terms of return on sales and EBITDA [earnings before interest, taxes, depreciation, and amortization] margin."[41] Collins G. Ntim found that the South African stock market values diversity, but values ethnic diversity more than gender diversity.[42]

The study "Board Diversity, Firm Risk, and Corporate Policies" by Gennaro Bernile, Vineet Bhagwat, and Scott E. Yonker[43] is seriously mischaracterized by Nasdaq.[44] The study results "suggest that no single component of the diversity index drives our baseline inferences concerning the effect of aggregate board diversity." Additionally, "[i]n particular, we construct an index for demographic diversity, based on age, gender, and ethnicity, and one for cognitive diversity, based on educational background, financial expertise, and outside board experience. We then repeat the tests reported in Table 3 for each separate index. The OLS [ordinary least squares] estimates in Panel C suggest that firm risk covaries negatively with board diversity along both the demographic and cognitive dimensions."[45] In other words, the study does not support, as claimed, the Nasdaq conception of diversity.

A thorough examination of the literature and of the materials cited in Nasdaq's submission shows that its empirical assertions have virtually no basis in the literature. Its submission is deeply misrepresentative.

Correlation and Causation. In addition, Nasdaq seems not to grasp the difference between correlation and causation. Even if there were a correlation between improved financial performance and board diversity (as defined by Nasdaq)—and the empirical literature does not even come close to supporting such a conclusion—that does not imply causation. In fact, a

reasonable hypothesis is that such diversity is the corporate equivalent of a luxury good. If a firm is doing well financially, management can devote time to ancillary activities like getting good press and virtue-signaling.

SROs as Regulators

There are many so-called SROs.[46] Notable SROs include the Financial Industry Regulatory Authority (FINRA), the New York Stock Exchange (NYSE), and Nasdaq. They are regulators. Presently, SROs often are not "self" regulators since the regulated industry does not control the regulator.[47]

SROs are delegated a high degree of regulatory authority by the Commission and Congress.[48] Membership is mandatory if a firm wishes to do business, and member firms must comply with SRO rules. Member firms are subject to potentially stiff fines and other sanctions for non-compliance with SRO rules. As discussed below, many courts have held that they are therefore state actors. Others have differed. If Nasdaq is held to be a state actor acting on behalf of government, then it would be subject to the more stringent constitutional protections that limit government action. More often than not, courts hold that SROs are state actors when it is good for the SROs and ruled to the contrary when it is bad for the SROs. If an SRO is deemed a state actor, then constitutional protections apply as if the SRO were a government agency. If the SRO is not treated as a state actor, then they are subject to the same requirements as other private businesses or employers.

SROs as State Actors? In *Jackson v. Metropolitan Edison Co.*, the Supreme Court held that in determining whether the actions of a private party constitute state action, "the inquiry must be whether there is a sufficiently close nexus between the State and the challenged action of the regulated entity so that the action of the latter may be fairly treated as that of the State itself."[49] In *Blum v. Yaretsky*, the Supreme Court held that "a State normally can be held responsible for a private decision only when it has exercised coercive power or has provided such significant encouragement, either overt or covert, that the choice must in law be deemed to be that of the State.... [T]he required nexus may be present if the private entity has exercised powers that are 'traditionally the exclusive prerogative of the State.'"[50]

In an unpublished[51] 2015 opinion, the Second Circuit held that FINRA is not a state actor.[52] In a similarly unpublished 2011 opinion, the Eleventh Circuit raised (and then side-stepped) the issue by finding that even if FINRA were a state actor, FINRA had provided due process in the case being considered.[53] Courts determining whether FINRA's predecessor organizations, the National Association of Securities Dealers (NASD) (which used

to operate the NASD Automated Quotation system that became Nasdaq) and the New York Stock Exchange, were state actors were divided (although a majority found in most contexts relating to due process that they were not).[54] These cases, however, are of uncertain relevance given the differences between FINRA, NASD, or NYSE governance structures then and Nasdaq now; changes in the statutory and regulatory structure over time; and evolution in the judicial state action doctrine and the Supreme Court's separation of powers jurisprudence.

The Internal Revenue Service has found that "FINRA is a corporation serving as an agency or instrumentality of the government of the United States" for purposes of determining whether FINRA fines are deductible as a business expense.[55] A "penalty paid to a government for the violation of any law" is not deductible under Internal Revenue Code section 162(f).

Furthermore, courts have routinely held that FINRA and its predecessor organizations *are* government actors for purposes of immunity from private lawsuits against them.[56] For example, in *Standard Investment Chartered Inc. v. National Association of Securities Dealers,*[57] the Second Circuit held that

> [t]here is no question that an SRO and its officers are entitled to absolute immunity from private damages suits in connection with the discharge of their regulatory responsibilities. This immunity extends both to affirmative acts as well as to an SRO's omissions or failure to act.... It is patent that the consolidation that transferred NASD's and NYSE's regulatory powers to the resulting FINRA is, on its face, an exercise of the SRO's delegated regulatory functions and thus entitled to absolute immunity.... The statutory and regulatory framework highlights to us the extent to which an SRO's bylaws are intimately intertwined with the regulatory powers delegated to SROs by the SEC and underscore our conviction that immunity attaches to the proxy solicitation here.[58]

Like Schrödinger's cat, simultaneously dead and alive, SROs are, under current rulings, both a state actor (for purposes of barring liability and for tax purposes) and, generally, not a state actor (for purposes of absolving them of constitutional due process, equal protection, and other requirements; for Administrative Procedure Act purposes; and for other purposes).

The Proposed Rule: Inconsistent with the Principles of Equal Protection and the Civil Rights Act

This section does not pretend to be an exhaustive or authoritative discussion of the complex labyrinth of Supreme Court jurisprudence regarding

equal protection under the Fifth and Fourteenth Amendments, disparate impact, and the Civil Rights Act. It should, however, give the commission and other policymakers pause regarding three matters.

1. The legal issues raised by the proposed rule are far outside the Commission's technical competence.

2. The ethical issues raised by the proposed rule are profound.

3. Although the outcome of potential litigation is unclear, the proposed rule may well be successfully challenged in court on both constitutional and Civil Rights Act grounds.[59]

The Civil Rights Act. The Civil Rights Act of 1964 makes it an unlawful employment practice for an employer to "limit, segregate, or classify his employees or applicants for employment...because of such individual's race, color, religion, sex, or national origin." Specifically, it reads as follows:

> Unlawful Employment Practices
>
> (a) Employer practices. It shall be an unlawful employment practice for an employer—
>
> (1) to fail or refuse to hire or to discharge any individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual's race, color, religion, sex, or national origin; or
>
> (2) to limit, segregate, or classify his employees or applicants for employment in any way which would deprive or tend to deprive any individual of employment opportunities or otherwise adversely affect his status as an employee, because of such individual's race, color, religion, sex, or national origin.[60]

The Civil Rights Act also makes preferential treatment based on numbers or percentages unlawful:

> Preferential Treatment Not to be Granted on Account of Existing Number or Percentage Imbalance
>
> (j) Nothing contained in this subchapter shall be interpreted to require any employer, employment agency, labor organization, or joint labor–management committee subject to this subchapter to grant preferential treatment to any individual or to any group because of the race, color,

> religion, sex, or national origin of such individual or group on account of an imbalance which may exist with respect to the total number or percentage of persons of any race, color, religion, sex, or national origin employed by any employer, referred or classified for employment by any employment agency or labor organization, admitted to membership or classified by any labor organization, or admitted to, or employed in, any apprenticeship or other training program, in comparison with the total number or percentage of persons of such race, color, religion, sex, or national origin in any community, state, section, or other area, or in the available work force in any community, state, section, or other area.[61]

Classifying a worker as an employee or independent contractor can be notoriously difficult and different standards are used for different purposes at the federal and state level.[62] The Civil Rights Act statutory definition is effectively circular. The Equal Employment Opportunity Commission guidance provides that board members *probably* will not be deemed an employee for purposes of the Civil Rights Act.[63] In California, however, directors are explicitly deemed employees for some purposes.[64] While directors may not be deemed employees for Civil Rights Act purposes, the proposed rule certainly violates the principles of the act—and the proposed rule would most likely be a violation were directors deemed employees.

Equal Protection and Race. As discussed in the previous section, Nasdaq as a regulator may very well be deemed a state actor. Courts have so held. In that case, the equal protection provisions of the Constitution are applicable. Certainly, the Commission in its capacity as a government agency approving the Nasdaq rule is subject to those constitutional provisions. Equal protection principles apply to federal agencies and state actors delegated authority by the federal government because they have been incorporated into the due-process clause of the Fifth Amendment.[65]

The Supreme Court has held that:

- "A racial classification, regardless of purported motivation, is presumptively invalid and can be upheld only upon an extraordinary justification."[66]

- "Absent searching judicial inquiry into the justification for such race-based measures, there is simply no way of determining what classifications are 'benign' or 'remedial' and what classifications are in fact motivated by illegitimate notions of racial inferiority or simple racial politics."[67]

- "Laws that explicitly distinguish between individuals on racial grounds fall within the core of the Equal Protection Clause's prohibition against race-based decision-making."[68]

- "Racial and ethnic distinctions of any sort are inherently suspect, and thus call for the most exacting judicial examination.… There is no principled basis for deciding which groups would merit 'heightened judicial solicitude' and which would not. Courts would be asked to evaluate the extent of the prejudice and consequent harm suffered by various minority groups."[69]

- "The way to stop discrimination on the basis of race is to stop discriminating on the basis of race."[70]

Equal Protection and Sex. Similar decisions generally prohibit discrimination on the basis of sex on equal protection grounds.[71] The Supreme Court has held that "the reviewing court must determine whether the proffered justification is 'exceedingly persuasive.'… The justification must be genuine, not hypothesized or invented post hoc in response to litigation. And it must not rely on overbroad generalizations about the different talents, capacities, or preferences of males and females."[72] The Supreme Court recently extended Title VII protections to gay and transgender persons by holding that discrimination based on homosexuality or transgender status necessarily entails discrimination based on sex.[73]

Racism and Sexism: The Proposed Rule Is a Moral Step Backwards

> I have a dream that my four little children will one day live in a nation where they will not be judged by the color of their skin but by the content of their character.[74]
>
> —Martin Luther King, Jr.

> Sex, like race, is a visible, immutable characteristic bearing no necessary relationship to ability.[75]
>
> —Ruth Bader Ginsburg (in oral argument as an attorney in *Frontiero v. Richardson*)

> The Constitution abhors classifications based on race, not only because those classifications can harm favored races or are based on illegitimate motives, but also because every time the government places citizens on racial registers and makes race relevant to the provision of burdens or benefits, it demeans us all. Purchased at the price of immeasurable human suffering, the equal protection principle reflects our Nation's understanding that such classifications ultimately have a destructive impact on the individual and our society.[76]
>
> —Justice Clarence Thomas (*Grutter v. Bollinger)*

Racism: A belief that race is a fundamental determinant of human traits and capacities.[77]

Sexism: Prejudice or discrimination based on sex; behavior, conditions, or attitudes that foster stereotypes of social roles based on sex.[78]

The proposed rule is racist and sexist in that it mandates that firms establish quotas and discriminate based on sex, skin color, ethnicity, or sexual orientation rather than making determinations based on individual achievement, talent, experience, or competence. It defines diversity entirely in terms of these immutable characteristics—instead of the myriad of other kinds of diversity such as a director's achievement, expertise, experience, approach to business or business philosophy, educational background, socio-economic background, ethical views, political views, integrity, geographic location, and so on.

Morally, it represents a marked step backwards. It is rejection of the principle that people should be judged on the content of their character and their individual achievement rather than their sex, race, national origin, ethnicity, or sexual orientation. It is rejection of the principle that people should be judged as individuals rather than as members of a racial or sexual group. It is a rejection of the principle of equal protection under the law (or, in this case, regulations promulgated under law). It is a rejection of the principle that we are all created equal. Legal discrimination or quotas on the basis of race or sex should be a relic of the past.

Faux Diversity. The type of diversity created by the proposed rule would be faux diversity—skin deep, if you will. It is a rejection of the kind of diversity that is most likely to enable a business to understand the true diversity of the American people and actually be relevant to business profitability, such as a director's achievement, expertise, experience, approach to business or business philosophy, educational background, socio-economic background, ethical views, political views,[79] integrity, or geographic location. There is also strong reason to believe that those chosen under such a rule

but who "self-identify" as women, a designated minority, or LGBTQ+ will have been educated in the same handful of schools and come from the same coastal urban centers as most existing directors.

The Proposed Rule Rests on a Faulty Premise

The Nasdaq proposed rule rests on a faulty premise. Nasdaq falsely asserts that shareholders demand the corporations that they own discriminate on the basis of sex, race, ethnicity, or sexual orientation. Shareholders are free to instruct management to do so or to pursue other ESG or social justice objectives via shareholder resolution. When afforded the opportunity to do so, they very rarely do.[80] None of the seven proposals on the subject that went to votes in 2019 earned more than 3 percent of the vote.[81] A very high percentage of the shareholder proposals submitted are submitted by government pension funds in their capacity as shareholders for political purposes.[82]

Of course, entrepreneurs are today free to form benefit corporations or benefit limited liability companies (LLCs) that under state laws permit a business to serve a social purpose, as well as the purpose of making a profit, rather than form a traditional business that is organized only to earn a return for its owners. But relatively few businesses are so organized and relatively little investor capital flows to benefit corporations or LLCs. Individuals are free to invest in these companies, but fiduciaries have no business investing others' money in such enterprises absent an *explicit* indication that investors agree with the social goals of the enterprise and are willing to accept a lower rate of return.[83]

Mutual funds and exchange traded funds devoted to socially responsible investing are growing. Because these are voluntary and the terms of the investment are fully disclosed, this is perfectly fine. But such funds are still a very minor share of overall investment because most investors are unwilling to sacrifice returns to achieve "social justice" objectives.

The True Agenda: Remaking the Purpose of Business

This section is a very abbreviated discussion of the many issues regarding the purpose of business, theories of the corporation, corporate social responsibility, and so on. Traditionally, the purpose of businesses has been to earn a return for its owners by cost-effectively combining the capital and entrepreneurial spirit of its founders and owners with the labor and

talent of its employees in a competitive environment to satisfy the wants and needs of its customers. The relationship between owners, management, workers, suppliers, and customers are—subject to certain broad constraints imposed by law—privately decided and voluntary.

With increasing stridency, there is a major effort under way to redefine the purpose of businesses to achieve various social or political objectives unrelated to earning a return, satisfying customers, or treating workers or suppliers fairly. This is being done under the banner of social justice, CSR, stakeholder theory, ESG criteria, SRI, sustainability, diversity, business ethics, common-good capitalism, or corporate actual responsibility.[84]

If successful, these attempts to redefine the purpose of business as the pursuit of ESG or social justice objectives will have marked adverse social consequences. Management will be even less accountable to anyone.[85] To the extent that firms make decisions based on considerations other than cost-effectively meeting the needs and wants of their customers, their costs will increase, and they will become less productive and less competitive. Either returns will decline, wages will stagnate, prices will increase, or the quality of the goods and services they provide will decline (which is effectively a price increase). Because wages are closely tied to productivity over time, wages will grow more slowly or stagnate. As firms become less competitive, jobs will be lost. The value of the retirement accounts of millions of people will be adversely affected. Similarly, the pensions of millions more that are funded by returns on equity investments will be endangered.

Less Management Accountability

In large, modern corporations there is a separation of ownership and control. There is a major agent–principal problem because management and the board of directors often, to varying degrees, pursue their own interest rather than the interests of shareholders. Profitability is, however, a fairly clear measure of the success or failure of management and the board. If a firm becomes unprofitable or lags considerably in profitability, the board may well replace management, shareholders may replace the board, or another firm may attempt a takeover.

Systematic implementation of regulatory ESG or CSR requirements would make management dramatically less accountable since they would come at the expense of profitability, but the metrics relating to success or failure of achieving ESG or CSR requirements would be largely unquantifiable. For that matter, ESG or CSR requirements themselves tend to be amorphous and ever-changing. The same is true

for "stakeholder capitalism." How and on what basis is management's allocation of resources to various stakeholders to be assessed? The entire effort would make businesses more akin to government or not-for-profit enterprises.

The Social Welfare Cost of ESG Requirements

The broader social costs associated with ESG requirements can, in principle, be quantified. This section provides an analytical framework that may be useful in analyzing the social welfare costs of ESG requirements.

To the extent ESG objectives are not pursued by businesses for the purpose of making a profit, $R > R_{ESG/CSR}$, where R is the rate of return on investment in the absence of ESG, CSR, sustainability requirements, diversity requirements, or stakeholder theory implementation, and $R_{ESG/CSR}$ is the rate of return after implementation of those requirements. The difference, $R - R_{ESG/CSR}$, is economically analogous to a tax. It is a reduction in return due to the pursuit of ESG objectives. Thus, $R - R_{ESG/CSR} = Tax_{ESG/CSR}$. This means that various techniques used in public finance to analyze the social welfare impact of taxes may be used to quantitatively analyze the social welfare cost of these provisions (i.e., $Tax_{ESG/CSR}$).

A tax has an excess burden or deadweight loss that can be calculated.[86] By introducing a wedge ($Tax_{ESG/CSR}$) between, in this case, the gross return and the net return, ESG/CSR reduces the size of the capital market and therefore output and employment. In a well-functioning market, the price of a capital asset should be equal to the present value of the expected future income stream generated by the asset net of taxes and depreciation.[87] Introducing a new tax (in this case $Tax_{ESG/CSR}$) would reduce the expected future income stream, and therefore, the price of the asset. It would also cause investment to flow out of the affected sector or jurisdiction.

Who bears the actual economic burden of the corporate income tax is an open question.[88] The analysis of who bears the burden of $Tax_{ESG/CSR}$ would be the same. One thing is certain: It cannot be corporations. A corporation is a legal fiction, and legal fictions do not pay taxes—people pay taxes. The corporate tax could be borne by corporate shareholders in the form of lower returns;[89] owners of all capital (again in the form of lower returns);[90] corporate customers in the form of higher prices;[91] or employees (in the form of lower wages).[92] It is, almost certainly, some combination of these.[93] The economics profession has changed its thinking on this issue several times over the past four decades, but the latest —and highly plausible —consensus is that workers probably bear *more than half* of the burden of the corporate income tax because capital is highly mobile.[94] Labor's share of the corporate

tax burden is potentially as high as three-quarters.[95] Shareholders (investors) probably bear most of the remainder.[96] Initially (i.e., in the short run), the impact on shareholder returns would be greater. Adjustments take time. In the long run, ESG requirements ($Tax_{ESG/CSR}$) would have a disproportionately negative impact on labor due to capital factor mobility.

Federalizing Corporate Governance

Traditionally, corporate governance is a function of state law and private decision-making. The Nasdaq rule is one more large step toward the federalization of corporate governance. Jurisdictional competition and freedom of action by private actors is much more likely to lead to desirable outcomes than one-size-fits-all mandates by national regulators.[97]

Diversity Statistical Reporting

If the Commission decides to mandate (or allow SROs to mandate) diversity reporting greater than what is currently required under Regulation S-K,[98] then it should require reporting on the many kinds of diversity that are important to business success, not merely the race, ethnic origin, sex, and sexual orientation of its board members. Diversity reporting should include:

1. Experience (job titles, responsibilities and functions, notable achievements);

2. Other board positions held (in the past and currently);

3. Industries worked in;

4. Education (degrees conferred, subject matter studied, schools attended, and school locations);

5. Professional certifications, accreditations, and awards;

6. Relevant cultural, charitable, policy, public service, or similar activities;

7. Geographic location of residence and business (country, state, region, and city); and

8. Other factors considered by the corporation when selecting the board member.

Conclusion

The Nasdaq proposed rule on board diversity has no basis in the economics literature. This should be unsurprising because sex, sexual orientation, race, and ethnicity have nothing to do with competence. Nasdaq's claim that the economics literature supports the proposed rule is a blatant misrepresentation of the economics literature.

The proposed rule represents a marked step back morally, as it requires discrimination on the basis of sex, race, ethnicity, and sexual orientation. It is, at a minimum, a violation of the principles of the Civil Rights Act of 1964 and the equal protection clause of the Fourteenth Amendment. With respect to the SEC, which must approve or disapprove the rule, there is a strong possibility that the courts would rule that it is a violation. With respect to Nasdaq, it would depend on whether the courts held Nasdaq to be a state actor in its regulatory capacity and whether board members were held to be employees for Civil Rights Act purposes. Many courts have held SROs to be state actors in various contexts.

The proposed rule is inconsistent with the Commission's mission and its statutory charge. The proposed rule neither protects investors, nor promotes the maintenance of fair, orderly, and efficient markets, nor facilitates capital formation.

The Nasdaq proposed rule rests on a faulty premise. Nasdaq falsely asserts that shareholders are demanding the corporations they own discriminate on the basis of sex, race, ethnicity, or sexual orientation. Shareholders are free to instruct management to do so or to pursue other ESG or social justice objectives via shareholder resolutions. When afforded the opportunity to do so, however, they rarely do.

Nasdaq also embraces the stakeholder theory of business purpose in which shareholders—rather than being treated as the owners of the business—are reduced to just one more corporate interest group to be placated by a powerful and largely unaccountable management.

The true agenda of social justice advocates—apparently including Nasdaq management—is to remake the purpose of business. Traditionally, the purpose of a business has been to earn a return for its owners

by cost-effectively combining the capital and entrepreneurial spirit of its founders and owners with the labor and talent of its employees in a competitive environment to satisfy the wants and needs of its customers. The relationship between owners, management, workers, suppliers, and customers are, subject to certain broad constraints imposed by law, privately decided and voluntary.

With increasing stridency, there is a major effort under way to redefine the purpose of businesses to achieve various social or political objectives unrelated to earning a return, satisfying customers, or treating workers or suppliers fairly. If successful, these attempts to redefine the purpose of business will have marked adverse social consequences. Management will be even less accountable to anyone since the metrics of success will become highly amorphous and constantly changing. Businesses will become less productive and less competitive. Jobs will be lost, and wages will grow more slowly. The social welfare cost of going down this road would be considerable.

The proposed rule is also one more major step toward the one-size-fits-all federalization of corporate governance. Last, if the SEC chooses to countenance diversity statistical reporting, it should require reporting of types of diversity that are more relevant to business success than the immutable racial, ethnic or sexual characteristics of its directors.

The Securities and Exchange Commission should disapprove this proposed Nasdaq rule change. If the Commission does not do so, then Congress should prohibit securities regulations—including those promulgated by SROs—that discriminate on the basis of race, ethnicity, or sex.

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Endnotes

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8. Ibid.
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10. Ibid.
11. Ibid.
12. 15 U.S. Code § 78s(b)(2)(B). See also 17 Code of Federal Regulations § 240.19b-4 (2020).
13. U.S. Securities and Exchange Commission, "What We Do," http://www.sec.gov/about/whatwedo.shtml#intro (accessed February 22, 2021). The statutory charge is: "Whenever pursuant to this title the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation." See Securities Exchange Act of 1934, Public Law No. 73–291, § 3(f), and Securities Act of 1933, Public Law No. 73–22, § 2(b). See also U.S. Senate Banking Committee, letter to the SEC, February 12, 2021, https://www.banking.senate.gov/imo/media/doc/NASDAQ_LETTER.pdf (accessed February 22, 2021).
14. Public Law No. 88–352. See especially § 703 (42 U.S. Code § 2000e-2), and *Watson v. Fort Worth Bank & Trust*, 487 U.S. 977 (1988).
15. See discussion below, under the heading "The Proposed Rule: Inconsistent with Equal Protection and the Civil Rights Act."
16. See, for example, *Regents of Univ. of California v. Bakke*, 438 U.S. 265 at 291, 296 (1978); *Grutter v. Bollinger*, 539 U.S. 306 at 309 and 334 (2003); *Ricci v. DeStefano*, 557 U.S. 557 (2009) (Title VII prohibits intentional acts of employment discrimination based on race, color, religion, sex, and national origin.); *Richmond v. J. A. Croson Co.*, 488 U. S. 469 (1989); and *Wygant v. Jackson Bd. of Education*, 476 U. S. 267 (1986).
17. See "What is Critical Race Theory?," in Richard Delgado and Jean Stefancic, *Critical Race Theory: An Introduction*, 3rd ed. (New York: New York University Press, 2017), p. 3, and Kevin R. Johnson, "Richard Delgado's Quest for Justice for All," *Law & Inequality: A Journal of Theory and Practice*, Vol. 33, No. 2 (2015) https://scholarship.law.umn.edu/cgi/viewcontent.cgi?article=1213&context=lawineq (accessed February 22, 2021) ("A brief, simple commentary cannot do justice to Delgado's pioneering legal scholarship —he is nothing less than a legend, a sort of LeBron James or Michael Jordan among legal academics."). See also Jonathan Butcher and Mike Gonzalez, "Critical Race Theory, the New Intolerance, and Its Grip on America," Heritage Foundation *Backgrounder* No. 3567, December 7, 2020, https://www.heritage.org/sites/default/files/2020-12/BG3567.pdf.
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20. Each of these terms (with the possible exception of the latter two, which are of comparatively recent vintage), has evolved in meaning over time and has substantially—even dramatically—different meanings depending on the author or speaker. There is a voluminous literature discussing—but seldom *defining*—these concepts. In the case of "social justice," the term has changed meaning with the political and social situation for two centuries. In contemporary political parlance, it is associated with ideologies that are, at the very least, deeply suspicious of market outcomes and that countenance a high degree of government intervention in the economy. Often, it is a proxy term for Social Democratic or socialist views on economics and critical race theory on social issues. Its economic dimension rests on the premise that a pre-determined distribution of goods should be enforced by the state. This is a substantially different conception of justice than most, which rely

on evaluating individual actions, merit, and desert. This *Backgrounder* does not address the details of these various ideas. Nasdaq's discussion in its proposed rule submission is typical. It opines about how important "social justice" is (and "stakeholders" are) as the motivation for the proposed rule. Yet it fails to actually discuss what social justice is or to define "stakeholder"—let alone offering suggestions on how boards or management would weigh the claims of competing "stakeholders" or the implications of these concepts for shareholders and society at large. To Nasdaq, social justice and stakeholders are buzzwords or fuzzwords that count as virtue-signaling for Nasdaq management. For a selection of recent, and more serious, discussions of these concepts from both critical and supportive perspectives, see Gonzalez, *The Plot to Change America*; Peter W. Wood, *Diversity Rules* (New York: Encounter Books, 2019); Brian Barry, *Why Social Justice Matters* (Cambridge: Polity Press, 2005); Michael Novak, Paul Adams, and Elizabeth Shaw, *Social Justice Isn't What You Think It Is* (New York: Encounter Books, 2015); David Miller, *Principles of Social Justice*, revised ed. (Cambridge: Harvard University Press, 2001); Thomas Patrick Burke, *The Concept of Justice: Is Social Justice Just?* (New York: Bloomsbury Academic, 2011); and Friedrich A. von Hayek, "The Atavism of Social Justice," in Friedrich A. von Hayek, *New Studies in Philosophy, Politics, Economics and the History of Ideas*, chapter 5 (Abingdon-on-Thames: Routledge, 1978). For historical context, see Leonard Trelawny, *The Elements of Social Justice* (London: George Allen & Unwin, 1922), and John Bates Clark, *Social Justice Without Socialism* (Boston: Houghton Mifflin, 1914).

21. See the section below, headed "The Social Welfare Cost of ESG Requirements."
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26. See U.S. Securities and Exchange Commission, "Regulation S-K, Questions and Answers of General Applicability," September 21, 2020, https://www.sec.gov/divisions/corpfin/guidance/regs-kinterp.htm#116-11 (accessed February 22, 2021).

> Question 116.11
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> Question: In connection with preparing Item 401 disclosure relating to director qualifications, certain board members or nominees have provided for inclusion in the company's disclosure certain self-identified specific diversity characteristics, such as their race, gender, ethnicity, religion, nationality, disability, sexual orientation, or cultural background. What disclosure of self-identified diversity characteristics is required under Item 401 or, with respect to nominees, under Item 407?
>
> Answer: Item 401(e) requires a brief discussion of the specific experience, qualifications, attributes, or skills that led to the conclusion that a person should serve as a director. Item 407(c)(2)(vi) requires a description of how a board implements any policies it follows with regard to the consideration of diversity in identifying director nominees. To the extent a board or nominating committee in determining the specific experience, qualifications, attributes, or skills of an individual for board membership has considered the self-identified diversity characteristics referred to above (e.g., race, gender, ethnicity, religion, nationality, disability, sexual orientation, or cultural background) of an individual who has consented to the company's disclosure of those characteristics, we would expect that the company's discussion required by Item 401 would include, but not necessarily be limited to, identifying those characteristics and how they were considered. Similarly, in these circumstances, we would expect any description of diversity policies followed by the company under Item 407 would include a discussion of how the company considers the self-identified diversity attributes of nominees as well as any other qualifications its diversity policy takes into account, such as diverse work experiences, military service, or socio-economic or demographic characteristics. [February 6, 2019]

U.S. Securities and Exchange Commission, "Section 134, Item 501," September 21, 2020, https://www.sec.gov/divisions/corpfin/guidance/regs-kinterp.htm#133-13 (accessed February 22, 2021).

> Question 133.13
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> Question: In connection with preparing Item 401 disclosure relating to director qualifications, certain board members or nominees have provided for inclusion in the company's disclosure certain self-identified specific diversity characteristics, such as their race, gender, ethnicity, religion, nationality, disability, sexual orientation, or cultural background. What disclosure of self-identified diversity characteristics is required under Item 401 or, with respect to nominees, under Item 407?

Answer: Item 401(e) requires a brief discussion of the specific experience, qualifications, attributes, or skills that led to the conclusion that a person should serve as a director. Item 407(c)(2)(vi) requires a description of how a board implements any policies it follows with regard to the consideration of diversity in identifying director nominees. To the extent a board or nominating committee in determining the specific experience, qualifications, attributes, or skills of an individual for board membership has considered the self-identified diversity characteristics referred to above (e.g., race, gender, ethnicity, religion, nationality, disability, sexual orientation, or cultural background) of an individual who has consented to the company's disclosure of those characteristics, we would expect that the company's discussion required by Item 401 would include, but not necessarily be limited to, identifying those characteristics and how they were considered. Similarly, in these circumstances, we would expect any description of diversity policies followed by the company under Item 407 would include a discussion of how the company considers the self-identified diversity attributes of nominees as well as any other qualifications its diversity policy takes into account, such as diverse work experiences, military service, or socio-economic or demographic characteristics.

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47. William A. Birdthistle and M. Todd Henderson, "Becoming a Fifth Branch," *Cornell Law Review*, Vol. 99, No. 1 (2013), pp. 1–69, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2172935 (accessed February 22, 2021) ("SROs have been losing their independence, growing distant from their industry members, and accruing rulemaking, enforcement, and adjudicative powers that more closely resemble governmental agencies such as the Securities and Exchange Commission and the Commodity Futures Trading Commission.... This process by which these self-regulatory organizations shed their independence for an increasingly governmental role is highly undesirable from an array of normative viewpoints. For those who are skeptical of governmental regulation, deputizing private bodies to increase governmental involvement is clearly problematic."); Andrew F. Tuch, "The Self-Regulation of Investment Bankers," *George Washington Law Review*, Vol. 83, No. 1 (December 2014), pp. 101–175, http://www.gwlr.org/wp-content/uploads/2015/03/83-Geo-Wash-L-Rev-101.pdf (accessed February 22, 2021); Hester Peirce, "The Financial Industry Regulatory Authority: Not Self-Regulation after All," Mercatus Center *Working Paper*, January 2015, https://www.mercatus.org/system/files/Peirce-FINRA_0.pdf (accessed February 22, 2021); and Daniel M. Gallagher, "Market 2012: Time for a Fresh Look at Equity Market Structure and Self-Regulation," U.S. Securities and Exchange Commission, October 4, 2012, https://www.sec.gov/News/Speech/Detail/Speech/1365171491376 (accessed February 22, 2021). Occupation licensing is often controlled by SROs or quasi-governmental organizations. On occupation licensing generally as a barrier to entry, see White House, "Occupational Licensing: A Framework for Policymakers," July 2015, https://obamawhitehouse.archives.gov/sites/default/files/docs/licensing_report_final_nonembargo.pdf (accessed February 22, 2021), and Dick M. Carpenter et al., "*License to Work: A National Study of Burdens from Occupation Licensing*," Institute for Justice, May 2012, https://www.ij.org/images/pdf_folder/economic_liberty/occupational_licensing/licensetowork.pdf (accessed February 22, 2021).
48. David R. Burton, "Reforming FINRA," Heritage Foundation *Backgrounder* No. 3181, February 1, 2017, https://www.heritage.org/sites/default/files/2017-02/BG3181.pdf; Roberta S. Karmel, "Should Securities Industry Self-Regulatory Organizations Be Considered Government Agencies?" *Stanford Journal of Law, Business & Finance*, Vol. 14, No. 1 (Fall 2008), http://brooklynworks.brooklaw.edu/cgi/viewcontent.cgi?article=1376&context=faculty (accessed February 22, 2021); Peirce, "The Financial Industry Regulatory Authority: Not Self-Regulation After All"; Jonathan Macey and Caroline Novogrod, "Enforcing Self-Regulatory Organization's Penalties and the Nature of Self-Regulation," *Hofstra Law Review*, Vol. 40 (2012), pp. 963–1003, https://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=5671&context=fss_papers (accessed February 22, 2021); and Luis A. Aguilar, "The Need for Robust SEC Oversight of SROs," U.S. Securities and Exchange Commission, May 8, 2013, https://www.sec.gov/News/PublicStmt/Detail/PublicStmt/1365171515546 (accessed February 22, 2021).
49. *Jackson v. Metropolitan Edison Co.*, 419 U.S. 345, 351, 95 S.Ct. 449, 42 L.Ed.2d 477 (1974).
50. *Blum v. Yaretsky*, 457 U.S. 991, 1004-05, 102 S.Ct. 2777, 73 L.Ed.2d 534 (1982).
51. See Federal Rules of Appellate Procedure (FRAP) 32.1, and John Szmer, Robert K. Christensen, and Ashlyn Kuersten, "The Efficiency of Federal Appellate Decisions: An Examination of Published and Unpublished Opinions," *The Justice System Journal*, Vol. 33, No. 3 (2012), p. 319, http://spia.uga.edu/faculty_pages/rc/law_pa_files/Pub12_JSJ_EfficiencyFedAppCourts.pdf (accessed February 22, 2021) (finding that three-quarters of federal appellate decisions are now unpublished [unreported] and given that FRAP 32.1, after January 1, 2007, allows attorneys to cite opinions "designated as 'unpublished,' 'not for publication,' 'non-precedential,' 'not precedent,' or the like, unpublished opinions are of greater importance).
52. *Santos-Buch v. Financial Industry Regulatory Authority, Inc.*, U.S. Court of Appeals for the Second Circuit, No. 14-2767-cv, January 30, 2015, unpublished opinion (accessed February 22, 2021).
53. *Busacca v. S.E.C*, U.S. Court of Appeals for the Eleventh Circuit, No. 10-15918, December 28, 2011, unpublished opinion, https://www.sec.gov/litigation/opinions/2010/34-63312-appeal.pdf (accessed February 22, 2021).
54. *D'Alessio v. S.E.C.*, 380 F.3d 112, 120 n.12 (2d Cir. 2004) (discussing whether the NASD is a state actor, but asserting that a determination of that issue was not necessary in that case); *D.L. Cromwell Investments v. NASD Regulation*, 279 F.3d 155 (2d Cir. 2002) (finding that NASD is not a state actor); *Desiderio v. NASD*, 191 F.3d 198, 206 (2d Cir. 1999) (finding that NASD is not a state actor but recognizing that "private entities may be held to constitutional standards if their actions are 'fairly attributable' to the state"); *Gold v. SEC*, 48 F.3d 987 (7th Cir. 1995) (finding that due process was provided and side-stepping the state action issue); and *Intercontinental Industries, Inc. v. American Stock Exchange*, 452 F.2d 935 (5th Cir. 1971) ("The intimate involvement of the [American Stock] Exchange with the Securities and Exchange Commission brings it within the purview of the Fifth Amendment controls over governmental due process."). The American Stock Exchange was acquired by the New York Stock Exchange in 2008 and since 2012 has been called NYSE MKT. See also *Saad v. SEC*, 718 F. 3d 904 (DC Cir. 2013) (finding that the commission abused its discretion in failing to address several potentially mitigating factors when upholding a FINRA lifetime bar).
55. Office of Chief Counsel, Memorandum No. 201623006, Internal Revenue Service, June 3, 2016, http://brokeandbroker.com/PDF/IRSFINRAFines.pdf (accessed February 22, 2021).

56. "The NYSE, as a[n] SRO, stands in the shoes of the SEC in interpreting the securities laws for its members and in monitoring compliance with those laws. It follows that the NYSE should be entitled to the same immunity enjoyed by the SEC when it is performing functions delegated to it." See *D'Alessio v. New York Stock Exchange, Inc.*, 258 F.3d 93 (2d Cir. 2001). See also *Sparta Surgical Corp. v. National Association of Securities Dealers, Inc.*, 159 F.3d 1209 (9th Cir. 1998), and *Weissman v. Nat'l Association of Securities Dealers, Inc.*, 500 F.3d 1293 (11th Cir. 2007).
57. 637 F.3d 112 (2d Cir. 2011), cert. denied January 17, 2012.
58. Ibid. (Emphasis added.)
59. *Watson v. Fort Worth Bank & Trust*, 487 U.S. 977, 992 (1988) ("We agree that the inevitable focus on statistics in disparate impact cases could put undue pressure on employers to adopt inappropriate prophylactic measures. It is completely unrealistic to assume that unlawful discrimination is the sole cause of people's failing to gravitate to jobs and employers in accord with the laws of chance. It would be equally unrealistic to suppose that employers can eliminate, or discover and explain, the myriad of innocent causes that may lead to statistical imbalances in the composition of their workforces" [internal citations omitted].).
60. Section 703 of the Civil Rights Act of 1964, 42 U.S. Code § 2000e-2.
61. 42 U.S. Code § 2000e–2(j).
62. David R. Burton, "A Guide to Labor and Employment Law Reforms," Heritage Foundation *Backgrounder* No. 3535, October 9, 2020, https://www.heritage.org/sites/default/files/2020-10/BG3535.pdf. See especially the "Independent Contractors" section.
63. Equal Employment Opportunity Commission, "Compliance Manual on 'Threshold Issues,'" § 2-III(A)(1)(d), https://www.eeoc.gov/laws/guidance/section-2-threshold-issues#2-III-A-1-d (accessed February 22, 2021) ("In most circumstances, individuals who are partners, officers, members of boards of directors, or major shareholders will not qualify as employees.").
64. Cal. Labor Code § 3351(c) (The definition of employee includes "[a]ll officers and members of boards of directors of quasi-public or private corporations while rendering actual service for the corporations for pay.").
65. *Bolling v. Sharpe*, 347 U.S. 497 (1954), and *Adarand Constructors, Inc. v. Pena*, 515 U.S. 200 (1995). See also *Buckley v. Valeo*, 424 U.S. 1 (1976).
66. *Shaw v. Reno*, 509 U.S. 630, 643-644 (1993). See also *Brown v. Board of Education of Topeka*, 347 U.S. 483 (1954); *Loving v. Virginia*, 388 U.S. 1 (1967), and *Personnel Administrator of Mass. v. Feeney*, 442 U.S. 256, 272 (1979).
67. *Richmond v. J. A. Croson Co.*, 488 U. S. 469, 493 (1989).
68. *Miller v. Johnson*, 515 U.S. 900, 905 (1995).
69. *Regents of Univ. of California v. Bakke*, 438 U.S. 265 at 291, 296 (1978).
70. *Parents Involved in Community Schools v. Seattle School District No. 1*, 551 U.S. 701, 748 (2007), https://www.supremecourt.gov/opinions/boundvolumes/551bv.pdf (accessed February 22, 2021).
71. *Reed v. Reed*, 404 U.S. 71 (1971); *Frontiero v. Richardson*, 411 U.S. 677, 688 (1973) ("classifications based upon sex, like classifications based upon race, alienage, and national origin, are inherently suspect and must therefore be subjected to close judicial scrutiny."); *Weinberger v. Wiesenfeld*, 420 U.S. 636 (1975); *Craig v. Boren*, 429 U.S. 190 (1976); *Califano v. Goldfarb*, 430 U.S. 199 (1977); *Kirchberg v. Feenstra*, 450 U. S. 455 (1981); *United States v. Virginia*, 518 U.S. 515 (1996); and *Nevada Department of Human Resources v. Hibbs*, 538 U.S. 721 (2003).
72. *United States v. Virginia*, 518 U.S. 515, 533 (1996).
73. *Bostock v. Clayton County*, 590 U.S. ___ (2020), https://www.supremecourt.gov/opinions/19pdf/17-1618_hfci.pdf (accessed February 22, 2021) ("discrimination based on homosexuality or transgender status necessarily entails discrimination based on sex.... In Title VII, Congress adopted broad language making it illegal for an employer to rely on an employee's sex when deciding to fire that employee.... We do not hesitate to recognize today a necessary consequence of that legislative choice: An employer who fires an individual merely for being gay or transgender defies the law.")
74. Martin Luther King, Jr., "I Have a Dream," address delivered August 28, 1963, https://kinginstitute.stanford.edu/king-papers/documents/i-have-dream-address-delivered-march-washington-jobs-and-freedom (accessed February 22, 2021).
75. Katherine Franke, "Symposium: The Liberal, Yet Powerful, Feminism of Ruth Bader Ginsburg," October 9, 2020, https://www.scotusblog.com/2020/10/symposium-the-liberal-yet-powerful-feminism-of-ruth-bader-ginsburg/ (accessed February 22, 2021), and Robert Cohen and Laura J. Dull, "Supplemental Online Material for 'Teaching About the Feminist Rights Revolution': Ruth Bader Ginsburg as 'The Thurgood Marshall of Women's Rights,'" November 2017, https://tah.oah.org/november-2017/supplemental-online-material-for-teaching-about-the-feminist-rights-revolution-ruth-bader-ginsburg-as-the-thurgood-marshall-of/ (accessed February 22, 2021).
76. *Grutter v. Bollinger*, 539 U. S. 306, 353 (2003), Thomas opinion (concurring in part and dissenting in part), https://www.supremecourt.gov/opinions/boundvolumes/539bv.pdf (accessed February 22, 2021).
77. Merriam-Webster Online, "Racism," https://www.merriam-webster.com/dictionary/racism (accessed February 22, 2021).
78. Ibid.

79. It is probably not advisable to require reporting on the political ideology or the party affiliation of board members and management: The country is politicized enough. But the one study that the author found on the subject appears to show a strong, statistically robust positive impact of political heterogeneity of boards on firm performance. Incheol Kim, Christos Pantzalis, and Jung Chul Park, "Corporate Boards' Political Ideology Diversity and Firm Performance," *Journal of Empirical Finance*, Vol. 21 (2013), https://ssrn.com/abstract=2055800 (accessed February 22, 2021).
80. See, e.g., *Proxy Preview, 2020*.
81. Ibid. at p. 66.
82. For example, see Scott M. Stringer, "Boardroom Accountability Project," and Ramonas, "Illinois Treasurer Urges SEC to Adopt Diversity Mandates."
83. David R. Burton, comment letter to Jeanne Wilson (regarding Financial Factors in Selecting Plan Investments), July 30, 2020, https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95/00595.pdf (accessed February 22, 2021), and David R. Burton, comment letter to Jeanne K. Wilson (regarding Fiduciary Duties Regarding Proxy Voting and Shareholder Rights), October 5, 2020, https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB91/00232.pdf (accessed February 22, 2021).
84. See footnote 20 above.
85. See next section.
86. Arnold C. Harberger, "The Incidence of the Corporation Income Tax," *Journal of Political Economy* (June 1962), pp. 215–240; Alan J. Auerbach and James R. Hines, "Taxation and Economic Efficiency," in Martin Feldstein and A. J. Auerbach, eds., *Handbook of Public Economics* (Amsterdam: North Holland, 2002); and John Creedy, "The Excess Burden of Taxation and Why It (Approximately) Quadruples When the Tax Rate Doubles," New Zealand Treasury *Working Paper* No. 03/29, December 2003, https://treasury.govt.nz/sites/default/files/2007-10/twp03-29.pdf (accessed February 22, 2021). See also, for example, N. Gregory Mankiw, *Principles of Economics*, 4th ed. (Boston: Cengage Learning, 2006), chapter 8 (or many other textbooks on price theory, microeconomics, or principles of economics).
87. See Robert E. Hall and Dale Jorgenson, "Tax Policy and Investment Behavior," *American Economic Review*, Vol. 57, No. 3 (June 1967), pp. 391–414. This section covers the basic user cost of capital analysis with taxes. See also Dale W. Jorgenson, *Investment: Capital Theory and Investment Behavior* (Cambridge, MA: MIT Press, 1996), and John Creedy and Norman Gemmell, "Taxation and the User Cost of Capital: An Introduction," New Zealand Treasury *Working Paper* No. 04/2015, March 2015, https://www.wgtn.ac.nz/cpf/publications/pdfs/2015-pubs/WP04_2015_Taxation-and-User-Cost.pdf (accessed February 22, 2021).
88. In the economics literature, this question is usually phrased as, "What is the incidence of the corporate income tax?"
89. Government estimators are among the few who cling to the view that shareholders bear most of the burden. Joint Committee on Taxation, "Modeling the Distribution of Taxes on Business Income," JCX–14–13, October 16, 2013, https://www.jct.gov/publications.html?func=download&id=4528&chk=4528&no_html=1 (accessed February 22, 2021) (25 percent labor), and Julie Anne Cronin et al., "Distributing the Corporate Income Tax: Revised U.S. Treasury Methodology," *National Tax Journal*, March 2013, https://www.ntanet.org/NTJ/66/1/ntj-v66n01p239-62-distributing-corporate-income-tax.pdf (18 percent labor) (accessed February 22, 2021).
90. The non-corporate sector can be affected because competition will eventually cause wages, prices, and after-tax returns in the corporate *and* non-corporate sectors to be the same. For a more detailed explanation, see Arnold C. Harberger, "The Incidence of the Corporation Income Tax," *Journal of Political Economy*, Vol. 70, No. 3 (June 1962), pp. 215–240.
91. The focus of the economics profession to date has been almost exclusively the impact on capital and labor rather than customers.
92. Arnold C. Harberger, "The ABCs of Corporation Tax Incidence: Insights into the Open-Economy Case," in *Tax Policy and Economic Growth* (Washington, DC: American Council for Capital Formation, 1995); Arnold C. Harberger, "The Incidence of the Corporation Income Tax Revisited," *National Tax Journal*, Vol. 61, No. 2 (June 2008), pp. 303–312, http://www.ntanet.org/NTJ/61/2/ntj-v61n02p303-12-incidence-corporation-income-tax.pdf (accessed February 22, 2021); Matthew H. Jensen and Aparna Mathur, "Corporate Tax Burden on Labor: Theory and Empirical Evidence," *Tax Notes*, June 6, 2011, https://www.aei.org/wp-content/uploads/2011/06/Tax-Notes-Mathur-Jensen-June-2011.pdf (accessed February 22, 2021); Kevin A. Hassett and Aparna Mathur, "A Spatial Model of Corporate Tax Incidence," American Enterprise Institute, December 1, 2010, https://www.aei.org/wp-content/uploads/2011/10/-a-spatial-model-of-corporate-tax-incidence_105326418078.pdf (accessed February 22, 2021); Robert Carroll, "The Corporate Income Tax and Workers' Wages: New Evidence from the 50 States," Tax Foundation *Special Report* No. 169, August 3, 2009, https://taxfoundation.org/corporate-income-tax-and-workers-wages-new-evidence-50-states/ (accessed February 22, 2021); Desai Mihir, Fritz Foley, and James Hines, "Labor and Capital Shares of the Corporate Tax Burden: International Evidence," December 2007, http://piketty.pse.ens.fr/files/Desaietal2007.pdf (accessed February 22, 2021); and "Why Do Workers Bear a Significant Share of the Corporate Income Tax?" in Jason J. Fichtner and Jacob M. Feldman, "The Hidden Cost of Federal Tax Policy," 2015, https://www.mercatus.org/system/files/Fichtner-Hidden-Cost-ch4-web.pdf (accessed February 22, 2021). For a contrary view, see Kimberly A. Clausing, "In Search of Corporate Tax Incidence," *Tax Law Review*, Vol. 65, No. 3 (2012), pp. 433–472, http://ssrn.com/abstract=1974217 (accessed February 22, 2021).
93. It requires extreme, implausible assumptions about elasticities of demand for, or supply of, factors for this not to be the case. Alan J. Auerbach, "Who Bears the Corporate Tax? A Review of What We Know," National Bureau of Economic Research *Working Paper* No. 11686, October 2005, http://www.nber.org/papers/w11686.pdf (accessed February 22, 2021); William M. Gentry, "A Review of the Evidence on the Incidence of the Corporate Income Tax," Department of the Treasury, Office of Tax Analysis, *OTA Paper* No. 101, December 2007, https://www.treasury.gov/resource-center/tax-policy/tax-analysis/Documents/WP-101.pdf (accessed February 22, 2021); and Stephen J. Entin, "Tax Incidence, Tax Burden, and Tax Shifting: Who Really Pays The Tax?" Heritage Foundation *Center for Data Analysis Report* No. 04–12, November 5, 2004, http://s3.amazonaws.com/thf_media/2004/pdf/cda04-12.pdf.

94. In a competitive market, capital will flow from jurisdictions with a relatively low expected after-tax return to jurisdictions with a relatively high expected after-tax return until the expected after-tax returns are equal. Social and legal barriers reduce labor mobility relative to capital mobility. Gentry, "A Review of the Evidence on the Incidence of the Corporate Income Tax"; William C. Randolph, "International Burdens of the Corporate Income Tax," Congressional Budget Office *Working Paper* 2006–09, August 2006, https://cbo.gov/sites/default/files/cbofiles/ftpdocs/75xx/doc7503/2006-09.pdf (accessed February 22, 2021); and R. Alison Felix, "Passing the Burden: Corporate Tax Incidence in Open Economies," Federal Reserve Bank of Kansas City, October 2007, https://www.kansascityfed.org/Publicat/RegionalRWP/RRWP07-01.pdf (accessed February 22, 2021).
95. Ibid.
96. As opposed to non-corporate capital and customers.
97. See, for example, Roberta Romano, *The Genius of American Corporate Law* (Washington: AEI Press, 1993).
98. U.S. Securities and Exchange Commission, "Regulation S-K, Questions and Answers of General Applicability." For a discussion of securities law disclosure requirements, see David R. Burton, "Securities Disclosure Reform," Heritage Foundation *Backgrounder* No. 3178, February 13, 2017, https://www.heritage.org/sites/default/files/2017-02/BG3178.pdf.