The Sound of Silence in Corporate Director Resignations

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This Article seeks to provide an in-depth theoretical, empirical, and policy analysis of an underdeveloped topic in corporate law: director departure. We argue that outspoken director resignations are an integral aspect of effective corporate governance. Disgruntled corporate directors who disagree with the firm's policies or practices alert shareholders to internal misconduct, encouraging market reactions that pressure the company to make necessary changes. Disclosure of conflict is particularly important in mitigating information asymmetry between shareholders and management, allowing investors to promptly react to relevant events within the firm.

Despite the governance benefits of resignations in protest, we show that outspoken director resignations are few in number. We undertake an intensive theoretical analysis of the vectors that limit the desire or ability of directors to resign in protest. We highlight that Delaware Court of Chancery decisions Puda Coal and Fuqi limit the ability of directors to resign in protest due to fears of personal liability for breach of fiduciary duty. Similarly, we note that directors prefer to resign quietly to preserve their reputation in the director labor market. We illustrate structural biases in the boardroom that may impede directors from resigning in protest and negatively affecting their fellow peers. Lastly, we describe the effect of director compensation on their decision whether to outspokenly depart. Beyond the departing director, we highlight potential limitations on firms to disclose resignations as "outspoken."

In light of these potential limitations, we provide a hand-collected empirical analysis of over 54,000 Form 8-K disclosures of S&P 500 firms between the years 2016-2024. Our findings coincide with our theoretical discussion: outspoken departures comprise only around 0.1% of disclosed director resignations in our sample. In the rare cases in which directors resign in

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protest, their departures follow public exposure to the relevant conflict. We complement our empirical study by examining several test cases which provide strong evidence regarding disagreements between departing directors or officers and the firm. Despite such disagreements, firm disclosures in these cases kept silent.

Based on our empirical findings and theoretical analysis, we discuss certain policy implications that may serve to increase the frequency of outspoken director resignations. We highlight possible changes to Form 8-K disclosure requirements and necessary SEC enforcement of disclosure violations. Likewise, we discuss creating a concrete legal framework of director resignations that minimizes the uncertainty arising from the Delaware decisions. To balance interests, we note the ability of corporations to file defamation suits to protect firms against bad-faith resignations.

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INTRODUCTION

General Company Inc. is a renowned corporation led in part by Javier, an experienced director dedicated to furthering the company's image and increasing shareholder profits. Javier finds himself at a crossroads – the board furthers decisions that Javier believes will damage General Company's reputation. Other directors, like Carlos and Maria, authorized large sum transfers to third parties and claimed that the company was repaid in full, yet failed to provide audited financial statements justifying their claims. Javier pushes for an audit committee investigation, but management derails the investigation by failing to appropriately fund the committee's expenses, leaving the transfer uninvestigated for years. Requests are unheard, meetings remain neglected, and management begins to spiral out of control. Javier, unable to affect change within General Company, decides to resign in protest, utilizing his senior position to alert shareholders to the firm's internal misbehaviors.

Intuitively, many would agree that Javier's course of action was necessary in exposing misgivings within General Company. Yet, according to cases like the 2013 Delaware decision in *Fuqi*, Javier's "reward" for resigning in protest may not be praise and increased pay, but rather personal liability for breach of fiduciary duty.[1] Furthermore, Javier will be branded a "troublemaker" by other firms and will find himself unable to attain future employment, despite his good faith attempt to affect change within the company. As a result, directors like Javier are pressured to remain silent, fearful of the negative consequences they may face when resigning in protest. We refer to this as "the sound of silence" in director departures.

Outspoken director resignations are crucial to a firm's governance structure. Directors, as salaried employees, are generally permitted to resign irrespective of motive or circumstance. Those who are unsatisfied with practices that their firm engages in may resign in protest, signaling to shareholders that their resignation stems from disagreement.[2] As fiduciaries bound to protect shareholder interests,[3] they may express vocal opposition to alert investors to internal misbehaviors. If unable to create effective change from within, directors may seek to publicize their disagreement with the firm and utilize the market to push companies to remedy internal misconduct.

This tool can be particularly effective in furthering necessary changes within the firm. Shareholders, who suffer from information asymmetry with management,[4] are promptly alerted by the departures of important

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[1] Rich ex rel. Fuqi Int'l, Inc. v. Chong, 66 A.3d 963 (2013).

[2] *See infra* Section I.A.1.

[3] This view is commonly referred to as "shareholder primacy" in the corporate literature. *See* Dodge v. Ford Motor Co., 204 Mich. 459 (1919) ("A business corporation is organized and carried on primarily for the profit of the stockholders"); Dorothy S. Lund & Elizabeth Pollman, *The Corporate Governance Machine*, 121 COLUM. L. REV. 2563, 2576 (2021) ("Thus, by the end of the 1980s, the separation of ownership and control became 'the master problem,' and pursuing shareholder value was regularly identified as a core corporate objective"); D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277, 277-78 (1998) ("The structure of corporate law ensures that corporations generally operate in the interests of shareholders… Corporate directors have a fiduciary duty to make decisions that are in the best interests of the shareholders"); Stephen M. Bainbridge, *Participatory Management Within a Theory of the Firm*, 21 J. CORP. L. 657, 717 (1996) ("the shareholder wealth maximization norm ... has been fully internalized by American managers"); Mark J. Roe, *Political Preconditions to Separating Ownership from Corporate Control*, 53 STAN. L. REV. 539, 545 (2000).

[4] Michael C. Jensen and William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON. 305 (1976) (describing the agency problem that arises from separating ownership and control between shareholders and management); Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 880 (2005) ("Imperfect Information – The most common argument against expansions in shareholder voting rights is based on informational disadvantage that shareholders are likely to have vis-à-vis managements").

figures who appear to have no option other than to "pack their bags and leave." To mitigate negative market reactions that arise from outspoken director resignations, the company must then react timely and remedy the policies or practices in question. In this way, experienced directors can fulfill their fiduciary duties and utilize their ability to resign as a "last resort" for promoting effective change within the firm.

Despite the inherent governance advantages in outspoken director resignations, we hypothesize that outspoken director resignations are few in number. We provide a theoretical analysis of potential vectors that may limit the ability and desire of directors to resign in protest. Furthermore, we highlight potential limitations on the firm that may inhibit its desire to disclose outspoken departures.

First, we point to the risks of potential liability for breach of fiduciary duties that directors face when resigning, specifically in protest.[5] Here, we discuss recent developments from two notable 2013 Delaware decisions, *Puda Coal* and *Fuqi*, which exacerbated the uncertainty regarding director resignations.[6] Second, we discuss the effect of personal reputation on departing directors' desire to voice their frustration when resigning.[7] Directors who resign in protest are often seen as "troublemakers" by other firms, and as a result they are effectively "blacklisted" from future employment. Third, we explain that directors are limited due to structural biases within the board.[8] Directors are often susceptible to network and friendship biases that may negatively affect their desire to bring about public scrutiny and possible regulatory action on their peers. Lastly, we discuss the effect of financial incentives on outspoken director resignations.[9]

To test our hypothesis, we provide a hand-collected empirical analysis of director resignations in the current S&P 500 companies between 2016-2024.[10] We find that out of 3,825 resignations, only 4 were disclosed as arising from disagreement with the firm's operations, policies, and practices, approximately 0.1% of disclosed departures. Due to the sensitive, hand-collected nature of our empirical research, we highlight certain trends that were not discussed in previous literature: for example, outspoken resignations often followed public exposure to the relevant conflict, minimizing the informativeness of the disclosures themselves. Similarly, firms tend to increase disclosure surrounding directors at their date of appointment and remain silent at the date of their departure.

Furthermore, we examine specific test cases collected in our sample in which resignations that resulted from disagreement were not properly disclosed. Such, for example, was the case with Peter Thiel's resignation

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[5] *See infra* Section II.A.1.

[6] Fuqi, *supra* note 1; In re Puda Coal Stockholders' Litigation, C.A. No. 6476-CS (Del. Ch. Feb. 6, 2013).

[7] *See infra* Section II.A.2.

[8] *See infra* Section II.A.3.

[9] *See infra* Section II.A.4.

[10] *See infra* Section III.

from Meta. Thiel, Meta's first angel investor dating back two decades, "did not stand for re-election" in 2022, citing no disagreements with the firm.[11] Yet, later news reports detailed Thiel's disagreements with the company's Metaverse policy prior to resigning and his views on the firm's effect on politics.[12] Likewise, we note the resignation of senior officers from Tesla that were improperly disclosed. Chief accounting officer Dave Morton resigned from the firm, without citing circumstances of conflict.[13] However, Morton later detailed feelings of neglect from executives, including CEO Elon Musk, regarding financial hurdles related to privatizing the firm.[14] In cases like these, shareholders are left in the dark, unaware of the true motivations behind the director or corporate officer's decision to resign. Shareholders' right to material information is hampered, and their ability to affect necessary change within the firm is minimized.

Based on our theoretical analysis and subsequent empirical findings, we offer a normative analysis of director resignations that highlights policy implications relating to the frequency of outspoken director resignations. Initially, we discuss increasing the disclosure requirements for firms surrounding director departures.[15] Afterwards, we encourage expanding SEC enforcement of disclosure violations relating to director resignations, including increasing sanctions for companies who fail to disclose conflict-related circumstances.[16] Then, we illustrate the benefits of a detailed legislative framework that governs the ability of directors to resign, specifically in protest, without incurring personal liability for breach of fiduciary duty.[17] This will minimize the uncertainty that arose from cases like *Puda Coal* and *Fuqi*, which, when necessary, will encourage good-faith directors to voice their misgivings upon departure.[18] Finally, we highlight the ability of companies to bring defamation suits against

[11] SEC Filings, i.e. Meta Platforms, Inc., Current Report (Form 8-K) (Feb. 5, 2022).
[12] Thomas Barrabi, *Peter Thiel confronted Mark Zuckerberg about metaverse focus before abrupt board resignation: report*, N.Y. POST (Apr. 25, 2023) https://nypost.com/2023/04/25/peter-thiel-confronted-zuckerberg-about-metaverse-focus-before-board-resignation-report/; Katie Paul et al., *Insight: Inside Meta's scramble to catch up on AI*, REUTERS (Apr. 26, 2023) https://www.reuters.com/technology/inside-metas-scramble-catch-up-ai-2023-04-25/; Katelyn Fossett, *The Black Box of Peter Thiel's Beliefs*, POLITICO (Sep. 20, 2021) https://www.politico.com/news/magazine/2021/09/20/peter-thiel-book-facebook-trump-jd-vance-blake-masters-josh-hawley-513121.
[13] SEC Filings, i.e. Tesla, Inc., Current Report (Form 8-K) (Sep. 4, 2018).
[14] Alex Sherman, *Tesla's chief accounting officer quit after concluding Elon Musk and others weren't listening to him about the go-private deal*, CNBC (Sep. 7, 2018) https://www.cnbc.com/2018/09/07/tesla-cao-dave-morton-quit-after-concluding-musk-wasnt-listening.html.
[15] *See infra* Section IV.A.
[16] *See infra* Section IV.B.
[17] *See infra* Section IV.C.
[18] Fuqi, *supra* note 1; Puda Coal, *supra* note 6.

departing directors who utilize their right to resign in protest in bad faith.[19]

This essay will be divided into 4 parts. Part I describes the right of directors to resign, specifically in protest. Furthermore, this part illustrates the SEC's current disclosure requirements for director resignations. Part II introduces a theoretical framework analyzing the vectors that limit outspoken director resignations. Part III presents our hand-collected empirical analysis of director resignations and highlight findings that arose from our research. Similarly, this section examines relevant test cases within our sample that strengthen our claim. Part IV offers relevant policy implications that connect our empirical findings and theoretical analysis regarding outspoken departure.

This Article seeks to fill the void in current corporate literature regarding director departure and its role in corporate governance through several major contributions. First, this Article aims to provide an in-depth theoretical framework regarding outspoken director resignations. Second, it presents a unique discussion on the case law surrounding director resignations, specifically the developments that arose from 2013 Delaware decisions *Puda Coal* and *Fuqi*. Third, it offers hand-collected data from over 54,000 Form 8-K disclosures that allow us to analyze unique trends in director departure that were not previously apparent. Through our empirical analysis, we were able to collect potential test cases that highlight disagreements between departing directors and firms that were disclosed "quietly." Finally, it connects empirical and theoretical findings in director resignations with effective policy implications that are based in part on recent developments within the field of corporate law.

I. DIRECTOR RESIGNATIONS AND CORPORATE GOVERNANCE

In this part, we illustrate the right of corporate directors to resign, generally irrespective of motive or circumstance. We explain how resignation in protest can be an effective governance tool, specifically by informing shareholders of material events related to the firm's condition. This, we argue, coincides with the fiduciary duty of directors to disclose material information to shareholders, including upon departure from the firm. Afterwards, we outline the SEC's current disclosure requirements regarding director resignations and highlight the benefits of disclosure transparency between directors and shareholders.

A. Rights and Ramifications of Director Resignations

1. *Right to Resign*

Corporate directors are permitted to resign at any time upon notice given to their respective corporation. In Delaware, for example, under Section 141(b) of the Delaware General Corporation Law, "[any] director may resign at any time upon notice given in writing or by electronic

[19] *See infra* Section IV.D.

transmission to the corporation," and "resignation is effective when the resignation is delivered."[20] The legislative history of this section illustrates that the purpose of the statute was to "prevent a corporate director who desires to resign from having his status placed in doubt by a refusal or failure of the board to act."[21]

Directors are not limited by the acceptance of the firm to tender their resignation, including acceptance by the board.[22] As salaried employees, they are protected by the free labor rule, which holds that one cannot be compelled to keep a position of employment by refusal of another to accept their resignation.[23] Here, the legislature's emphasis on delivery of the resignation illustrates that departure is largely meant to remain in the hands of the resigning director.

Directors are also free to decide the method of their resignation. Although Section 141(b) notes that director resignation may be effective through written notice, the Delaware Court of Chancery has ruled that an oral resignation can be similarly effective because the statutory language can be construed as permissive rather than mandatory.[24] Likewise, with the exception of limits on subsequent competition, directors are generally able to resign irrespective of circumstance.[25] Delaware law does not list the circumstances in which directors may resign, nor does it delineate its limitations. Instead, the courts are required to provide the framework by which directors may depart from their positions.[26]

The rationale behind the right to resign lies in notions prevalent in constitutional law, which hold that directorship does not entail forced

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[20] Del. Code Ann. tit. 8 §141(b) (2022). Section 141(b) was amended in 2000 to permit director resignations to be submitted by "electronic transmission" as defined in §232(c).
[21] WELCH EDWARD ET AL., FOLK ON THE DELAWARE GENERAL CORPORATION LAW 390 (2018).
[22] Dillon v. Berg, 326 F. Supp. 1214, 1224 (D. Del.), *aff'd*, 453 F.2d 876 (3d Cir. 1971) (per curiam).
[23] Marine Forwarding Shipping Co. v. Barone, La.App., 154 So.2d 528, 530 (4th Cir. 1963). Courts have recognized that this right is not absolute, subject to circumstances that may entail personal liability for directors, which we explain later. *See infra* Section II.A.1.
[24] *See*, *e.g.*, Biolase, Inc. v. Oracle Partners, L.P., 97 A. 3d 1029, 1033-1034 (Del. 2014) (finding "sensible and reasonable" the Court of Chancery's interpretation of section 141(b) as taking a permissible approach that authorizes the specified resignation yet does not rule out other forms of resignation); Boris v. Schaheen, C.A. No. 8160-VCN, slip op. at 48 (Del. Ch. Dec. 2, 2013) ("[A] director may resign orally… subsequent actions consistent with an oral resignation can support finding a resignation without written notice").
[25] In re Telesport Inc., 22 B.R. 527 (Bankr. E.D. Ark. 1982) ("Corporate officers are entitled to resign for a good reason, a bad reason, or no reason at all…"); *Frantz Manufacturing Co. et al. v. EAC Industries,* 501 A.2d 401, 423 (Del. 1985) ("Directors are also free to resign").
[26] However, as we show later, the courts fail to provide the necessary framework that guides directors upon resignation. *See infra* Section II.A.1.

servitude.[27] Courts have often justified the right to resign on the basis that the 13th Amendment prohibits involuntary personal service that is not punishment for a crime.[28] In fact, the Supreme Court has often upheld the objective of the 13th Amendment to prevent contractual arrangements that prevent the ability to resign.[29] At the state level, legislation is enforced to protect the salaried employee's right to refuse the undesired performance of a contract.[30]

Resignation of corporate directors is not without its limitations. The courts have recognized circumstances in which directors cannot resign from their respective firms without exposing themselves to possible breach of fiduciary duties for "jumping ship".[31] Nevertheless, directors are generally permitted to resign, notwithstanding the limitations recognized in case law.[32] As we later explain, director

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[27] Adolf A. Berle, *"Control" in Corporate Law,* 58 COLUM. L. REV. 1212, 1217 (1958) ("Acceptance of a directorship does not entail forced servitude: a director can resign at any time and for wholly personal motives, including no doubt the simple con sideration that he no longer wants the responsibility").

[28] *See, e.g.*, Clyatt v. United States, 197 U.S. 207 (1905) (upholding the ability of Congress to enforce the Thirteenth Amendment's prohibition of involuntary servitude through anti-peonage legislation); Pollock v. Williams, 322 U.S. 4, 25 (1943) (holding a statute that forces an employee to remain under certain conditions to be a violation of the Thirteenth Amendment's prohibition on involuntary servitude). *See also* Conrad G. Tuohey, *Corporate Director Resignation*, 33 ARK. L. REV. 106, 111 (1979); Rebecca E. Zietlow, *Free at Last! Anti-Subordination and The Thirteenth Amendment*, 90 BU. L. REV. 255, 290-294 (2010) (describing the courts' protection of the Thirteenth Amendment's ban on involuntary servitude through cases involving the Anti-Peonage Acts).

[29] *See, e.g.*, United States v. Kozminski, 487 U.S. 931 (1988); Ruben J. Garcia, *The Thirteenth Amendment and Minimum Wage Laws*, 19 NEV. L.J. 479, 507 (2018) (describing the intentions of the Thirteenth Amendment, including prohibiting "arrangements that prevent the right to quit"); Ryanne Bamieh, *The New Abolition; The Legal Consequences of Ending All Slavery and Involuntary Servitude*, 59 HARV. C.R.-C.L. L. REV. 245, 275 (2024) ("…the Supreme Court has clarified that involuntary servitude includes labor coerced through the use of the legal system, not simply through physical force").

[30] *See, e.g.,* George Rutherglen, *Constitutionalizing Employees' Rights: Lessons from the History of the Thirteenth Amendment,* 27 WISCONSIN J. L. GEND. SOC. 162, 165 (2012) (describing the enforcement of the Peonage Abolition Act in Alabama). The importance here is the utilization of laws seeking to enforce the values of the 13th Amendment against involuntary labor. *See* Zietlow, *supra* note 27; George Rutherglen, *State Action, Private Action, and the Thirteenth Amendment*, 94 VA. L. REV. 1367, 1368 (2008) ("Thus the [Thirteenth] Amendment has been interpreted to prohibit private contracts of peonage that forced an employee to continue to work for his master despite his decision to quit").

[31] *See infra* note 90.

[32] In addition, we note that directors are not absolved of liability from misconduct that occurred through their tenure simply for resigning from the firm. In *Xerox v. Genmoora*, for example, Judge Brown highlighted that corporate directors are not free from liability for breach of fiduciary duty simply for "jumping ship." *See* Xerox Corp. v. Genmoora Corp., 888 F.2d 345, 355 (1989) (explaining that under such logic, "if a commercial airline pilot were to negligently aim his airplane full of passengers at a mountain, and

resignations can have wide-ranging implications on the firm, the departing director, shareholders, and the public alike.

2. *Outspoken Resignations and Effective Governance*

The right to resign, specifically in protest, also has its foundations in fiduciary and corporate law. Directors are seen as fiduciaries of the corporation and its shareholders, which requires them to act in the best interest of the firm.[33] They are required, both by their duty of care and loyalty, to reasonably act with an undivided loyalty to the firm's shareholders.[34] As a result, a director's failure to further the interests of their beneficiaries can constitute a breach of their fiduciary duties.

Directors can utilize resignation from their position as a vehicle to fulfill their fiduciary duties to shareholders. Those who are unhappy with practices that the firm engages in are able to resign in protest, signaling

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then bail out before impact, he would not be liable because he was not at the controls when the crash occurred").

33 Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939); Asaf Eckstein & Gideon Parchomovsky, *Towards a Horizontal Fiduciary Duty,* 104 CORNELL L. REV. 803, 812 (2019) ("The imposition of a fiduciary duty on directors and officers is intended to align their interests with those of the corporation and ensure that they act with the best interest of the corporation in mind"); Zohar Goshen & Gideon Parchomovsky, *The Essential Role of Securities Regulation*, 55 DUKE L.J. 711, 748 (2006) ("The primary role of corporate law is to minimize agency costs, most notably by imposing fiduciary duties on the board of directors and the management, and requiring corporate governance mechanisms"); REINER R. KRAAKMAN ET AL., THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 21-22 (2004); John C. Coffee Jr., *The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role*, 89 COLUM. L. REV. 1618, 1642 (1989).

34 The director's duty of care requires that he or she acts with a reasonable amount of available material information when making business decisions, which includes the decision to depart from a firm in its current condition. *See, e.g.,* In re Walt Disney Co. Derivative Litig., 907 A.2d 693, 749 (Del. Ch. 2005); Smith v. Van Gorkom, 488 A.2d 858, 871 (Del. 1985); Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) ("…directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them"); Julian Velasco, *A Defense of the Corporate Law Duty of Care*, 40 J. CORP. L. 647, 649 (2015) ("…the duty of care is necessary to let fiduciaries know that they have a legal duty to pursue the beneficiaries' interests with skill and diligence (i.e., carefully), and not merely to avoid conflicts of interest (i.e., loyally)"). The director's duty of loyalty requires them to act in the best interests of the firm and its shareholders, preemptively acting to ensure the protection of these interests. *See* Guth, *supra* note 33, at 510; Gregory H. Shill, *The Golden Leash and the Fiduciary Duty of Loyalty*, 64 UCLA L. REV. 1246, 1274 (2017) ("Agents owe 'a fiduciary duty to act loyally for the principal's benefit in all matters connected with the agency relationship'… it is well established that directors, as agents of the corporation-principal, owe a duty to act loyally for its benefit"); Yaron Nili, *Horizontal Directors*, 114 NW. U.L. REV. 1179, 1202 (2020) ("Directors, as agents of the corporation-principal, owe a duty of loyalty to act for that corporation's benefit"); Lyman Johnson, *After Enron: Remembering Loyalty Discourse in Corporate Law*, 28 DEL. J. CORP. L. 27, 38-39 (2003).

to shareholders that the resignation arises from disagreement.[35] Here, directors distance themselves from the firm through departure, proclaiming that they do not wish to align themselves with the interests or behaviors of the company's leadership.[36]

Resignation in protest acts as a powerful governance tool in the corporate structure. Directors express vocal opposition to alert investors to internal misbehaviors and mitigate the information asymmetry between shareholders and management.[37] When directors are unable to create effective change within the firm, they may opt to "exit" from the company, signaling that their values are incompatible with the policies of the firm.[38] Due to the inherent disadvantages of resignation, this tool can be particularly effective in articulating to investors and the public that there ought to be changes within in the company.[39]

Outspoken director resignation is particularly informative: the board of directors plays a central role in corporate governance,[40]and directors

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35 For the SEC's regulations regarding resignation in protest, *see* U.S. SEC, EXCHANGE ACT FORM 8-K (last updated Dec. 14, 2023) https://www.sec.gov/divisions/corpfin/guidance/8-kinterp.htm.

36 Piergaetano Marchetti, Gianfranco Siciliano, & Marco Ventoruzzo, *Dissenting Directors*, 18 EUR. BUS. ORG. L. REV. 1, 17 (2017) ("A deeper and more general dissent, possibly still originating from a specific transaction or corporate decision, can also be expressed with the more dramatic option of resigning from the board"). Of course, resignation may derive from other reasons. For example, a director may resign because they feel overburdened, because they can improve their compensation elsewhere, or because the company is unable or unwilling to provide sufficient D&O insurance. *See, e.g.*, Roberta Romano, *What Went Wrong With Directors' and Officers' Liability Insurance?*, 14 DEL. J. CORP. L. 1, 1-2 (1989) ("There are reports of directors resigning because their firms has lost insurance coverage.")

37 *Id.*, at 2 ("Vocal opposition by a director, for example, might help correct a good-faith mistake or, in more serious and extreme circumstances, warn the market of possible abuse and other risks for investors… notwithstanding the potential importance of director dissent as a governance tool…").

38 *See generally* Albert O. Hirschman, EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINE IN FIRMS, ORGANIZATIONS, AND STATES (1970); David A. Katz & Laura A. McIntosh, *Can You Resign from the Board of a Troubled Company*, CLS BLUE SKY BLOG (May 23, 2013) https://clsbluesky.law.columbia.edu/2013/05/23/can-you-resign-from-the-board-of-a-troubled-company/ ("When a director's attempts to investigate an apparent problem are met with stonewalling by management or other directors, or when a director's efforts to cause the board to take action are met with intractable resistance, the director is likely to consider resignation as he or she likely will believe that his or her ability to effect change has been compromised").

39 For example, directors are impeded by reputational and financial incentives that limit their desire to resign. *See infra* Sections II.B, II.D. When directors voluntarily relinquish these benefits, the result is that the costs of the directorship outweigh its benefits, signaling to investors possible misgivings within the firm. *See* Keren Bar-Hava et al., *Do Independent Directors Tell the Truth, the Whole Truth, and Nothing but the Truth When They Resign?,* 36 J. ACC. AUDIT. FIN. 3, 4 (2021).

40 Stephen M. Bainbridge & M. Todd Henderson, *Boards-R-Us: Reconceptualizing Corporate Boards*, 66 STAN. L. REV. 1051, 1053 (2014) ("Although day-to-day decisions are made by managers, directors are obligated to make fundamental decisions, like hiring and

are expected to implement high standards of governance and compliance with laws, regulations, and ethics.[41] Directors act as watchdogs on behalf of shareholders, monitoring management, ensuring the financial success of the firm, and advising senior managers on the firm's strategic direction.[42] Since shareholders lack the ability to exercise oversight of management, they enlist the board as a tool to convey material information.[43]

The information conveyed by outspoken resignations is relevant in the market, assisting investors in considering the possible implications of their investments in certain firms. Director resignations, specifically in protest, tend to result in lower stock prices and public scrutiny of the firm.[44] Negative market reactions to the relayed information cause management to reconsider relevant policies and practices, specifically to mitigate worsening stock performance,[45] analyst reactions,[46] and unwanted media attention.[47] The firm is forced to change its business

firing the managers, setting compensation incentives, raising capital, and entering into mergers and acquisitions… this latter category of decisions routinely involves high stakes and potential conflicts among corporate stakeholders, making the board the place where legal rules about corporate governance have the most relevance"); Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 VA. L. REV. 675, 679-80 (2007) ("Boards play a central role in the standard view and the legal structure of the modern publicly traded corporation with dispersed ownership… [the power to run the company] is vested in the board of directors, under whose direction the business and affairs of the corporation are supposed to be managed").

41 *See*, *e.g.*, John Armour et. al, *Board Compliance*, 104 MINN. L. REV. 1191, 1208 (2020); Sean J. Griffith, *Corporate Governance in an Era of Compliance*, 57 WM. & MARY L. REV. 2075, 2109 (2016).

42 Donald C. Langevoort, *Commentary: Puzzles About Corporate Boards and Board Diversity*, 89 N.C.L. REV. 841, 842-44 (2011).

43 Bainbridge & Henderson, *supra* note 40, at 1062 ("But the corporation's nominal owners – the shareholders – lack both the legal right and, in most cases, the practical ability to exercise meaningful oversight of the corporation's management… as a result, the legal system evolved alternative accountability structures to punish and deter wrongdoing by firm agents, most notably the board of directors").

44 Rudiger Fahlenbrach, Angie Low, & Rene M. Stulz, *Do Independent Director Departures Predict Future Bad Events?,* 30 REV. FIN. STUD. 2313 (2017) (showing the negative consequences firms face after independent director departures, including worse stock and operating performance).

45 *See, e.g.*, Paul Gompers, Joy Ishii, & Andrew Metrick, *Corporate Governance and Equity Prices*, 118 Q. J. ECON. 107 (2003) (finding a striking relationship between corporate governance and stock returns); Lucian A. Bebchuk, Alma Cohen & Allen Ferrell, *What Matters in Corporate Governance?*, 22 REV. FIN. STUD. 783 (2009) (showing that corporate governance affects firm's abnormal stock returns).

46 Kee H. Chung & Hoje Jo, *The Impact of Security Analysts' Monitoring and Marketing Functions on the Market Value of Firms*, 31 J. FIN. & QUANT. ANAL. 493, 493-97, 511 (1996); Stephen J. Choi, *The Problems with Analysts*, 59 ALA. L. REV. 161, 167-70 (2007); Tao Chen et al., *Do Analysts Matter for Governance? Evidence from Natural Experiments*, 115 J. FIN. ECON. 383, 383-84, 406-07 (2015).

47 Michal Barzuza, Quinn Curtis, & David H. Webber, *The Millennial Corporation: Strong Stakeholders, Weak Managers*, 28 STAN. J. L. BUS. FIN. 255 (2023) (explaining how market

strategy to appease disgruntled investors, specifically as a result of transparency upon director departure.[48]

This transfer of material information through resignation relates to the essence of a director's fiduciary duty: ensuring that the firm works in the best interest of shareholders.[49] The courts often recognize the duty of directors to disclose material information to shareholders, including cases in which the director does not have self-interest in said disclosure.[50] In Lynch v. Vickers Energy Corp., for example, the Supreme Court of Delaware emphasized that the duty to disclose requires full disclosure to the corporation's stakeholders of "all the facts and circumstances" relevant to the board's decision.[51] Director disclosure is essential to corporate governance and fiduciary obligations in that shareholders cannot exercise their rights without material understanding of the firm's condition and business affairs.[52] Specifically, reporting credible

pressures and social demands by employees, consumers, investors, and other market participants push firms to improve governance practices); Michael Dewally & Sarah Peck, *Upheaval in the Boardroom: Outside Director Public Resignations, Motivations and Consequences,* 16 J. CORP. FIN. 38, 39 (2010) ("Resignations accompanied by public criticism can put pressure on the remaining directors to improve firm performance"); Alexander Dyck & Luigi Zingales, *The Corporate Governance Role of the Media*, *in* THE RIGHT TO TELL: THE ROLE OF THE MEDIA IN DEVELOPMENT, THE WORLD BANK (2002) (showing that the media plays an important role in shaping corporate governance and policy).

48 *See generally* RICHARD A. BREALEY & STEWART C. MYERS, PRINCIPLES OF CORPORATE FINANCE 15 (5th ed. 1996) (describing the role of shareholder pressure in remedying agency problems between shareholders and management).

49 *See supra* notes 33-34.

50 Smith v. Van Gorkom, *supra* note 34; Weinberger v. Uop, 457 A.2d 701, 712 (1983); Jack B. Jacobs, *The Fiduciary Duty of Disclosure after Dabit*, 2 J. BUS. TECH. L. 391, 397 (2007) ("…the Delaware Supreme Court held that failure to disclose material information to stockholders could expose directors to liability for breach of fiduciary duty in the highly different context where the directors have no conflict at all, i.e., are disinterested in the transaction"); Reza Dibadj, *Disclosure as Delaware's New Frontier*, 70 HASTINGS L.J. 689, 702 (2019) ("But at its core, *Weinberger* may also hinge on disclosure—as students of corporations law remember, arguably the key factor against the defendants was the non-disclosure of a report stating that the acquirer would be willing to go beyond the price offered… While [*in re Caremark*] is typically studied as a "duty to monitor" case under duty of care, there is also an under-appreciated component that revolves around disclosure").

51 Lynch v. Vickers Energy Corp., 383 A.2d 278, 279 (Del. 1977). *See also* William M. Lafferty, Lisa A. Schmidt & Donald J. Wolfe, Jr., *A Brief Introduction to the Fiduciary Duties of Directors Under Delaware Law*, 116 PENN ST. L. REV. 848-849 (2012) (describing the development in *Vickers Energy* and its context in the duty of disclosure).

52 Leo E. Strine et al., *Loyalty's Core Demand: The Defining Role of Good Faith in Corporation Law*, GEO L. J. 629, 638-39 (2010) ("…in cases dealing with the disclosure obligations directors owe when asking stockholders to vote on a particular matter, Delaware courts have often said that the duty to disclose all material facts arises out of, or implicates, both the duty of loyalty and care"); Faith Stevelman Kahn, *Transparency and Accountability: Rethinking Corporate Fiduciary Law's Relevance to Corporate Disclosure*, 34 GA. L. REV. 505, 515–16 (2000) ("From a more conventional perspective, corporate disclosure must be studied as an aspect of corporate governance because shareholders cannot exercise their

information to shareholders, regardless of method, attests to the efforts of the director to act in good faith and adhere to their duty of loyalty.[53]

At times, directors who wish to comply with their duties may be required to utilize resignation as a method of relaying this information, especially when other methods are not successful or are potentially harmful to the directors themselves. Directors who publicize negative information regarding the firm during their tenure may be exposed to potential lawsuits for breach of duty of loyalty.[54] As a result, directors are limited in their ability to transfer such material knowledge to shareholders while fulfilling their positions. Therefore, it is imperative that directors be able to utilize the potential power of resignation in protest in situations when it serves to benefit the firm and its shareholders.[55]

We do not argue that resignation benefits firm governance regardless of circumstance. Directors serve important governance roles, and their departures can have wide-ranging effects on the firm's monitoring system and internal controls. As a result, director resignations may negatively impact governance structures in certain situations. Nevertheless, outspoken resignations are useful in informing shareholders of material information that cannot be easily relayed throughout the natural course of a director's tenure. Furthermore, when directors have already made the decision to depart from the firm, outspoken resignation better serves the interests of shareholders and their right to understand the material condition of the firm.

B. Disclosure of Director Resignations

When a director resigns, is removed, or refuses to stand for re-election, public companies are required to submit a Form 8-K to the

governance rights – including their right to determine whether to hold or to sell their shares on an informed basis – without adequate, accurate information about their firms' financial condition and material business affairs"). Professor Stevelman Kahn also highlights a similar development as found in *Caremark* regarding the necessity of information transfer between directors and shareholders. *See Id*., at 511.

[53] *Id*., at 512 ("Because information about material corporate business affairs – and the ability to represent it accurately and credibly to third parties – will continue to be a highly precious commercial asset, corporate fiduciary law will continue to evolve standards under the duty of care [and also the duties of loyalty and good faith, as discussed hereinafter] for managers' oversight of gathering and reporting this information in both the firm's and shareholders' best interests").

[54] This is because such information quickly leads to drops in the firm's stock price and reputation, which can be construed as acting against the best interests of the corporation and its shareholders. *See, e.g.,* Fahlenbrach, *supra* note 44.

[55] In this Article, we specifically highlight the aspect of the duty of disclosure adjacent to departure. Our focus is not on the director's general duty throughout their tenure, although it constitutes an important aspect of the director's fiduciary duties that should be expanded upon separately.

SEC.[56] In this form, the company must file an Item 5.02 8-K filing reporting the event within four business days of its occurrence.[57] SEC regulations require that when directors resign due to disagreements with the company's operations, policies, or practices, firms disclose the date of resignation, positions held by the director on board committees at the time of resignation, and a "brief description of the circumstances" surrounding the resignation that the company believes caused its occurrence.[58] If a director resigns without disagreement, then the company is required solely to disclosure the date and occurrence of the event.[59]

The company must then provide the departing director with a copy of its Item 5.02 disclosure.[60] Afterwards, the director has the opportunity to submit a letter to the company stating whether the director agrees with the statements made in its disclosure, and, if not, stating the respects in which they disagree.[61] If the director submits such a letter, then the company is required to file the letter as an amendment to the previously filed Form 8-K within two business days.[62]

Disclosure serves an important role in mitigating the agency problem between shareholders and management. Shareholders entrust managerial staff with running the firm's operations while partaking in the profits.[63] Management, unable to claim the whole of the firm's profits, are then less incentivized to expend effort, generating agency costs that reduce the firm's value.[64] This agency relationship creates information asymmetry between the passive shareholders and active day-to-day managers, which limits the shareholder's ability to effectively monitor the firm's operations.[65]

One way to mitigate this asymmetry is through information disclosure, whether voluntary or mandatory, which allows shareholders to remain informed regarding the firm's condition and react accordingly.[66] By requiring firms to periodically disclose "material facts"

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[56] Mary Ellen Carter & Billy S. Soo, *The Relevance of Form 8-K Reports*, 37 J. ACC. RES. 119, 121 (1999); Sec. 13, 15 of the Securities Exchange Act (1934) (codified at 15 U.S. Code § 78m).

[57] SEC Form 8-K Guidelines, *supra* note 35.

[58] *Id.* The guidelines do not outline the expected quantity of disclosure or the types of circumstances that companies must disclose.

[59] *Id.*

[60] *Id.*

[61] *Id.*

[62] *Id.*

[63] Jensen & Meckling, *supra* note 4.

[64] *Id.*; Zohar Goshen & Richard Squire, *Principal Costs: A New Theory for Corporate Law and Governance*, 117 COLUM. L. REV. 767, 776 (2017) (citing Jensen & Meckling's agency theory, explaining that the separation of ownership and control results in managers partaking in self-seeking behavior).

[65] *See supra* note 4.

[66] *Id.*; *see also* Dulacha G. Barako, Phil Hancock & H.Y. Izan, *Factors Influencing Voluntary Corporate Disclosures by Kenyan Companies*, *in* 14 CORPORATE GOVERNANCE, AN INTERNATIONAL REV. 107, 108 (2006) (discussing the benefits of voluntary disclosure

that may negatively affect shareholders, policymakers minimize the informational gap between the parties, subsequently reducing monitoring costs and keeping shareholders engaged.[67]

This is especially true in the case of director resignations. The director acts as a central advisor to the firm, monitoring the behavior of management and developing the firm's long-term business strategy.[68] Given their role, a director's resignation, and especially the motives behind their departure, contains relevant information for shareholders that allows them to react timely to disagreements that may negatively affect the firm.[69]

Such information can be particularly useful for shareholders.[70] Transparency in resignation is essential to market mechanisms that aim to restrict opportunistic behavior from directors and officers, or mismanagement resulting from incompetence.[71] For example, disclosure

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in mitigating information asymmetry between management and shareholders); Paul M. Healy & Krishna G. Palepu, *Information Asymmetry, Corporate Disclosure, and the Capital Markets: A Review of the Empirical Disclosure Literature*, 31 J. ACC. ECON. 405, 406 (2001) (explaining the governance benefits of regulated financial disclosures); Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice is Not Investor Empowerment*, 85 VA. L. REV. 1335 (1999) (illustrating the necessity of mandatory firm disclosure to remedy market failures and enforce socially optimal levels of issuer disclosure).

[67] Paul G. Mahoney, *Mandatory Disclosure as a Solution to Agency Problems*, 62 U. CHI. L. REV. 1047, 1051-52 (1995) ("The evident purpose of such disclosures is to help the shareholders monitor management's self-interested behavior… by reducing monitoring costs, disclosure reduces overall agency losses"); John Armour, Henry Hansmann, & Reiner Kraakman, *Agency Problems, Legal Strategies, and Enforcement*, Discussion Paper No. 644, 1, 3 (2009) ("Law can play an important role in reducing agency costs. Obvious examples are rules and procedures that enhance disclosure by agents…").

[68] Directors serve to ensure that managers act in the interest of shareholders, mitigating agency costs that arise from the aforementioned asymmetries between shareholders and management. They act as management monitors, providing oversight and incentives for management to protect shareholder objectives and maximize profit. *See* Lynne L. Dallas, *The Multiple Roles of Corporate Boards of Directors*, 40 SAN DIEGO L. REV. 781, 801 (2003). Similarly, they advise management on corporate strategy, setting overall objectives and highlighting possible strategic opportunities. *See Id.*, at 807.

[69] Bar-Hava et al., *supra* note 39; Cassandra D. Marshall, *Are Dissenting Directors Rewarded?* (2010), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1668642 (discussing the filing of 8-Ks and how they provide material information that shareholders should know about).

[70] Some may argue that such information is likely to make its way to shareholders through market channels, such that federal disclosure is not particularly necessary. However, this does not account for several discrepancies that may occur in the market. First, firms may not heed market concerns, relegating important news to mere unsubstantiated rumors. Second, there is no guarantee that the market will effectively (and honestly) relay such pertinent information to shareholders as can be done through disclosure. For a nuanced discussion highlighting the benefits of relaying information to shareholders through mandatory securities disclosure, *see* Fox, *supra* note 66.

[71] Brealey & Myers, *supra* note 48, at 13-15 (explaining how transparency in disclosures assists in promoting market mechanisms that prevent opportunistic behavior of management, such as hostile takeovers).

is particularly effective in allowing for hostile takeovers.[72] When management is failing and ineffective, shareholders can assume control to relieve it of its duties and ensure that the firm's managerial staff serves to maximize shareholder profit.[73] Disclosure of conflict, including that which arises from outspoken director resignation, reduces the risks of potential takeovers and ensures that acquisitions reflect the real share value of the firm.[74] The result is that shareholders can effectively enforce management's fiduciary duties on the basis of transparent disclosures, including disclosure of conflicts arising from director resignations.[75]

Transparency serves to benefit other market participants as well. For example, material information relayed through disclosure can serve more sophisticated investors – notably, institutions who hold large equity stakes in the market.[76] These investors have gradually increased their intervention in the governance affairs of their portfolio companies, pushing to mitigate managerial costs and ensure the effectiveness of the firm's internal controls.[77] Disclosure of circumstances of conflict relating to a departing director allows for sophisticated investors to push to remedy internal misbehaviors, including through active voting participation and direct engagements with management,[78] or even by adjusting their corporate guidelines which allow investors to communicate with their portfolio companies and provide their

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[72] Fox, *supra* note 66, at 1364 ("Even more importantly, disclosure increases the threat of hostile takeover when managers engage in non-share-value-maximizing behavior").

[73] *See, e.g.,* John C. Coffee, Jr., *Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer's Role in Corporate Governance*, 84 COLUM. L. REV. 1145, 1192-95 (1984); Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1173-74 (1981).

[74] Fox, *supra* note 66, at 1363-64 (illustrating that "disclosure both makes a takeover less risky for potential acquirers and reduces the chance that an inaccurately high share price will deter a value-enhancing acquisition").

[75] *Id.*

[76] One example of the proliferation of these institutional investors is the "Big Three" – BlackRock, State Street, and Vanguard – who hold ownership stakes in a large proportion of public companies in the United States. *See* Lucian A. Bebchuk & Scott Hirst, *Big Three Power, And Why It Matters*, 102 B.U. L. REV. 1547, 1550 (2022).

[77] *See, e.g.,* Edward B. Rock & Marcel Kahan, *Index Funds and Corporate Governance: Let Shareholders Be Shareholders* 100 B.U. L. REV. 1771, 1776 (2020) ("Properly viewed, index funds in general—and the Big Three in particular—are valuable corporate citizens that make substantial positive contributions to the governance of their portfolio companies"); Jill Fisch, Assaf Hamdani, & Steven Davidoff Solomon, *The New Titans of Wall Street: A Theoretical Framework for Passive Investors*, 168 U. PA. L. REV. 17, 25-26 (2019) (highlighting the governance roles of passive investors in alignment with more actively managed funds); Assaf Hamdani & Sharon Hannes, *The Future of Shareholder Activism*, 99 B.U. L. REV. 971, 973 (2019) ("The other important development is the rise of activist hedge funds, which use proxy fights and other tools to pressure public companies into making business and governance changes").

[78] *Id. See also* Matthew J. Mallow & Jasmin Sethi, *Engagement: The Missing Middle Approach in the Bebchuk-Strine Debate*, 12 N.Y.U. J. L. BUS. 385, 389 (2016) (highlighting the use of engagement by asset managers and institutional investors to influence management).

expectation and perspective on various corporate governance aspects.[79] Similarly, analysts and media personnel benefit from increased disclosure, allowing them to generate relevant news reports or reevaluate certain investments based on new material information.[80]

Beyond external market players, transparency in disclosures can be useful in reducing information asymmetry between directors themselves.[81] At times, directors may refrain from expressing their frustrations with the firm's strategy or policies, which results in a disparity between disgruntled directors and their peers.[82] When departing directors remain silent, the result is that their fellow directors are impeded from being exposed to their misgivings with the firm. Form 8-K disclosures can be effective tools in relaying the departing director's frustrations to remaining directors, allowing them to react accordingly.[83]

Disclosures of conflict between disgruntled directors and the firm upon departure can also serve the managerial staff. When directors express misgivings with certain policies or hirings within the firm, their frustrations may not reach senior managerial figures who lack access to board meeting protocols.[84] Outspoken resignations can serve useful in relaying information to such figures, encouraging them to foster change within the firm and avoid further controversy.

As a result, the SEC instituted guidelines requiring disclosure of director departures that arise from disagreement with the company's policies and practices.[85] Form 8-K disclosures ensure that firms disclose

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[79] Asaf Eckstein, *The Rise of Corporate Guidelines in the United States, 2005-2021: Theory and Evidence*, 98 IND. L. J. 921, 934-937 (2023).

[80] *See infra* notes 118 and 165.

[81] Eckstein & Parchomovsky, *supra* note 33, at 830 ("In their capacity as officers, individual members are exposed to data and analysis that are not available to other board members… likewise, they engage in meetings and interactions with third parties in which their peers on the board do not partake").

[82] For example, imagine cases where a director is frustrated with the firm's business strategy or monitoring system, but prefers not to disclose their frustrations to fellow directors. Similarly, imagine cases where directors are frustrated with certain executive hirings yet remain silent to refrain from conflict among their peers.

[83] This is accompanied by the aforementioned Delaware General Corporation Law, which generally pushes for director resignation to be accompanied with written notice. This encourages outspoken resignations that inform remaining directors about each other's statuses. *See* Dillon v. Berg, *supra* note 22.

[84] Eckstein & Parchomovsky, *supra* note 33, at 834 ("Nonetheless, there is an element of interdependence even among corporate officers… each officer must rely on informational inputs she receives from her peers… even an accomplished CEO cannot be expected to do well on her job without accurate legal advice and the full cooperation of other organs… other office holders critically depend on the information and instructions they receive from the firm's CEO and upper management").

[85] *Id.* For a comparison of the SEC's tendency to encourage disclosure for senior departures, *see* Jagan Krishnan & Jayanthi Krishnan, *Litigation Risk and Auditor Resignations*, 72 ACC. REV. 539, 541 (1997) (describing the SEC's support for disclosure of auditor resignations).

"current" reports following particularly extraordinary corporate events.[86] To heighten the continuity and speed of disclosures, the SEC introduced amendments to the Form 8-K requirements, including shortening the period between resignation of directors and its disclosure.[87] As we hypothesize, and later show in our empirical analysis, these requirements fail to encourage proper disclosure of outspoken director resignations.

II. THEORETICAL LIMITATIONS ON OUTSPOKEN DEPARTURE

In this part, we provide an in-depth theoretical analysis that seeks to understand potential limitations on outspoken director resignations. We highlight that directors are wary of resigning, specifically in protest, due to fear of breach of fiduciary duty, as heightened by Delaware decisions *Puda Coal* and *Fuqi*.[88] In addition, we note that directors seek to preserve their reputation, and outspoken resignations can negatively affect their reputational value in the director labor market. Afterwards, we highlight how directors are impeded by structural biases that limit their desire to bring about negative attention upon their fellow directors. Furthermore, we illustrate the negative effects of director compensation on their desire to resign in protest. Finally, we highlight potential limitations on firms to disclose outspoken resignations.

A. Director Limitations

1. *Breach of Fiduciary Duties*

Despite the courts' recognition of their right to resign,[89] directors are limited in their ability to exercise this right. One such limitation is the possibility to incur personal liability for breaching their fiduciary duties when resigning from their position. The courts have long recognized limitations to the abilities of directors to resign depending on the company's condition prior to and following their departure.[90] With that, there is no legislative framework that governs the circumstances under

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[86] Jennifer B. Lawrence & Jackson W. Prentice, *The SEC Form 8-K: Full Disclosure or Fully Diluted? The Quest for Improved Financial Market Transparency*, 41 WAKE FOREST L. REV. 913, 915 (2006).

[87] *Id.*, at 917.

[88] Fuqi, *supra* note 1; Puda Coal, *supra* note 6.

[89] In re Telesport Inc., *supra* note 25 ("Corporate officers are entitled to resign for a good reason, a bad reason, or no reason at all…"); Frantz Manufacturing Co. v. EAC Industries, 501 A.2d 401, 423 (Del. 1985) ("Directors are also free to resign").

[90] *See, e.g.,* Hagshenas v. Gaylord, 199 Ill. App. 3d 60 (1990); Sebastian v. Zuromski, 1993 WL 78713 (N.D. Ill. 1993) (citing *Hagshenas*, explaining that "even after resignation from corporate management, an officer and director of a closely held corporation was potentially liable for breach of fiduciary duties owed to his fellow shareholders"); Pearlie Koh, *Once a Director, Always a Fiduciary*?, 62 CAMBRIDGE L.J. 403, 409-10 (2003) (highlighting the duties of corporate directors post-resignation under the corporate opportunity doctrine).

which resignation in itself can breach a director's fiduciary duty, leaving directors vulnerable to personal liability amid legal uncertainty.[91]

Prior to 2013, the courts largely sufficed with the declaration that directors "cannot terminate their agency or accept the resignation of others if the immediate consequence would be to leave the interests of the company without proper care and protection."[92] Although this test, derived from case law, appears clear and practical, there is little elaboration regarding what constitutes "immediate consequence" and "without proper care and protection." Furthermore, applications of this test generally involved cases of blatant willful ignorance to immediate damages directors knew their respective companies were set to face.[93] As a result, the courts were not obliged to elaborate this criterion and often left the issue to later decisions.[94]

In 2013, two Delaware Chancery Court cases further expanded upon the possibility of directors to incur personal liability for resigning from their respective companies: *In re Puda Coal, Inc. Stockholders Litigation* and *Rich v. Chong (Fuqi)*.[95] In *Puda Coal*, three independent directors were accused of breaching their fiduciary duties after resigning from the company's board of directors.[96] Shareholders argued that the directors failed to properly intervene when becoming aware that the CEO and chairman appropriated and sold a majority of the company's assets to an affiliate without compensation. The directors, who comprised the audit committee that initially reported the chairman's actions, did not push to sue to recover the assets and instead resigned, leaving the chairman as

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[91] Directors are generally concerned that resigning from troubled firms can bring about personal liability, whether justified or not. *See* Katz & McIntosh, *supra* note 38.

[92] VICTOR MORAWETZ, A TREATISE ON THE LAW OF PRIVATE CORPORATIONS, §§ 563 (2nd ed. 1886); Gerdes v. Reynolds, 28 N.Y.S.2d 622 (1941); Zeltner v. Zeltner Brewing Co., 174 N.Y. 247, 253 (N.Y. 1903) ("[Morawetz] supports the view above expressed with the statement: 'It seems clear, also, that directors cannot terminate their agency or accept the resignation of others if the immediate consequence would be to leave the interests of the company without proper care and protection'").

[93] These cases often involved extraordinary circumstances, including knowledge of impending looting and raids on corporate assets. S*ee, e.g.,* DePinto v. Landoe et al., 411 F.2d 297 (9th Cir. 1969) (highlighting that directors are unable to resign so to avoid opposing impeding raids on the firm's corporate assets); Benson v. Braun et al., 155 N.Y.S.2d 622, 626 (N.Y. S.Ct. 1956) (explaining that directors cannot resign knowing that their successors seek to loot the company); Byron F. Egan, *Fiduciary Duties of Corporate Directors and Officers in Texas*, 43 TEX. J. BUS. L. 45, 189 (highlighting that the test that arose from *Gerdes* largely develops liability only in circumstances of particularly severe and foreseeable harm).

[94] *See, e.g.,* Sebastian v. Zuromski, *supra* note 90 ("It is not inconceivable that fiduciary duties may obligate a person not to abandon a venture such as a partnership or close corporation"). As we explain in this chapter, the later Delaware cases were similarly notable in that they were brought in the motion-to-dismiss stage.

[95] Fuqi, *supra* note 1; Puda Coal*, supra* note 6.

[96] *See* Katz & McIntosh, *supra* note 38.

the sole remaining director.[97] As a result, the directors could absolve themselves of personal liability.

Chancellor Strine denied the directors' motion to dismiss the claims of breach of fiduciary duty, explaining that the directors knowingly chose to quit and leave the company "under the sole dominion of a person they [believed had] pervasively breached his fiduciary duty of loyalty."[98] Chancellor Strine elaborated that there are circumstances of resignations that do not absolve directors of liability, and decreed that a situation such as that of *Puda Coal* may warrant such a decision.[99] Furthermore, Chancellor Strine explained that even with evidence of directors attempting to act in good faith (e.g., attempts to investigate prior to being stonewalled by management), those same directors could still conceivably be held liable.[100]

The possibility of liability for breach for resigning became evermore evident in *Rich v. Chong*, where directors failed to act against inadequate internal controls. There, the company, over two years, saw directors resign *en masse* in protest to its mishandling of an audit committee investigation meant to remedy internal misbehavior and lackluster adherence to governance procedures.[101] Shareholders filed a derivative suit against the directors, arguing that they systemically failed to maintain adequate internal controls, make efforts in good faith to remedy these inadequacies, and prevent the company from presenting shareholders with misleading financial statements.[102]

Vice Chancellor Glasscock rejected the directors' motion to dismiss, suggesting that the directors may have abdicated their duties by failing to further effective investigations and remedy the company's internal misbehaviors. Directors missed apparent "red flags" and failed to consciously act to prevent further wrongdoing, as required by their duty of loyalty.[103] Vice Chancellor Glasscock referred back to Chancellor Strine's ruling in *in re Puda Coal, Inc*. and illustrated the issue with directors

[97] Puda Coal, *supra* note 6, at 13.
[98] *Id.,* at 16.
[99] *Id.*, at 19.
[100] *Id*., at 16.
[101] Fuqi, *supra* note 1.
[102] *Id.*
[103] *Id.*, at 983. Abdication of a director's formal duties can constitute a breach of duty of loyalty and a lack of good faith. *See* In re Pattern Energy Grp. S'holders Litig., C.A. No. 2020-0357-MTZ (Del. Ch. May. 6, 2021). Vice Chancellor Glasscock referenced the tests required by a director's duty of oversight, commonly referred to as *Caremark* claims. *See* In re Caremark International Inc. Derivative Litigation, 698 A.2d 959 (Del. Ch. 1996). This duty, an aspect of a director's duty of loyalty, is breached when directors (1) fail to implement effective reporting or information systems or controls, or (2) having implemented such systems, consciously fail to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention. *See* Stone v. Ritter, 911 A.2d 362, 370 (Del. 2006).

abandoning troubled companies to the sole control of those who do not further the company's interests.[104]

Both *Puda Coal, Inc.*, and *Rich v. Chong* illustrate that directors, including those who unsuccessfully attempt to remedy internal misbehaviors, can face personal liability for resigning from their positions. Directors who utilize their right to resign, even in protest to internal misbehavior as in *Rich v. Chong* or following attempts to investigate as in *Puda Coal*, are not exonerated from liability for their departure, despite circumstances that may justify their resignation. The result is that directors are deterred from resigning from their positions, limiting the ability of directors to use their right to resign to further necessary changes within their respective companies or to protect themselves from forthcoming lawsuits.

This limitation is especially difficult due to the uncertainty that remains after the introduction of these cases. Neither in *Puda Coal* nor in *Rich v. Chong* does the court establish clear and effective subtests to determine when resignation becomes a breach of fiduciary duty, as these discussions occurred at early stages in the respective suits.[105] As a result, directors who consider utilizing their right to resign are left unaware of which circumstances justify their resignation and which require them to remain present.

As seen in *Rich v. Chong*, the ability to resign as a form of protest to corporate misbehavior is hampered, leaving unsatisfied directors with one less tool at their disposal to fulfill their fiduciary duties. The firm saw two directors explicitly resign due to management's mishandling of the audit committee investigation, as well as another who resigned due to management engaging an accounting firm without approval from the audit committee.[106] However, these directors were not differentiated from those who resigned quietly or failed to highlight internal misbehaviors within the firm.[107] Consequently, directors are not only deterred from resigning, but also specifically from resigning in protest. Those who do may face legal repercussions alongside other negative

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[104] *Id.*, at 981.

[105] In both cases, judgments were brought in the motion-to-dismiss stage, in which the judges were not obligated to come to a definite ruling regarding the liability of the former directors. As a result, both cases fail to provide specific tests that govern the connection between resignation and fiduciary duties. For example, the courts fail to highlight necessary actions which directors must take to avoid liability. Similarly, there is no differentiation between directors who act in good faith to remedy misgivings and those who make performative steps to avoid scrutiny. The result is that directors are left with no feasible guidance to avoid suits for breach of fiduciary duty.

[106] SEC Filing, i.e. Fuqi International, Inc., Current Report (Form 8-K) (Jan. 27, 2012). We note that other Form 8-K disclosures around this time largely highlighted "personal reasons" for the reason behind departure. *See, e.g.,* SEC Filing, i.e. Fuqi International, Inc., Current Report (Form 8-K) (Jun. 16, 2011); SEC Filing, i.e. Fuqi International, Inc., Current Report (Form 8-K) (Jul. 30, 2011); SEC Filing, i.e. Fuqi International, Inc., Current Report (Form 8-K) (Jan. 16, 2012); SEC Filing, i.e. Fuqi International, Inc., Current Report (Form 8-K) (Mar. 31, 2012).

[107] *Id.*

effects that outspoken resignation has on departing directors, as we explain below.

2. *Personal Reputation*

Reputation serves an important role in directorship, whether in the director's personal value in the market or in their ability to fulfill their positions. Preservation and enhancement of reputation is a primary factor for directors in the labor market.[108] Directors are often appointed based on their reputations, and as such they are keen on maintaining a positive image.[109] This also serves directors in their roles, as boards with more respected directors engage better with investors and stakeholders.[110] As a result, directors are hesitant to further decisions that may negatively impact their reputation, including resigning in protest.

Personal reputation can limit the desire of directors to outspokenly depart. Directors who resign in protest are often perceived as "troublemakers" in the director labor market, finding themselves unable to attain future employment.[111] Outside firms are wary of voluntarily bringing upon themselves public controversy. Thus, they are hesitant to sign on directors who previously spoke out and generated negative market reactions against their former employers. For example, Marshall found that directors who resign in protest suffer a net loss of 85% in board seats in the five-year period following the disagreement.[112] Despite the aforementioned governance advantages in outspoken director

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[108] Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 J.L. ECON. 301, 315 (1983). Masulis and Mobbs frequently highlight the effect of reputational incentives on the motivation of directors to fulfill their duties. *See, e.g.,* Ronald W. Masulis & Shawn Mobbs, *Independent Director Incentives: Where Do Talented Directors Spend Their Limited Time and Energy?*, 111 J. FIN. ECON. 406 (2014); Ronald W. Masulis & Shawn Mobbs, *Influential Independent Directors' Reputation Incentives: Impacts on CEO Compensation Contracts and Financial Reporting*, 82 J. CORP. FIN 1 (2023). Likewise, professional reputation affects future directorships, specifically as it relates to negative exposure. *See, e.g.,* Eliezer M. Fich & Anil Shivdasani, *Are Busy Boards Effective Monitors*, 61 J. FIN. 689 (2006) (discussing the effect of shareholder lawsuits on directorships); Vyacheslav Fos & Margarita Tsoutsoura, *Shareholder Democracy in Play: Career Consequences of Proxy Contests*, 114 J. FIN. ECON. 1 (2014) (highlighting the effect of proxy contest nominations on directorships); Jin-hui Luo & Yue Liu, *Does the Reputation Mechanism Apply to Independent Directors in Emerging Markets? Evidence from China*, 16 CHINA J. ACC. RES. 1 (2023).

[109] Fabian Gogolin, Mark Cummins, & Michael Dowling, *The Value of Director Reputation: Evidence from Outside Director Appointments*, 27 FIN. RES. LETTERS 266 (2018).

[110] Lex Suvanto, *Should a Board Have a Reputation?*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 9, 2018) https://corpgov.law.harvard.edu/2018/08/09/should-a-board-have-a-reputation/.

[111] Bar-Hava et al., *supra* note 39, at 5; Marchetti, Siciliano & Ventoruzzo, *supra* note 36, at 674 (explaining that dissent impacts director reputation); Hsin-Ti Chang, *Dissenting Opinions of Independent Directors in Taiwan: An Empirical Study*, 15 U. PA. ASIAN L. REV. 1, 18 (2019) (describing the manner in which dissent creates a 'troublemaker' reputation).

[112] Marshall, *supra* note 69.

resignations, the director labor market does not positively react to their departures.

Directors' reputations are particularly impacted when their departures arise from fraud-related circumstances. Following incidents of financial fraud, for example, directors experience significant declines in future employment as directors.[113] This decline is especially potent when the fraud is more severe and when the director bears greater responsibility for failing to monitor such misbehavior within the firm.[114] As a result, directors are wary of publicizing fraud-related disagreements with the firm and exposing themselves to "blacklisting" in the labor market.[115]

Interestingly, recent studies have shown a surprising trend regarding outspoken director resignation and future employment: directors are rewarded in the labor market for dissent that occurs during their directorship yet are negatively affected when dissenting through resignation. For example, Jiang, Wan, and Zhao found that director dissent is eventually rewarded in the director labor market through increased outside opportunities and lowered risk of regulatory sanctions.[116] Directors who air dissenting opinions are favored by firms as critics and decision makers, individuals who provide necessary contrast and board diversity.[117] Likewise, they anticipate regulatory scrutiny by pushing to remedy internal misconduct within the firm prior to public exposure. Yet, as shown above, directors who dissent upon departure are ostracized in the labor market.

Furthermore, directors' reputations may suffer from public criticism that arises from resigning in protest. Directors, when outspokenly departing from the firm, expose internal misgivings to the public eye, encouraging scrutiny over the details that led up to the aforementioned disagreement. In turn, directors incidentally open themselves to

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113 Eliezer M. Fich & Anil Shivdasani, *Financial Fraud, Director Reputation, and Shareholder Wealth* 86 J. FIN. ECON. 306 (2007).

114 *Id.*

115 This, especially because firms are quick to remove officers who were adjacent to such events. For example, Karpoff et al. found in their sample that over 90% of individuals who were identified as responsible for financial misrepresentation during SEC enforcement proceedings lost their positions. *See* Jonathan M. Karpoff, D. Scott Lee, and Gerald S. Martin, *The Consequences to Managers for Financial Misrepresentation*, 88 J. FIN. ECON. 193 (2008).

116 Wei Jiang, Hualin Wan, & Shan Zhao, *Reputation Concerns of Independent Directors: Evidence from Individual Director Voting*, 29 REV. FIN. STUD. 655 (2016).

117 Daniel Ferreira, *Board Diversity, in* CORPORATE GOVERNANCE: A SYNTHESIS OF THEORY, RESEARCH, AND PRACTICE 225, 227 (H. Kent Baker & Ronald Anderson eds., 2011); Mariateresa Torchia, Andrea Calabro & Michele Morner, *Board of Directors' Diversity, Creativity, and Cognitive Conflict*, 45 INT'L STUD. MGMT. & ORG. 6, 8 (2015); Marchetti et al., *supra* note 36; Daniel P. Forbes & Frances J. Milliken, *Cognition and Corporate Governance: Understanding Boards of Directors as Strategic Decision-Making Groups*, 24 ACAD. MGMT. REV. 489 (1999); Maretno Harjoto & Indrarini Laksmana, *Board Diversity and Corporate Social Responsibility*, J. BUS. ETHICS 1 (2015) ("…board diversity enhances firms' ability to satisfy the needs of their broader groups of stakeholders").

criticisms relating to the fulfillment of their position, whether it be claims of failed oversight or mismanagement.[118] If directors are somewhat involved in the events resulting in their outspoken resignation, they are even further incentivized to remain silent and minimize public exposure.

This further culminates due to the fear of liability that directors face when resigning from their positions, as discussed above. Directors do not wish to encourage public scrutiny that may expose themselves to potential lawsuits, especially amid the aforementioned legal uncertainty that directors face in lawsuits for breach of fiduciary duty. Litigation serves as a reputational risk,[119] especially since claims of breach negatively affect the perception of stakeholders, and society at large, regarding the resigning director.[120] Subsequently, directors prefer to limit public exposure and preserve their personal reputations.

The concern with reputation is that directors will maximize their personal interests at the expense of shareholders, whose interests they are hired to represent.[121] This creates an agency problem between directors and shareholders, whose interests deviate due to non-professional factors like personal reputation. The result is that shareholders are negatively affected, specifically in that directors are wary of utilizing their right to resign in protest as a governance tool against internal misconduct. This becomes especially apparent when directors are responsible for monitoring the exact situations which caused them to

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[118] Journalists and other media bodies often hunt for corporate scandals, and so outspoken resignations can push directors into the eyesight of these headhunters. When news media reports governance crises, like those that arise from director resignations, the result is that the public, and future employers, associate the departing director with the "scandal," creating a negative perception of the director in the public eye. *See, e.g.,* Dyck & Zingales, *supra* note 47; Boris Groyberg et al., *The Scandal Effect*, HARV. BUS. REV. ONLINE (2016) https://hbr.org/2016/09/the-scandal-effect. For discussions on the hunt for corporate scandals, *see* Kathleen F. Brickey, *From Boardroom to Courtroom to Newsroom: The Media and the Corporate Governance Scandals*, 33 J. CORP. L. 625 (2008); Michael J. Borden, *The Role of Financial Journalists in Corporate Governance*, 22 FORDHAM J. CORP. FIN. L. 311 (2007).

[119] Asaf Eckstein & Gideon Parchomovsky, *The Agent's Problem*, 70 DUKE L. J. 1509, 1544-1551 (2021).

[120] Roy Shapira, *Reputational Theory of Corporate Law*, 26 STAN. L. POL. REV. 1, 10 (2015); Dain C. Donelson, *The Merits of Securities Litigation and Corporate Reputation*, 41 CONTEMP. ACC. RES. 424 (2024) (discussing the negative effects of meritorious litigation on corporate reputation); Roy Shapira, *Reputation Through Litigation: How the Legal System Shapes Behavior by Producing Information*, 91 WASH. L. REV. 1193 (2016) (highlighting the connection between legal and reputational sanctions of market participants).

[121] Bar-Hava et al., *supra* note 39; Rudiger Fahlenbrach, Angie Low, & Rene M. Stulz, *The Dark Side of Outside Directors: Do They Quit Ahead of Trouble?,* (NBER Working Paper No. w15917, 2010), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1590746. Directors are required by their fiduciary duties to act in the interests of shareholders. *See supra* note 3. However, personal reputational considerations deter directors from prioritizing these interests, as highlighted above.

resign, as they do not wish to suffer "reputational penalties" for oversight failures.[122]

It is important to note that several studies have determined a positive reputation vector that may encourage directors to resign, specifically in protest. For example, some studies show that director resignation increases with reputation and weak firm performance.[123] In anticipation of public criticism of management, particularly as a result of internal misconduct, directors may feel inclined to "jump ship" and preserve their reputations by departing from the firm.[124] In the context of outspoken resignation, Dewally and Peck found that "public resignations are motivated by the reputational concerns of directors."[125] As a result, some may argue that the negative effect of reputation on director resignations is minimized by the converse positive reputation vector.

To this, we offer several responses. First, we argue that the positive reputation vector is minimized by the aforementioned fear of breach of fiduciary duty. Directors who resign in an attempt to "jump ship" and shield themselves from public criticism are not immune from personal liability for the misconduct that occurred during their tenure.[126] Therefore, directors can be drawn into the public eye by shareholders who wish to hold them accountable for breach, even after the fact. The result is that anticipatory resignation, especially when publicized, can bring about unintended consequences for the director, limiting their desire to outspokenly depart.

Second, we highlight the difference between the reputational concerns of inside and outside directors. In their 2009 study, Asthana and Balsam found that the positive reputation vector is weaker for inside directors due to the effects of bonding with the firm and compensation.[127] And, although outside directors are susceptible to "jumping ship," they are also particularly susceptible to the negative reputation vector illustrated in this chapter.[128] Outside directors are

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[122] Dewally & Peck, *supra* note 47, at 51; Jun Du et al., *Does Independent Directors' Monitoring Affect Reputation? Evidence from the Stock and Labor Markets*, 11 CHINA J. ACC. RES. 91, 92 (2018) ("…most of these studies have found that on average investors react negatively to these adverse signals of weak board monitoring and that independent directors suffer reputational penalties if they do not vigilantly monitor top management").

[123] Bar-Hava et al., *supra* note 39; Fahlenbrach, *supra* note 44, at 2315.

[124] Xiaodong Qiu & James A. Largay III, *When Outside Directors Resign: Go Publicly or Leave Quietly?,* 24 ACAD. MGMT. PERSPECTIVES 86 (2010); Preet Deep Singh & Chitra Singla, *Impact of Independent Directors' Resignations on Firm's Governance*, IIMA Working Papers WP2016-03-36, Indian Institute of Management Ahmedabad, Research and Publication Department (2016); Matthew Semadeni et al., *Fight or Flight: Managing Stigma in Executive Careers*, 29 STRAT. MGMT. J. 557 (2008).

[125] Dewally & Peck, *supra* note 47.

[126] *See supra* note 90.

[127] Sharad Asthana & Steven Balsam, *Determinants of Outside Director Turnover,* REV. ACC. FIN. (2013).

[128] We note that the absolute majority of literature discussing the negative reputation vector specifically describes outside/independent directors, suggesting a particularly powerful effect on these categories of directors. Coupled with Asthana and Balsam's

hailed as experts in decision control and governance, which means that firms place higher emphasis on their professional reputation at the date of appointment.[129] The result is that outside directors are particularly hesitant to resign, specifically in protest, in order to avoid diminishing their expert reputation and garnering public controversy.

Therefore, we argue that the negative reputation vector outweighs its positive counterpart in the directors' decision of whether to resign in protest. Subsequently, personal reputation is prioritized over the interests of shareholders, which goes against the principle of shareholder primacy prevalent in corporate law.[130] It should be noted that reputation is not a malevolent factor in of itself. Our concern is that it may deter good-faith directors from resigning in protest to governance failures within the firm, which benefits shareholders and society at large. In Part IV, we offer policy suggestions that are meant to balance the importance of director reputation while ensuring that it does not come at the expense of proper governance and shareholder interests.

3. *Structural Bias*

Structural biases in the boardroom may limit a director's desire to resign in protest. Directors are fiduciaries responsible for decision-making within the firm, and they are expected to act independently of irrelevant considerations.[131] However, directors are rational agents, and consequently are susceptible to conscious and unconscious biases that affect their decision making.[132] The concern is that directors, responsible for monitoring management and acting as gatekeepers within the firm, are unable to independently make decisions that align with the interests of the firm and its shareholders.[133] As a result, these biases will act against

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findings, the result is that the negative vector outweighs the positive. *See Id*; Bar-Hava et al., *supra* note 39; Fahlenbrach, *supra* note 44; Gogolin et al., *supra* note 109; Chang, *supra* note 111; Du et al., *supra* note 122; Singh, *supra* note 124.

[129] Jensen & Meckling, *supra* note 4.

[130] *See supra* note 2.

[131] Yaron Nili, *Out of Sight, Out of Mind: The Case for Improving Director Independence Disclosure*, 43 J. CORP. L. 35, 44 (2017) ("Indeed, in a widely held public company, it has become increasingly important that directors be independent of those controlling the firm's day-today operations—the managers—who have interests that at times might be adverse to those of shareholders"); Lucian A. Bebchuk & Assaf Hamdani, *Independent Directors and Controlling Shareholders*, 165 U. PA. L. REV. 1271, 1285 (2017) ("Independence requirements strengthen these market incentives by ensuring that directors have no conflicts that could undermine their effectiveness as monitors of management"); Jill E. Fisch, *Taking Boards Seriously*, 19 CARDOZO L. REV. 265, 265-266 (1997).

[132] Lisa M. Fairfax, *The Uneasy Case for the Inside Director*, 96 IOWA L. REV. 127, 152-153 (2010) (describing the natural biases that arise from board membership).

[133] Claire A. Hill & Brett H. McDonnell, *Disney, Good Faith, and Structural Bias*, 32 J. CORP. L. 833, 853 (2007) ("For all these reasons, the board's critical faculties may not be fully engaged because the directors are biased against corporate interests and in favor of the not-infrequently-differing interests of officers, controlling stockholders, fellow directors, or themselves").

the ability of directors to resign in protest and relay information to shareholders.

Board-decision making is vulnerable to a plethora of biases that impact directors' abilities to make effective, impartial choices. Directors can be negatively affected by external behavioral factors, including conflicts of interest, emotional attachments, dominant personalities, and anchored attitudes.[134] Decisions may also be impacted by directors' social ties, which may interfere with the ability of directors to carry out their fiduciary duties.[135]

When a director contemplates the decision to resign, specifically in protest, they are forced to consider the impact of their departure on directors who remain at the firm. Due to the negative market reactions and public criticism of directors that arises from outspoken resignation, directors may be hesitant to publicize their disagreement with the firm.[136] Despite their duties to inform shareholders of internal misconduct, directors may prefer to remain silent to maintain their relationships and protect their fellow board members.

Velasco, in his seminal work on biases in the boardroom, separates structural bias into three relevant paradigms – implicit conspiracy, relationship biases, and ingroup biases.[137] First, directors may pursue group interests regardless of their personal connection to the relevant benefit. This theory holds that directors may subconsciously favor each other out of solidarity or in expectation of similar treatment.[138] In the context of resignation, directors may naturally remain silent as a result of shared ideals with their former peers. For example, directors are naturally ill-disposed to shareholder litigation and public scrutiny.[139] Resignation in protest is likely to drag the board into the public eye, where firms may consequently face derivative suits by disgruntled investors and even enforcement action by authorities.[140] As a result, departing directors are inclined to resign quietly.

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[134] James D. Cox & Harry L. Munsinger, *Bias in the Boardroom: Psychological Foundations and Legal Implications of Corporate Cohesion*, 48 LAW & CONTEM. PROB. 83 (1985).

[135] Rachel A. Fink, *Social Ties in the Boardroom: Changing the Definition of Director Independence to Eliminate "Rubber-Stamping" Boards*, 79 S. CAL. L. REV. 455 (2006). Likewise, the courts have recognized the ability of social ties to interfere with directors' decision-making. For example, the Delaware Court of Chancery discussed the possibility of social ties impacting a director's prioritization of shareholder interests. *See* In re. Oracle Corp. Derivative Litigation, 824 A.2d 917 (Del. Ch. 2003).

[136] Remaining directors will likely be subject to strict public scrutiny and reputational damage that affects the firm when a director resigns in protest. *See infra* Section II.B.

[137] Julian Velasco, *Structural Bias and the Need for Substantive Review,* 82 WASH. U. L. Q. 821, 853-70 (2004).

[138] In its strong form, directors may pursue general immediate interests that benefit the group, like utilizing their control to preserve their positions of power within the firm. In its weak form, directors may act together as a result of sharing similar ideals, which consequently align their interests in the decision-making process. *See Id.*, at 856-857.

[139] *Id.*, at 857.

[140] Eckstein & Parchomovsky, *supra* note 33, at 814-16.

Second, directors may favor each other out of friendship and/or collegiality.[141] Boards are often comprised of directors who serve for a number of years and foster connections with one another.[142] This is especially true when they come from similar professional or academic backgrounds. The result is that directors create personal relationships that may affect their ability to make impartial decisions in the interests of shareholders.[143] Directors who are frustrated with the firm's policies or practices may be disincentivized from speaking out if their resignation negatively impacts their peers. They may be hesitant to generate conflict surrounding the firm and the board, especially due to their desire to maintain their social capital within the boardroom and the industry.[144] As a result, directors are unable to carry out their fiduciary duties, and shareholders are underprioritized.

Third, directors may suffer from unconscious favoritism stemming from a psychological phenomenon known as ingroup bias. This phenomenon holds that individuals tend to favor others within their group than those outside of it.[145] This bias is especially prevalent among directors, due to their relative homogeneity, cultural familiarity, and shared experience as holders of desirable professional positions.[146] Directors subconsciously identify with their boardroom peers, and as a result are inclined to protect the members of their group. Similar to the effects of implicit conspiracy and relationship bias, ingroup sentiment restricts directors from resigning in protest and negatively impacting the remaining directors with whom they identify.

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[141] Jill E. Fisch, *The Overstated Promise of Corporate Governance*, 77 U. CHI. L. REV. 923, 928 (2010) ("Corporate boards are, [Jonathan Macey] claims, subject to capture as a result of management ties, cognitive biases, and social norms that undermine directors' ability to exercise independent judgment… directors are, for example, bound by norms of collegiality that make it difficult to question management"); JONATHAN R. MACEY, CORPORATE GOVERNANCE: PROMISES KEPT, PROMISES BROKEN 61 (2008).

[142] Yaron Nili, *The Fallacy of Director Independence*, 2020 WISC. L. REV. 491, 504 (2020) ("Having the significant human capital, social ties, and reputation invested in the corporation that long-term directors have culminated over time might compromise independent directors' willingness to act independently or hold insiders accountable").

[143] *Id.*; Fink, *supra* note 135; James D. Westphal, *Collaboration in the Boardroom: Behavioral and Performance Consequences of CEO-Board Social Ties*, 42 ACAD. MGMT. J. 7 (1999).

[144] *See, e.g.,* Reed E. Nelson, *The Strength of Strong Ties: Social Networks and Intergroup Conflict in Organizations*, 32 ACAD. MGMT. J. 377 (1989).

[145] Rupert Brown, *Social Identity Theory: Past Achievements, Current Problems and Future Challenges*, 30 EUR. J. SOC. PSYCH. 745, 747 (2000); Miles Hewstone, Mark Rubin, & Hazel Willis, *Intergroup Bias*, 53 ANN. REV. PSYCH. 575 (2002) ("Intergroup bias refers generally to the systematic tendency to evaluate one's own membership group (the in-group) or its members more favorably than a nonmembership group (the out-group) or its members").

[146] Cox & Munsinger, *supra* note 134. It should be noted that there is a recent trend away from homogenous corporate boards, which aims to diversify directors through gender, race, ideology, etc. *See, e.g.,* Anzhela Knyazeva, Diana Knyazeva, & Lalitha Naveen, *Diversity on Corporate Boards*, 13 ANN. REV. FIN. ECON. 301 (2021); Yaron Nili, *Beyond the Numbers: Substantive Gender Diversity in Boardrooms*, 94 IND. L. J. 145, 167 (2019).

Consequently, these biases negatively affect corporate governance within the firm.[147] Social-psychological prejudices undermine the ability of the board to monitor management and fulfill their role as impartial gatekeepers.[148] This extends to director departure, in which directors are inclined to resign in opposition to internal misconduct within the firm yet are limited due to inherent biases in the boardroom. The result is that shareholders are prevented access to pertinent information regarding the firm due to personal biases that are not relevant to the decision whether or not to resign in protest.

4. *Financial Incentives*

Financial incentives may play a significant role in deterring outspoken director resignations. Directors often receive compensation packages that allow them to obtain equity stakes in the firm, limiting their desire to publicize disagreements with the firm upon resignation and consequently hurt the firm's stock performance. Similarly, directors and other corporate officers are generously compensated, and as such they may prefer to protect their financial interests and refrain from utilizing their right to resign in protest.

Over the past few decades, director compensation has trended towards more diverse methods of payment.[149] Public firm directors are often rewarded with equity compensation from the firm, whether in the form of stock awards or options.[150] In fact, equity compensation in 2023 comprised around 63% of director pay.[151] Directors are increasingly becoming shareholders of the firm, resulting in salaried watchdogs who also benefit from positive changes in the firm's stock price.

As a result, directors are consequently incentivized to avoid policies or practices that negatively affect the firm's stock performance.[152]

[147] This is especially true regarding independent directors, who are hailed as impartial decision-makers that monitor issues like bias within the boardroom. However, they too are susceptible to biases, which negatively affects their "independent" status. *See* Nili, *supra* note 142.

[148] Bainbridge & Henderson, *supra* note 38, at 1098 ("…the final key function of modern boards is to serve as a monitor of management"). *See also* Fama & Jensen, *supra* note 56 (describing their roles as monitors); John C. Coffee, *The Acquiescent Gatekeeper: Reputational Intermediaries, Auditor Independence and the Governance of Accounting* (Colum. L. Econ., Working Paper No. 191, 2001) (describing their roles as gatekeepers).

[149] Lawrence A. Cunningham & Carlos Suarez, *Trends in Director Compensation*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jan. 26, 2024) https://corpgov.law.harvard.edu/2024/01/26/trends-in-director-compensation/.

[150] *Id.*

[151] BDO, The BDO 600: 2023 Study of Board Compensation Practices of 600 Mid-Market Public Companies (Oct. 2023), https://insights.bdo.com/2023-BDO-600.html.

[152] On one hand, equity-based compensation can often assist in aligning shareholder and director interests. *See, e.g.,* Stephen M. Bainbridge, *Director Primacy and Shareholder Empowerment*, 119 HARV. L. REV. 1735, 1741 (2006) ("For example, directors are increasingly paid in stock, which helps align director and shareholder interests"). On

Directors stand to gain from higher firm value, both through direct returns from the stock's value and through increased value in the labor market.[153] However, outspoken director resignation negatively affects the firm's stock price, consequently influencing the director's equity-based compensation.[154]

The result is that directors are inclined to avoid resigning in protest so to avoid the negative financial effects that follow such departures. Directors who are frustrated with the firm's policies or practices may prefer to resign quietly and avoid negatively impacting the stock awards they received in their compensation packages.[155] This is especially true considering that directors often receive stock options as part of their pay,[156] and resigning in protest would lower the stock price prior to the realization of their options. As a result, directors may prefer to quietly resign prior to realizing their options to maximize their value.

In addition, directors seek to protect the financial benefits they receive from their position. Directors are generously compensated in the labor market, earning compensation packages that often sum up to hundreds of thousands of dollars.[157] Directors who resign in protest both impede their immediate financial compensation from the firm and, as we explained above, minimize their ability to find future employment in the director market.[158] Once their reputational value is minimized, their future compensation is similarly affected.[159] The result is that outspoken directors are negatively affected financially in multiple ways, limiting their desire to resign in protest.

B. Firm Limitations

Firms also have several limitations that inhibit their desire to disclose resignations as "outspoken" – in other words, disclosures that highlight disagreement between the departing director and the firm. This includes financial, reputational, and legal incentives that diminish the firm's inclination to encourage outspoken director resignations. These

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the other hand, equity-based compensation can disincentivize outspoken resignations, which we argue does not coincide with shareholder interests.

153 Directors who hold stock options directly earn from increased firm performance, and vice versa. *See* David Yermack, *Renumeration, Retention, and Reputation Incentives for Outside Directors*, 59 J. FIN. 2281 (2005).

154 See, *e.g.,* Fahlenbrach, *supra* note 44.

155 Assaf Hamdani & Reinier Kraakman, *Rewarding Outside Directors*, 105 MICH. L. REV. 1677, 1683 (2007) ("Equity holdings reduce a director's incentive to uncover and disclose wrongdoing because doing so will normally depress share price").

156 Connor Damon, Jasper Luong, & Rachel Chiu, *2023 Director Compensation Report,* FW Cook (Oct. 17, 2023), https://www.fwcook.com/Publications-Events/Research/2023-Director-Compensation-Report/.

157 For example, we can take our empirical sample – directors in the S&P 500. Directors in these firms in 2023 were compensated on average with $321,220. Even outside the S&P 500, directors earned an average of $193,142. *See* Cunningham & Suarez, *supra* note 149.

158 *See supra* Section II.A.2.

159 Marshall, *supra* note 69.

limitations are more intuitive than those that affect the director, and as such will prompt a briefer discussion.

Firms may prefer to limit outspoken disclosures in light of the adverse effects of director resignations. Director resignations, especially outspoken versions, often lead to negative market reactions, including lowered stock performance, increased shareholder litigation, negative return events, worse mergers and acquisitions, and increased public scrutiny.[160] As a result, firms are likely to minimize their disclosure to avoid the market response.[161]

The stock-price effect is two-fold: firms with reduced stock performance are likely to trigger market responses for control and lead to hostile takeovers, in which outside buyers purchase controlling blocks or significant percentages of shares and remove incumbent officers to replace them with their own nominees.[162] This reflects back onto both the firm and its remaining officers, as they are increasingly susceptible to the risk of dismissal. Consequently, management and other directors may prefer to limit outspoken disclosures and prevent external market pressures.

Furthermore, resignations in protest, as we explained above, are likely to push the firm into the eyes of the media, analysts, and private plaintiffs.[163] Corporate media journalists hunt for exposés that negatively affect the firm's reputation, and investors react accordingly.[164] Media attention can dramatically impact investors' responses to the relevant misgivings, at times culminating in shareholder litigation.[165] Due to such external pressures, firms prefer to reduce public exposure to internal controversies that cause directors to resign.

Firm are especially hesitant because outspoken resignations are likely to drive enforcement authorities, like the SEC, to investigate possible enforcement actions against the firm. Beyond the direct penalties derived

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[160] Fahlenbrach, *supra* note 44; Jiang, *supra* note 116 (showing how dissent improves stock price efficiency and market transparency); Fahlenbrach 2010, *supra* note 121.

[161] *See*, *e.g.*, Carter & Soo, *supra* note 56. Carter & Soo analyze 5,736 Form 8-K filings in 1993, highlighting that over 26% were submitted after the due date, with negative filings, like director resignations, being postponed beyond said date. *See Id.,* at 120. This, they argue, highlights the manner in which timeliness affects the disclosure's informativeness to shareholders.

[162] Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110, 112-14 (1965).

[163] *See supra* Section II.A.2.

[164] *See supra* note 118.

[165] *See, e.g.*, Rick Cazier et al., *Media Sentiment and Shareholder Litigation* (2022), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4119585 (highlighting the effect of negative media sentiment on the likelihood of shareholder litigation regarding restatement announcements); S.P. Kothari, Xu Li, & James E. Short, *The Effect of Disclosures by Management, Analysts, and Financial Press on Cost of Capital, Return Volatility, and Analyst Forecasts: A Study Using Content Analysis*, 84 ACC. REV. 1639 (2009) (illustrating the effect of financial reporting on investors' response to disclosed events).

from securities regulation,[166] SEC investigations can prove costly for the firm in the market: regulatory proceedings may be followed with derivative suits,[167] significant stock price reactions,[168] and executive turnover.[169] Firms, and their officers, are subsequently incentivized to limit outspoken disclosures to avoid "catching the eye" of securities regulators.

To prevent this snowball effect, firms will likely utilize silent disclosures of director resignations that do not expand upon conflicts between the firm and the departing director. Here, the concern is that the firm, which is responsible for issuing the disclosure and whose officers are more knowledgeable about the firm's day-to-day affairs,[170] will intentionally minimize exposure of these circumstances to less informed shareholders and regulators. Similarly, directors are likely hesitant to come out publicly and counter the firm's disclosure, due to the limitations we discussed above.[171]

As a result, we hypothesize that outspoken disclosures in the market are few in number.[172] Both directors and firms have multiple incentives to keep disclosure of departures silent, limiting external parties like shareholders and regulators from accessing such information. In the next part, we will present the empirical analysis we undertook to determine the frequency of outspoken director resignations in light of these potential limitations.[173]

III. EMPIRICAL ANALYSIS

Despite the aforementioned benefits of outspoken director resignation, we were concerned with the practical effects of the theoretical vectors discussed in Part II on director departures. To

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166 SEC enforcement actions regularly include costly civil penalties for firms that engage in violative conduct. *See* David Rosenfeld, *Civil Penalties Against Public Companies in SEC Enforcement Actions: An Empirical Analysis*, 22 U. PA. J. BUS. L. 135 (2019).

167 In this context, academic studies have analyzed how shareholder derivative litigation follows FCPA investigations. *See, e.g.*, Amy Deen Westbrook, *Double Trouble, Collateral Shareholder Litigation Following Foreign Corrupt Practices Act Investigations*, 73 OHIO ST. L. J. 1217, 1228 (2012); Gabriela Jara, *Following on the Foreign Corrupt Practices Act: The Dynamic Shareholder Derivative Suit*, 63 DUKE L. J. 199 (2013).

168 Stephen J. Choi & Adam C. Pritchard, *SEC Investigations and Securities Class Actions: An Empirical Comparison*, 13 J. EMPIRICAL LEGAL STUD. 27, 29 (2016); Jonathan M. Karpoff, D. Scott Lee, & Gerald S. Martin, *The Cost to Firms of Cooking the Books*, 43 J. FIN. QUANT. ANAL. 581 (2008) (highlighting the costs of SEC enforcement actions on firm stock performance).

169 *See, e.g.*, Karpoff et al., *supra* note 115 (highlighting the effects of SEC enforcement proceedings on executive turnover).

170 Eckstein & Parchomovsky, *supra* note 33, at 834.

171 *See supra* Section II.A.

172 In addition to our empirical hypothesis, we offer policy implications related to increased disclosure requirements and SEC enforcement that are applicable to our theoretical analysis (and as we later show, our empirical findings). *See supra* Sections IV.A-B.

173 *Id.*

connect our theoretical discussion to the real-world director labor market, we tested our assumption thorough a comprehensive empirical analysis of director resignations and their disclosures.

In this part, we show that disclosures of director resignation that arise from "disagreement with the company's operations, policies, or practices" are particularly rare in number.[174] We highlight that in the few cases where departures were disclosed as arising from disagreement, said disclosure was preceded by public awareness to the relevant dispute. Furthermore, we highlight unique trends in the language used to describe director resignations. We show that firms often use various types of phrasing to convey director resignations to the public, utilizing disclosure tone to mitigate the possible effects of director departures. Notably, firms tend to limit their disclosures when discussing director resignations, while they tend to expand their disclosures when discussing director appointments. Finally, we analyze test cases that highlight the disclosure disparity in practice.[175]

A. Sample and Methodology

To understand the frequency of outspoken director resignations in the current governance framework, we analyzed firm disclosures through SEC Form 8-K filings. Through the SEC EDGAR database, we hand-collected 54,404 Form 8-K disclosures from the currently listed S&P 500 companies between the years 2016-2024. Within this sample, we noted 10,090 Item 5.02 8-K filings and differentiated between filings relating to director resignation and those relating to other Item 5.02 topics, including appointment of corporate officers and compensatory agreements.

For each firm, we noted the number of 8-K filings, the number of Item 5.02 references, and the number of filings relating to resignation of directors or senior executives. Furthermore, we collected the number of phrasings used by each firm to describe resignations and the reported circumstances of each resignation. Finally, we hand-collected the number and circumstances of resignations disclosed as pertaining to disagreements with the company's "operations, policies, and practices."

Our findings regarding the rarity of outspoken resignation, as shown below, concur with the findings obtained in previous studies. For example, Marshall collected 278 director departures that arose from disagreement between the years 1994-2006.[176] Similarly, Bar-Hava et al.

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174 *See infra* Section III.B.

175 *See infra* Section III.C.

176 Marshall, *supra* note 69. Due to the SEC's EDGAR database being limited to data from 2001, we were not able to collect the exact number of disclosed resignations between 1994-2006. Regardless, we analyzed the number of resignations between 2001-2006 using a keyword search in the EDGAR database with the words {departure of director}, {Item 5.02}, and {resignation}. Through this keyword search, we managed to collect 5,553 resignations between Jan. 1, 2001, and Dec. 31, 2006. 278 out of 5,553 total resignations estimates to around 5%. Thus, even without the number of

found that disclosed incidences of disagreement upon resignation constituted only about 1.6% of the sample they collected between 2004-2012.[177]

We should highlight that our empirical analysis is unique in several different ways. First, we provide a comprehensive hand-collected analysis of firm disclosures that allow us to analyze trends in director resignation that were not previously available.[178] We were able to analyze various nuances in our findings, such as comparisons between the language used to describe director appointments versus their resignations. Second, our analysis enabled us to collect potential test cases that highlight the gap between firm disclosures and actual resignations in practice. Third, we highlight figures that are even lower than previous estimations in the corporate empirical literature relating to outspoken director resignations. Finally, our sample period is set after the 2013 Delaware decisions in *Puda Coal* and *Fuqi*, which created potential implications for resigning directors regarding their fiduciary duties.

B. Findings

In this subsection, we provide figures relating to the frequency of outspoken director resignations and the manner in which they were disclosed. We hand-collected 3,825 filings of S&P 500 firms pertaining to director and senior executive resignations between the years 2016-2024.[179] Within this dataset, we identified the number of resignations that were disclosed as pertaining to disagreement with the firm's "operations, policies, and practices," as required by the SEC.[180] To understand the number of outspoken resignations in our sample, we define "disagreement" as explicit statements within the firm's 8-K disclosure

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resignations between 1994-2001, we can understand that outspoken resignations are not particularly frequent.

[177] Bar-Hava et al., *supra* note 39, at 15.

[178] This Article differentiates itself from Bar-Hava's work in several different ways. First, Bar-Hava provides a strictly empirical analysis of resignation disclosures, specifically analyzing departures in the context of independent directors. This Article aims to provide a theoretical analysis that explains why directors as a whole are limited in their desire or ability to resign in protest. In addition, we provide policy implications that seek to increase outspoken director resignations. Second, Bar-Hava's paper deciphers resignation disclosures as a whole, making little reference to the benefits or necessity of outspoken director resignations. This Article seeks to illustrate why outspoken resignations ought to be more prevalent, why they are not currently so, and how to ensure that they become more commonplace. Finally, our empirical analysis differs in that we hand-collected Form 8-K disclosures, allowing us to take a more in-depth look into the language that firms utilize upon disclosure. *See Id.*

[179] Although SEC requirements for senior executives are not necessarily identical to that of directors, our focus is to highlight the overall discrepancy of outspoken resignations among corporate officers who are privy to information that shareholders cannot access. This includes senior executives, whose resignations can provide similar, and possibly even greater, material information to shareholders. *See* SEC Form 8-K Guidelines, *supra* note 35.

[180] *See supra* Section I.B.

that point to disputes between the firm and the director adjacent to the date of departure. As such, filings that did not specify whether the resignation arose from disagreement were listed as "silent director resignations."

We found that out of 3,825 director and senior executive resignations from current S&P 500 firms between the years 2016-2024, only 4 were disclosed as resignations pertaining to "disagreement." In other words, only 0.1% of resignations in the sample period were "outspoken," in the sense that they were disclosed as pertaining to disagreement between the firm and the departing director. The aforementioned "outspoken" resignations are as such: 6 simultaneous resignations in protest from Williams Companies Inc. in 2016,[181] 4 simultaneous resignations in protest from Bio-Rad Laboratories, Inc. in 2017,[182] Dominique Mielle's resignation in protest from PG&E Co. in 2020,[183] and Steven Shulman's resignation in protest from Walgreen's Boots Alliance Inc. in 2022.[184]

The Williams Companies Inc. saw six directors simultaneously resign from the board in 2016 in protest to an unsuccessful attempt to oust CEO Alan Armstrong from his position.[185] This included departures of high-profile figures such as the Chairman of the Board and the Chair of the Strategic Review Administrative Committee.[186] Directors frequently raised issues with Armstrong's leadership, and their concerns increased after a multi-billion dollar takeover deal with Energy Transfer collapsed the week of their departure.[187] The firm saw fluctuations in stock price and widespread media attention following the incident, encouraging management to overhaul the board and insert more independent directors.[188]

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[181] SEC Filings, i.e. The Williams Companies, Inc., Current Report (Form 8-K) (Jul. 1, 2016).

[182] SEC Filings, i.e. Bio-Rad Laboratories, Inc., Current Report (Form 8-K) (Mar. 7, 2017).

[183] SEC Filings, i.e. PG&E Corporation, Inc., Current Report (Form 8-K) (Jun. 30, 2020).

[184] SEC Filings, i.e. Walgreens Boots Alliance, Inc., Current Report (Form 8-K) (Dec. 7, 2022).

[185] Williams Co. SEC Filing, *supra* note 178.

[186] *Id.*, Exhibit 17.1.

[187] Leslie Picker, *Half of William's Board Resigns After Vote to Oust C.E.O. Falls Short,* N.Y. TIMES (Jun. 30, 2016) https://www.nytimes.com/2016/07/01/business/dealbook/half-of-williamss-board-resigns-after-vote-to-oust-ceo-falls-short.html.

[188] The firm saw a near 6% drop in stock price the week following the incident – from $21.63 on June 30th to $20.35 on July 7th. In the period following the resignations, the firm pushed for board enhancement and increased director independence. Eventually, the firm saw a near 50% increase in stock price in the months following. *See* Leslie Picker, *Williams Companies, Under Pressure, Continues Board Overhaul*, N.Y. TIMES (Sept. 27, 2016) https://www.nytimes.com/2016/09/27/business/dealbook/williams-companies-under-pressure-continues-board-overhaul.html.

In 2017, four directors resigned in protest from Bio-Rad Laboratories, citing "disagreements with the management of the company regarding executive personnel and corporate governance matters."[189] Despite relatively little media attention following their resignations, we noted governance issues within the firm prior to their departures, including paying out punitive damages for whistleblower retaliation following a former executive's exposure of the firm's violations of the Foreign Corrupt Practices Act.[190] Following the directors' departure, the firm pushed to elect several new independent directors to strengthen and diversify the board.[191]

Ten directors resigned from PG&E Co. in 2020, following demands from California Governor Gavin Newsom to replace the board and improve safety policies after filing for bankruptcy.[192] Departing director Dominique Mielle resigned in protest, citing disagreements over the firm's implementation of the governor's plan and their agreement to retain energy consulting company Filsinger Partners.[193] The departures were covered extensively, though Mielle's departure in particular saw little media attention.[194]

Lastly, Steven Shulman resigned from Walgreens' board of directors in 2022 following the firm's decision not to qualify Shulman as an independent director.[195] Shulman explained that the firm's inability to accept his independent qualifications resulted in several board meetings in which he was prevented from participating, specifically due to his non-independent status.[196] The result was that Shulman felt that he could not properly fulfill his fiduciary duties to the firm and its shareholders.[197] Interestingly, Shulman highlighted in his resignation letter that he "felt

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189 Bio-Rad Laboratories SEC Filing, *supra* note 182.

190 Wadler v. Bio-Rad Labs., Inc., 141 F. Supp. 3d 1005 (N.D. Cal. 2015). Despite being listed as an "outspoken" resignation in our sample, Bio-Rad's Form 8-K filing highlights the discrepancies in disclosure that we wish to illustrate. There were mentions of disagreement with governance practices and personnel, yet the firm omitted specifications and directors did not provide subsequent responses.

191 Bio-Rad Laboratories, *Bio-Rad Intends to Propose Three New Independent Directors* (Mar. 13, 2017) https://investors.bio-rad.com/press-releases/news-details/2017/Bio-Rad-Intends-to-Propose-Three-New-Independent-Directors-03-13-2017/default.aspx.

192 Ivan Penn, *PG&E Appoints a New Board As it Eyes Its Bankruptcy Exit*, N.Y. TIMES (Jun. 10, 2020) https://www.nytimes.com/2020/06/10/business/energy-environment/pge-new-board-gavin-newsom.html.

193 PG&E SEC Filing, *supra* note 180. Also, *see* Dominique Mielle letter, Exhibit 99.1.

194 This, likely due to the widespread media attention involving the circumstances that led up to PG&E's bankruptcy filing. The firm amassed billions of dollars in liability for wildfires created by its equipment, some resulting in the deaths of multiple individuals alongside damage to public property. *See* Penn, *supra* note 192.

195 Walgreens SEC Filing, *supra* note 184. This, due to the Nominating and Governance Committee's recommendation to do so, based on the Nasdaq listing rules and the firm's Corporate Governance Guidelines.

196 *Id.*, Exhibit 17-1.

197 *Id.*

compelled to express [his] frustration associated with [his] board service to [the firm's] shareholders."[198]

In addition, we noted differences in the language used to describe director resignations between the different firms. We found that firms often adhere to one of four phrases to illustrate the premature departure of directors or senior executives prior to their term expiration date – "resign," "retire," "leave," and "not stand for re-election." We analyzed the frequency and variability of phrasing by firm, and we found that 293 firms, approximately 58.6% of our sample, utilize three or more types of phrasing when describing director resignations in their Form 8-K filings.

We also compared differences in the phrasing used to describe director resignations against phrasing used to describe director appointments. We noted that firms often expand their disclosure pertaining to directors at the date of appointment and minimize their disclosure at the date of departure. Firms within our sample often highlighted director's qualifications, background, expertise, and professional characteristics when introducing them to investors. However, disclosures regarding resignation are limited to 1-2 sentences where the company makes little mention of the departing director's qualities or contributions.

Firms likely utilized different phrasings to mitigate the informativeness of their disclosures of director resignations. Companies can take advantage of their linguistic discretion to minimize the negative effects that may arise from their disclosures.[199] In the context of director resignations, firms appear to utilize certain linguistic choices, such as minimizing and varying their filings, to minimize the impact of the firm's disclosures on shareholders, investors, and other market participants.

Similarly, we found that in the rare cases where firms did provide disclosure of director resignations pertaining to "disagreement" with the firm, it occurred after the public was already exposed to the relevant dispute. For example, in the case of Williams Companies Inc., the Wall Street Journal reported that half of its directors resigned one day prior to the date of the Form 8-K filing.[200] Similarly, in the case of PG&E, investors were aware weeks ahead of the directors' impending resignations after the governor of California required that the company

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[198] *Id.*

[199] *See, e.g.*, Natasha Bernhardt et al., *Language in Financial Disclosures*, in HANDBOOK OF FINANCIAL DECISION MAKING 154 (Hilary Gilles & David McLean eds., 2023) (highlighting the use of linguistic choices in financial disclosures to strategically influence investors' and stakeholders' views of the firm).

[200] *See* Williams Co. SEC Filing, *supra* note 181; Liz Hoffman, David Benoit, & Alison Sider, *Nearly Half of Williams Directors Resign*, WSJ (Jun. 30, 2016) https://www.wsj.com/articles/nearly-half-of-williams-directors-resign-1467324568. The directors voted in favor of an $20 billion external takeover deal by Energy Transfer Equity, which Armstrong pushed against. This is in addition to other disputes previously known to the public. *See* Michael Erman & Michael Flaherty, *Six Williams Cos Directors Quit After Failure to Oust CEO: Sources*, REUTERS (Jul. 1, 2016) https://www.reuters.com/article/idUSKCN0ZG35R/.

replace its directors.[201] It appears that outspoken resignations are not usually initiated by directors who aim to disclose information to investors and the public.

Firms, and directors, prefer to disclose resignations as those that do not arise from disagreement. The figures above highlight that companies utilize various tactics to minimize disclosures that may generate external controversy, including using ambiguous language in their filings. This is especially true due to the unclear guidelines of the SEC in describing what constitutes "disagreement" and which specific circumstances firms must disclose in their 8-K filings.[202]

Some may argue that our findings are not meaningful in that directors may have chosen to quietly resign simply because their resignations did not arise from disagreement. In other words, they may claim that the primary explanation for the lack of outspoken disclosures is that directors simply depart due to circumstances that do not relate to the firm.

First, there is an intuitive argument to be made against the notion that the absolute majority of directors resign without any relevant disagreements with the firm. Directorship is a highly desirable position that provides generous compensation, and turnover is not generally rewarded in the director labor market.[203] Furthermore, directors, with the exception of older "retirees," are not quick to relinquish their position because of strictly personal considerations, especially at earlier stages of their career.[204]

More importantly, the test cases below highlight that instances of omission from firms and directors are not uncommon.[205] As we will show, firms can and have circumvented SEC disclosure requirements, including corporations who repeatedly appear under the regulatory spotlight.[206] This holds true even in the age of increased SEC

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201 *See* Penn, supra note 192.

202 *See infra* Section IV.A.

203 Marshall, *supra* note 69; Cunningham & Suarez, *supr*a note 149 (discussing how directors are generously compensated on average, earning six-figure salaries that rise each year).

204 Dewally & Peck, *supra* note 47. They discuss how directors who are older have less incentive to preserve their reputation. Younger directors have more to lose from damaged reputations, which affects their decision-making when departing firms. Similarly, they found that resignations, specifically "conflict-related" ones, often result from circumstances like weak board performance and declining operating performance and sales.

205 *See infra* Section III.C.1.

206 The SEC largely focuses its attention on large public firms, increasing their duties to the regulator. S*ee, e.g.,* Barry W. Rashkover & Catherine B. Winter, *The impact of Sarbanes–Oxley on SEC Enforcement in Public Company Disclosure Cases — Part I*, 2 INT'L J. DISCL. GOV. 312 (2005) (discussing the expansion of the SEC's regulation of public firms); Rosenfeld, *supra* note 163, at 138 ("…the fact is that penalties for public companies are now the norm and a standard part of the resolution of most public company enforcement actions").

enforcement.[207] Our aforementioned statistical findings highlight that a majority of director departures are disclosed as "quiet," which is consistent with our earlier hypothesis. However, to strengthen our claim, we complement our findings with an in-depth analysis of relevant test cases that highlight the extent of the disclosure disparity in director resignations.

C. Test Cases

1. *Sample Cases*

Within our sample period, we discovered several cases in which a firm's disclosure of a director's resignation did not match the circumstances that were later reported. These are instances in which subsequent news reports highlight disagreement between the firm and the departing director over the company's operations, policies, and practices, yet their Form 8-K disclosures fail to reflect this conflict. Both case studies are particularly relevant in that they derive from top 10 firms of the S&P 500 companies.

First, we highlight the resignation of former director Peter Thiel from Meta. Thiel invested half a million dollars in the firm at its early stages, joining Meta's board of directors in 2005.[208] Thiel acted as a mentor to founder and CEO Mark Zuckerberg, providing robust leadership and financial insight.[209] In fact, Zuckerberg repeatedly praised Thiel's contributions to the firm throughout his tenure, citing his original, valuable insights.[210]

Meta reported Thiel's resignation in 2022, simply stating that Thiel "will not stand for re-election to the Company's Board of Directors."[211] Afterwards, Zuckerberg came out with a public statement praising Thiel, citing his "privilege to work with one of the great entrepreneurs of our

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207 The SEC has increasingly expanded the number of its enforcement actions and administrative proceedings, including steady increases in the past decade. For increases in the past few years, *see SEC Announces Enforcement Results for Fiscal Year 2023*, U.S. SEC. & EXC. COMM. (Nov. 14, 2023) https://www.sec.gov/news/press-release/2023-234; *Trends in SEC Enforcement Actions*, PWC (May 16, 2024) https://viewpoint.pwc.com/dt/us/en/pwc/in_depths/2024/assets/id202403.pdf.

208 Lauren Feiner & Ari Levy, *Peter Thiel to Step Down From Board of Facebook Parent Meta*, CNBC (Feb. 7 2022) https://www.cnbc.com/2022/02/07/peter-thiel-to-step-down-from-facebook-board.html.

209 Ben Gilbert and Kali Hays, *Peter Thiel is Resigning from Meta's Board to Focus on Electing Pro-Trump Candidates at the 2022 Midterms, Reports Say,* BUSINESS INSIDER (Feb. 8, 2022) https://www.businessinsider.com/peter-thiel-resigns-meta-board-of-directors-2022-2.

210 *Peter Thiel to Retire from Meta Board of Directors at 2022 Annual Shareholder Meeting*, META (Feb. 7, 2022) https://investor.fb.com/investor-news/press-release-details/2022/Peter-Thiel-to-Retire-from-Meta-Board-of-Directors-at-2022-Annual-Shareholder-Meeting/default.aspx; Kathleen Elkins, *Mark Zuckerberg Shares the Best Piece of Advice Peter Thiel Ever Gave Him*, CNBC (Aug. 28, 2016) https://www.cnbc.com/2016/08/25/mark-zuckerberg-shares-the-best-piece-of-advice-peter-thiel-ever-gave-him.html.

211 Peter Thiel Form 8-K Filing, *supra* note 11.

time."[212] However, later reports detailed specific disagreements between Thiel and the firm prior to his resignation. Thiel reportedly took issue with the firm's obsession with the Metaverse and its complacency regarding Meta's core social media business.[213] Meta invested billions into metaverse tech; however, the firm reportedly suffered from internal gaps in tech infrastructure.[214] In fact, Thiel supposedly raised these issues with Zuckerberg and the board meeting prior to his departure, yet to no avail.[215]

Thiel was also reported as a "lightning rod" at Meta due to his political views and influence in the company.[216] Thiel's relationship with the company reportedly diminished already from 2018 after disputes with a fellow director over his conversative political views, with Thiel and Zuckerberg's relationship being reported as tense in nature.[217] Furthermore, Thiel's controversial statements and investments often put Meta in the public spotlight, including financial support of firms that negatively affected Meta's business strategy.[218] However, Meta's disclosures make no mention of Thiel's ideological struggles with the firm and its leadership.

Second, we identified the departure of several corporate officers from Tesla. Within our sample period, Tesla disclosed zero instances of director resignation arising from disagreement. However, reports detail a string of departures from the company, including high-profile executives, that suggest that their resignations resulted from misgivings with the company's direction.[219]

One departure proved particularly significant. Dave Morton served as the firm's chief accounting officer, taking charge of the company's financial reporting and global accounting.[220] Morton previously served as vice president and chief financial officer of Seagate Technology, and was praised for his commitment towards shareholders.[221] Morton reportedly

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212 Salvador Rodriguez, *Peter Thiel to Step Down From Facebook Parent Meta's Board*, WSJ (Feb. 7, 2022) https://www.wsj.com/articles/peter-thiel-to-step-down-from-facebook-parent-metas-board-11644268545.

213 *See supra* note 12.

214 *Id.*

215 *Id.*

216 Rodriguez, *supra* note 212.

217 *Id. See also* Fossett, *supra* note 12.

218 Ryan Mac & Mike Isaac, *Peter Thiel to Exit Meta's Board to Support Trump-Aligned Candidates,* N.Y. TIMES (Feb. 7, 2022) https://www.nytimes.com/2022/02/07/technology/peter-thiel-facebook.html.

219 Dana Hull, *Tesla Loses Top Staff as Car Maker 'Stretched to the Limit'*, FINANCIAL REVIEW (Mar. 6, 2017) https://www.afr.com/companies/transport/tesla-loses-top-staff-as-car-maker-stretched-to-the-limit-20170306-gur9uw.

220 Matthew Heller, *Tesla CAO Morton Quits After a Month on Job*, CFO (Sep. 7, 2018) https://www.cfo.com/news/tesla-cao-morton-quits-after-a-month-on-job/658661/.

221 Davis S. Morton, CRUNCHBASE https://www.crunchbase.com/person/david-h-morton; *Seagate Technology Announces CFO Resignation* SEAGATE (Jul. 30, 2018) https://www.seagate.com/em/en/news/news-archive/seagate-technology-announces-cfo-resignation-pr/.

sought an opportunity to work with a visionary like CEO Elon Musk and affect relevant change within the firm.[222]

However, less than a month on the job, Morton abruptly resigned.[223] Morton cited no concerns with the firm's financial reporting or leadership, even during his exit interview.[224] Furthermore, the firm's disclosure reported no disagreement with Morton over the firm's policies or practices.[225] Despite this, later reports detailed Morton's feelings of neglect from company executives, including Musk, regarding financial obstacles related to taking the company private.[226] Days after joining the managerial staff, Musk brought the company into the public and regulatory spotlight after proposing on X, formerly Twitter, that he take the firm private.[227] Morton pushed to highlight his misgivings with the proposal, yet his concerns were not heeded.[228]

Again, we see an instance of resignation in which the disclosure does not match later reported circumstances. In the case of Tesla, this trend was not individual in nature. Despite relatively quiet 8-K disclosures, former senior executives later anonymously reported various reasons for their departure, including stressful work volume, mission creep, and a tense company culture.[229] However, for reasons such as those we analyzed in Part II, these executives preferred to remain silent, limiting their frustrations to anonymous, after-the-fact reports.

2. *Additional Examples*

The discrepancies we identified are not limited to the sample period. There are several notable cases prior to 2016 that shine light on the aforementioned disclosure disparity in director resignations. Although not in our sample, these earlier examples highlight the ever-growing gap between firm disclosures and actual resignations in practice.

The most notable case regarding the disclosure disparity occurred in 2006 with Hewlett-Packard. The firm became the target of SEC proceedings after providing a misleading disclosure relating to the abrupt resignation of one of its directors, which was adjacent to investigations of boardroom leaks within the firm.[230] The director, Thomas Perkins, voiced strong objections to the board's decision to ask another director to resign following the firm's investigation, and subsequently departed

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222 Sherman, *supra* note 14.
223 Dave Morton Form 8-K Filing, *supra* note 13.
224 Sherman, *supra* note 14.
225 Dave Morton Form 8-K Filing, *supra* note 13.
226 Sherman, *supra* note 14.
227 Jacob Sonenshine, *Musk Thrusts Tesla Holders Into Legal, Financial Limbo as SEC Probe Goes Formal*, THESTREET (Aug. 16, 2018) https://www.thestreet.com/markets/sec-subpoena-s-tesla-questions-about-take-private-loom-for-shareholders-14685907.
228 Sherman, *supra* note 14.
229 Hull, *supra* note 219.
230 SEC Releases, i.e. Administrative Proceeding, Exchange Act Release No. 3-12643 (May 23, 2007).

from the firm because of this decision.[231] However, the firm failed to disclose this disagreement in their 8-K filings, citing no disagreements between Perkins and the firm over its policies or practices.[232]

Several cases regarding oversight failure controversies also highlight resignations whose disclosures deviated from the actual circumstances in practice. Albeit not typical cases like Hewlett-Packard, in which the firm's disclosure failed to highlight disagreements with the departing director, they shine light on the disparity between firm disclosures and director resignations in practice.

In 2005, senior Walmart officials learned of an illegal bribery scheme at the firm's Mexican subsidiary, Wal-Mart de Mexico.[233] However, instead of expanding an internal investigation and disclosing these issues to authorities, Walmart officials prevented further inquiries and failed to take steps to resolve the internal misbehavior.[234] Former CEO and director Michael Duke resigned from his executive position years later following pressure, specifically due to an earlier email sent to him detailing the allegations.[235] However, Walmart's 8-K disclosure of Duke's resignation presents no insight into the circumstances culminating in his departure, summing it up to "retirement" from the position.[236] This, despite reports detailing pressure from shareholders to remove Duke from his executive and director position due to fears that executives were not held accountable for the scandal.[237]

Such was also the case with the Citigroup scandal, in which senior officials ignored possible warning signs of the forthcoming 2007 subprime mortgage crisis and expanded its subprime lending volume.[238] Following steep drops in share price and expected profits, CEO Charles Prince tendered his resignation from the company. Citigroup, in its Form 8-K disclosure, reported that Prince "resigned" from the position with no mention of circumstances leading up to his departure.[239]

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231 *Id.*
232 *Id.*
233 David Barstow, *Wal-Mart Hushed Up a Vast Mexican Bribery Case*, N.Y. TIMES (Apr. 21, 2012) https://www.nytimes.com/2012/04/22/business/at-wal-mart-in-mexico-a-bribe-inquiry-silenced.html.
234 *Id.*; Nandita Bose, *Walmart to Pay $282 million to Settle Seven-Year Global Corruption Probe*, REUTERS (Jun. 21, 2019) https://www.reuters.com/article/idUSKCN1TL27I/.
235 Barstow, *supra* note 233; *Walmart Administrative Officer Resigns,* YAHOO FINANCE (Feb. 28, 2013) https://finance.yahoo.com/news/2013-02-28-walmart-administrative-officer-resigns.html.
236 SEC Filings, i.e. Wal-Mart Stores, Inc., Current Report (Form 8-K) (Nov. 19, 2013).
237 Elizabeth A. Harris, *After Bribery Scandal, High-Level Departures at Walmart,* N.Y. TIMES (Jun. 5, 2014) https://www.nytimes.com/2014/06/05/business/after-walmart-bribery-scandals-a-pattern-of-quiet-departures.html. Duke's silent resignation is especially concerning considering that Duke was head of Walmart International at the time of the scandal. Yet, even after pressure to resign, Duke remained a member of the board, simply resigning quietly as chief executive officer.
238 Arthur E. Wilmarth Jr., *Citigroup: A Case Study in Managerial and Regulatory Failures*, 47 IND. L. REV. 69, 91 (2014).
239 SEC Filings, i.e. Citigroup, Inc., Current Report (Form 8-K) (Nov. 4, 2007).

However, later reports detail extensive shareholder criticism of Prince culminating around the date of the scandal, including conference calls illustrating investor frustrations with Prince's business strategies.[240] Investors and analysts repeatedly criticized Prince's leadership, specifically due to Citi's significant expenses and lower stock price, which intensified with the company's failed risk-taking adjacent to the mortgage crisis.[241] This was also the case with COO Robert Druskin and director George David, whose resignations contained no mention of the firm's strategical misgivings despite the timing coinciding with the company's financial turmoil.[242] Despite clear conflicts between investors and management over Citigroup's operations, disclosures of departure remained silent.

As shown above, firms at times minimize their disclosures by remaining silent as to disputes between departing officers and the company. Despite federal securities disclosure requirements, both firms and directors appear to avoid outspoken resignations so to circumvent negative market reactions and public scrutiny. Instead, departing directors prefer to limit their publicization of disagreements with the firm, often relegating themselves to *ex post* anonymous statements.

IV. POLICY IMPLICATIONS

In this part, we offer normative policy implications that arise from our empirical findings and theoretical analysis. First, we argue in favor of expanding the disclosure requirements for director resignations in the SEC's disclosure regulation. Second, we encourage increased regulatory enforcement of disclosure violations pertaining to director departures, both for firms and for departing directors themselves. Third, we urge for a clear legal framework determining breach of fiduciary duty upon resignation, which will minimize the uncertainty that arose from Delaware decisions *Puda Coal* and *Fuqi*. Finally, due to possible concerns that may be raised regarding bad-faith outspoken resignations, we highlight the ability of firms to utilize defamation suits.

A. Expanding Disclosure Requirements

As we explained above, director disclosure of conflicts upon resignation is an integral part of an effective corporate governance

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240 *With Billions Lost, Citi CEO Resigns,* DENVER POST (Nov. 4, 2007) https://www.denverpost.com/2007/11/04/with-billions-lost-citi-ceo-resigns/.

241 Wilmarth Jr., *supra* note 234, at 89.

242 SEC Filings, i.e. Citigroup, Inc., Current Report (Form 8-K) (Dec. 13, 2007); SEC Filings, i.e. Citigroup, Inc., Current Report (Form 8-K) (Feb. 28, 2008). *See also* Heidi Moore, *Druskin Exits Citigroup Amid $49bn SIV Rescue,* FINANCIAL NEWS (Dec. 14, 2007) https://www.fnlondon.com/articles/druskin-exits-citigroup-amid-siv-rescue-1-20071214. Adjacent to Citigroup's turmoil, the firm saw a string of directors resign from the firm. *See* In re Citigroup Inc. Shareholder Derivative Litigation, 788 F. Supp. 2d 211, 214 (S.D.N.Y. 2011) ("And five who were directors in November 2007—George David, Kenneth T. Derr, Roberto Hernandez Ramirez, Robert E. Rubin and Franklin A. Thomas—had left the board by September 2009").

structure.[243] Transparency between the executive management of the firm and its investors reduces the information asymmetry between the parties, allowing for investors to timely react to relevant controversies within the firm.[244] Vertically, providing investors with the requisite information mitigates agency costs and allows investors to ensure that directors implement effective internal controls.[245] Horizontally, departing directors alert their peers to misgivings that may not have been previously clear to them.[246] This allows the remaining directors to foster change within the firm, whether through changes in management or in business strategy.

However, current disclosure requirements are not effective in guiding firms (and directors themselves) as to the transparency that should be required of them. SEC regulations require that firms "briefly describe the circumstances" that surround the director's resignation; however, the SEC provides no clear explanation regarding what circumstances must be disclosed.[247] The guidelines do not list specific details relating to the departure that must be reported in the Form 8-K filing, allowing firms to easily circumvent disclosure requirements.

1. *Specification in Disclosure Guidelines*

General, amorphic disclosure requirements can hamper the transfer of material information to shareholders through securities filings. Broad guidelines allow firms to subjectively interpret federal disclosure regulation, which creates ambiguities in the required scope of disclosure and allows firms to generate filings to their favor.[248] With respect to director resignation, firms are granted leeway in deciding which details they may wish to disclose, specifically due to the generality of Item 5.02 guidelines.

To mitigate this ambiguity, the SEC ought to list certain circumstances that firms must disclose upon resignation of a director. Item 5.02 guidelines should require that firms disclose specific details relating to the director's resignation – such as the reason for departure, the extent of the firm's prior knowledge of said reasoning, the departing compensation package the director will receive, among other relevant details. Furthermore, the SEC can require that firms include explicit statements regarding whether or not the director's resignation stemmed from disagreement. To guide firms, the SEC can list specific types of disagreements that must be reported – including disagreements over

243 *See supra* Section I.B.

244 Brealey & Myers, *supra* note 48, at 14.

245 See *supra* note 4.

246 For further discussion regarding horizontal monitoring, *see* Eckstein & Parchomovsky, *supra* note 33.

247 SEC Form 8-K Guidelines, *supra* note 35.

248 *See, e.g.,* Sebastian Steuer & Tobias H. Troger, *The Role of Disclosure in Green Finance*, 8 J. FIN. REG. 1, 33 (2022) (discussing the impact of broad disclosure requirements on reports involving 'green' information).

executive compensation, fraudulent misconduct, director appointments, and the like.

We should note that we do not recommend a closed list of necessary circumstances. This is because it would allow for firms to circumvent disclosure requirements in cases where there may be relevant details for shareholders that are not listed in the Item 5.02 guidelines. Nevertheless, there ought to be an introductory list of specific circumstances that must be disclosed to ensure that firms know which details they must report and to what extent.[249] Specifying disclosure requirements can assist in guiding firms and simultaneously generate standards for firms that must be met in their filings.

2. *Transfer of Burden to Corporate Directors*

Currently, federal securities regulation requires that executive officers, namely the CEO and CFO, personally sign off on the firm's financial reports.[250] This includes Form 8-K reports, which must be signed prior to their filing.[251] Despite this requirement for executive officers, directors are not required to attest to the validity of the firm's Form 8-K filings. This, including cases of director resignation, where directors may voluntarily file a response letter if they choose.[252]

To ensure that directors have "skin in the game," the SEC should transfer the burden onto departing officers upon resignation. When the firm provides its Form 8-K disclosure relating to an officer's departure, regulators ought to require that the resigning officer personally sign off on the disclosure itself. In doing so, departing directors and senior executives personally attest to the validity of the firm's disclosure, similar to the requirements placed on executive officers.[253]

We suggest requiring that firms present their disclosure to the departing officer, after which the officer must sign off on the report if they agree with the disclosure's language. However, if the departing officer does not agree with the contents of the disclosure, they can provide a timely counter disclosure to the SEC revealing their disagreements with the firm's initial report. The firm is then subject to possible regulatory penalties upon investigation. If the firm's disclosure omits material circumstances and the departing officer fails to provide a relevant counter disclosure, then both parties can be subject to strict regulatory penalties. Similarly, the signing director would face possible liability for breach of fiduciary duty for failing to alert shareholders and regulators as to material omissions in the disclosure.

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[249] One added benefit of simplifying disclosures through specification is that it assists in mitigating overloading problems that often occur in mandatory securities disclosure. Ben-Shahar often discusses the issues that arise from these mandatory disclosures, including overloading and overaccumulation. *See, e.g.,* Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. PA. L. REV. 647, 686 (2011).

[250] Section 302 in Sarbanes-Oxley Act (codified at 15 U.S.C. § 7241).

[251] SEC Form 8-K Guidelines, *supra* note 35.

[252] *Id.*

[253] 15 U.S.C. § 7241.

Here, the concern is that directors may fail to adequately respond to disclosures of resignation that do not match the actual circumstances behind their departure. This is especially troubling since firms, and not the departing officers, are those who face consequences for material omissions in their disclosures.[254] In requiring that resigning directors attest to the validity of the disclosure, regulators ensure that these officers can be personally held accountable for material inconsistencies. As a result, departing directors will be encouraged to contest Item 5.02 disclosures that fail to present the actual circumstances relating to their resignation. Consequently, if departing directors are not willing to sign off on the firm's disclosure, then regulators can quickly understand the necessity for investigation of material omissions by the firm.

Some may argue that requiring directors to personally attest to the validity of the firm's disclosure will disincentivize officers from retroactively conveying their disagreement with the company. Directors who disagree with the firm's initial filing, and have not already provided a counter disclosure, will not exposes themselves to personal liability after the fact, limiting their desire to retroactively disclose disagreements with the firm.

To minimize this possible effect, the SEC can encourage retroactive disclosures through incentive programs that ease on the resigning director. For example, regulators can provide material rewards for officers who previously departed from firms without providing necessary counter disclosures and wish to remedy said omissions. This, similar to the incentives provided by the SEC for corporate whistleblowers under the Dodd-Frank Act.[255] Regulators can also consider minimizing penalties for the director that retroactively discloses their disagreement with the firm's Item 5.02 disclosure. In doing so, directors are incentivized to come forward and avoid harsher regulatory penalties that may come with material omission of circumstances relating to their departure.[256]

3. *Directors and Corporate Officers – Why Differentiate?*

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[254] Section 13(a) of the Securities Exchange Act, rule 31a-11 (codified at 15 U.S.C §78c).

[255] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 § 922, 124 Stat. 1376, 1899-1900 (2010) (codified at 15 U.S.C. § 78a et seq.) (whistleblower protection).

[256] Positive incentive programs relating to director resignation can be effective in encouraging both directors and firms to improve governance practices. For example, Hamdani and Kraakman discuss a positive incentive system relating to director resignation that they coin "the resignation rule." Here, directors can become eligible for rewards by filing a letter with the board: (1) announcing their resignation, (2) highlighting suspicions regarding internal misconduct within the firm, (3) identifying circumstances that arose their suspicions, and (4) describing their efforts to act or investigate the issue. Hamdani and Kraakman explain that this rule can align with a regulatory system and is not exclusive to the boardroom. *See* Hamdani & Kraakman, *supra* note 155, at 1703.

The current requirements for resignation of directors with cause are more stringent than those for that of other corporate officers. When high-level executive officers, including the CEO, CFO, and COO, resign, the company is solely required to disclose the occurrence and date of the event.[257] Firms are not required to disclose the officer's motivation for resigning regardless of the circumstances that resulted in the officer's resignation. However, when directors resign with cause, the company's disclosure requirements are increased.

To further mitigate the lack of outspoken resignations, the SEC ought to complement changes to director resignation disclosures with identical changes to their senior officer counterparts. Form 8-K guidelines do not require any explanation of circumstances of conflict as it relates to the departure of senior officers, despite the similar effect of their outspoken disclosures on the firm.[258] Expanding disclosure requirements to include other senior officers would serve to reduce the trend that arose within our findings and assist in mitigating the information asymmetry between shareholders and corporate officers as a whole. This is especially relevant because senior officers play increasingly important roles in corporate governance structures, and their unique positions allow them to convey material information that even directors are not privy to.[259]

The benefit of expanding disclosure requirements is that regulators will have more tools at their disposal to limit false or misleading Item 5.02 filings. The SEC will have more readily available knowledge pertaining to the firm's disclosure, and they can properly ensure that firms and departing officers comply with the Form 8-K guidelines. If not, then both firms and departing officers can be held accountable for the relevant omission.

B. SEC Enforcement of Disclosure Violations

High-quality financial reporting is essential to the securities market.[260] When securities disclosure requirements are credible and efficient, information is transparently passed to investors, allowing them to make informed decisions pertaining to their current and possible investments.[261] To facilitate this disclosure, there must be an effective regulator that ensures that firms adhere to the reporting requirements.

The SEC has received praise for its enforcement of securities law.[262] However, it has also received its fair share of criticism regarding its

[257] SEC Form 8-K Guidelines, *supra* note 35.
[258] *Id.*
[259] For a nuanced explanation of the role of the CEO in firm governance, for example, *see* Barzuza, Curtis, & Webber, *supra* note 47.
[260] Michael Sutton, *Financial Reporting in U.S. Capital Markets: International Dimensions*, 11 ACC. HORIZONS 96, 97 (1997).
[261] *Id.*
[262] *See, e.g.,* Jonathan N. Eisenberg, *13 Observations about the SEC's Enforcement Program*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 18, 2016) https://corpgov.law.harvard.edu/2016/04/18/13-observations-about-the-secs-

enforcement programs. Specifically, the SEC has been criticized for (1) its lack of aggressive enforcement of securities law, (2) its "slap-on-the-wrist" sanctions, and (3) its failure to require admissions of guilt, among others.[263] Since its conception in 1934, the SEC has been subject to various critiques of its enforcement policies, at times arguing that the regulatory body fails to implement securities regulations, and at other times claiming that it over-enforces against good-faith market participants.

1. *Lackluster Enforcement of Item 5.02 Requirements*

The SEC's enforcement policy regarding disclosure of director resignations is no exception. Throughout the past two decades, the SEC has done little to enforce its Form 8-K requirements and impede firms from omitting circumstances of conflict in their disclosures. There are few cases in which the SEC brought enforcement proceedings against firms for material omission in Item 5.02 filings. Despite the increasing number of enforcement actions against firms every year, little attention is given to disclosure of conflicts between firms and departing directors.

Furthermore, in the few cases we were able to identify, Item 5.02 violations were part of a broader failure to disclose, and the subsequent sanctions were minimal in nature. For example, in the case of Hewlett-Packard, who failed to disclose the disagreement between the firm and a resigning director, the consequence was simply a cease-and-desist order to refrain from further violations.[264] Despite clear violations of the Securities Exchange Act, the firm faced no punitive penalties for its omission of circumstances of conflict from its 8-K disclosure.

Similarly, in the case of Universal Bioenergy, Item 5.02 disclosure violations were a small part of a broader failure by the firm to file necessary disclosures.[265] The firm reportedly failed to disclose five Forms 10-K (annual) and thirteen Forms 10-Q (quarterly), as well as several other periodic disclosures that were reported delinquently.[266] Within the multiple disclosure failures, the firm also failed to file a Form 8-K regarding the former CEO's resignation. Although the firm faced serious regulatory penalties, including revocation of securities registration, these sanctions resulted from broad disclosure failures and not specifically from its inadequate disclosure of an executive resignation.[267]

We can see that the SEC very rarely enforces individual Item 5.02 disclosure violations in a sufficient manner. Firms are not deterred from

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enforcement-program/ (highlighting the principle accomplishments of the SEC enforcement program).

[263] Jonathan N. Eisenberg, *Recent Criticism of the SEC: Fair or Unfair?*, HARV. L. SCH. F. ON CORP. GOVERNANCE (May 25, 2016) *https://corpgov.law.harvard.edu/2016/05/25/recent-criticism-of-the-sec-fair-or-unfair/*.

[264] SEC Administrative Proceeding No. 3-12643, *supra* note 230.

[265] SEC Releases, i.e. Administrative Proceeding, Exchange Act Release No. 3-18461 (Apr. 23, 2019).

[266] *Id.*

[267] *Id.*

"softening" their disclosures of director resignation because there is no incentive to disclose circumstances of conflict. Such disclosures could negatively affect the firm's stock price and reputation,[268] and there is no record of harsh regulatory sanctions for omitting details from these disclosures.

2. *Towards Increased Sanctions and Field Examinations*

To ensure that firms comply with federal disclosure regulations, the SEC should take steps to increase its enforcement of Item 5.02 violations. One aspect of the SEC's enforcement program is its Division of Examinations, which aims to protect investors by conducting on-site exams among market participants.[269] This division performs examinations of investment advisors, including directors and corporate officers, to ensure that disclosures made to investors include necessary material facts.[270]

One possible remedy to the lack of outspoken disclosures is to expand the Division of Examinations to include periodic examinations of firms and their disclosures of director resignations. The SEC can perform arbitrary exit interviews with departing directors and their peers to investigate their motivations for resigning from the firm. Afterwards, they can cross-reference their findings with the firm's disclosure. Field work by regulators can be particularly effective in understanding the dynamics between market participants, and such examinations may assist in identifying lackluster disclosures of director resignations.[271]

Furthermore, the SEC can expand the sanctions imposed on firms who fail to disclose relevant circumstances of conflict in their Item 5.02 filings. Disclosure failures should be met with sufficient punitive penalties that deter firms from taking advantage of what they perceive to be "minimal" violations. This is especially feasible as the SEC need not prove scienter to establish violations of the Securities Exchange Act in the case of Form 8-K material omissions.[272] If the disclosure of a departing director or their peers differs from the firm's initial disclosure, then regulators can quickly investigate and impose relevant sanctions to deter future violations.

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[268] *See* Fahlenbrach, *supra* note 44.

[269] U.S. SEC, ABOUT THE DIVISION OF EXAMINATIONS https://www.sec.gov/exams/about.

[270] 2024 EXAMINATION PRIORITIES, U.S. SECURITIES AND EXCHANGE COMMISSION (2024).

[271] See, *e.g.*, Barry W. Rashkover & Laurin Blumenthal Kleiman, *SEC Enforcement and Examinations Concerning Hedge Funds*, 52 N.Y.L SCH. L. REV. 599 (2008) (describing the efficacy of the Securities and Exchange Commission's field examinations in their enforcement actions regarding hedge funds).

[272] Securities & Exchange Commission v. Savoy Industries, Inc., 587 F.2d 1149, 1167 (D.C. Cir. 1978) ("A similar analysis of Section 13(d)(1) leads us to conclude that the SEC need not prove scienter to establish a violation"). Scienter is defined as a mental state characterized by the intent to deceive, manipulate, or defraud.

Finally, we should note that enforcement is necessary to counteract the market challenges that inhibit directors from resigning in protest. Expanding disclosure requirements for firms and requiring that directors attest to the validity of the disclosure does not necessarily mitigate the director's fear of diminished market reputation. The result is that directors may remain deterred from resigning in protest due to concerns of future employment. Here, enforcement serves an important role: across-the-board enforcement of disclosure violations encourages widespread adherence to its policies, both from firms and from directors. Regulatory fines for personal directors can amount to significantly higher sums than the reputational costs of blacklisting in the labor market, and frequent enforcement of these penalties can serve to mitigate the reputation vector.[273]

C. Legal Framework for Resignations and Fiduciary Duties

Outspoken director resignations, as explained above, are inhibited by fears of liability for breach of fiduciary duty.[274] Directors who resign, especially in protest, can be held personally liable for breach, despite good faith attempts to alert shareholders. The result is that directors are prevented from realizing their right to resign, especially as a response to internal misbehavior that negatively affects the firm.

This is exacerbated by the legal uncertainty that arises from recent case law regarding director resignation. The decisions in Delaware decisions *Puda Coal* and *Fuqi* highlight that director resignation can result in personal liability but provide no clear framework for determining which cases of resignation constitute breach of duties of care and loyalty.[275] For example, the judges in both cases failed to distinguish between good-faith resignations in protest and bad-faith abdications of the director's position. The judges were not compelled to differentiate between different methods and motivations for resignation, likely due to the particular circumstances that shrouded both decisions.[276]

Furthermore, there is no legal framework governing the circumstances that may result in personal liability for breach of duty upon resignation. Although the law generally permits resignation regardless of motive, circumstance, or manner, these recent decisions impede the

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273 The SEC has wide discretion regarding its ability to fine individuals, and recent cases have shown that these fines can amass to large sums. *See, e.g.,* SEC v. Elon Musk Case No. 18-cv-8865 (S.D.N.Y.) (illustrating the $20 million fine that the SEC placed on Elon Musk for a series of false and misleading statements made in 2018); "SEC Obtains Record $92.8 Million Penalty Against Raj Rajaratnam," U.S. SECURITIES AND EXCHANGE COMMISSION (Nov. 8, 2011) https://www.sec.gov/news/press/2011/2011-233.htm.

274 *See supra* Section II.A.1.

275 Fuqi, *supra* note 1; Puda Coal, *supra* note 6.

276 For example, both cases revolved around firms with foreign operations, which heightens the director's fiduciary duty. Furthermore, both decisions came about in early stages of the proceeding, where the judges did not need to answer finally as to their liability.

ability of directors to freely resign.[277] Delaware law, for example, makes no mention of breach of fiduciary duty for director resignation, nor does it clarify what circumstances justify resignation, specifically in protest. The result is that directors are left in limbo, hesitant to resign in protest for fear of possible derivative suits by shareholders.

Policymakers ought to consider creating a clear legislative framework that provides specific tests to determine whether a director's resignation constitutes a breach of fiduciary duty. For example, the law should differentiate between resignations tendered in good faith, aiming to alert shareholders and regulators, and departures that are motivated by personal interests. Similarly, policymakers should provide specific legal protections for directors who resign in protest to internal misbehavior within the firm. As a result, directors would be able to properly consider the implications of their resignation and feel comfortable in doing so if the purpose is to protest misconduct within the firm.

A concise legal framework serves two main purposes: first, it works to guarantee that material information can be effectively relayed to investors through resignation. Second, it protects directors who do not wish to align themselves with the firm's misconduct. Directors who remain with the firm can face serious repercussions, including liability for breach of duty and harm to their professional reputation.[278] As a result, clear legal guidelines for departing directors can serve shareholder interests and simultaneously protect corporate officers who wish to resign from the firm.

D. Defamation Suits Against Bad-Faith Resignation

One concern that should be noted is the possible negative effects of outspoken resignations in bad faith. Although we argue that outspoken resignations are effective corporate governance tools, we are also aware of the consequences of encouraging resigning employees to speak out against their former employers. Specifically, outspoken resignations can be manipulated by disgruntled former employees who wish to cause reputational harm to the firm.[279] Some may argue that increasing the number of outspoken officer resignations could potentially increase the frequency of bad-faith resignations, which we do not purport to encourage.

To protect the firm's reputation against bad-faith resignations, we highlight the ability of corporations to file defamation suits against former employees who falsely criticize the firm's operations, policies, or

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[277] *See supra* Section II.A.1.

[278] For an explanation of the risks directors face regarding breach of duty, *see supra* note 54. For an explanation regarding the effect on the director's reputation, *see supra* Section II.A.2.

[279] *See*, *e.g.,* Dewally & Peck, *supra* note 47, at 39 ("Alternatively, [resignations] accompanied by public criticism might be benign events… they may be the actions of a lone disgruntled director or indicative of a personality clash between the director and the CEO or other members of the board").

practices.[280] Corporations, as separate legal personalities, are granted the right to sue for defamation if the departing director publicizes false claims about the firm that negatively impact its reputation and business.[281] This tool can serve effective in deterring disgruntled officers from taking advantage of the ability to resign in protest to unjustly cause reputational or financial harm to their former employers.

Nonetheless, it should be highlighted that this legal tool must be cautiously balanced. Although defamation suits can be particularly effective in deterring bad-faith outspoken resignations, they can also deter good-faith resignations if not regulated. The benefit of defamation law is that suits are notoriously difficult, and truth can be an absolute defense against claims of defamation by the firm.[282] Likewise, the burden of proof remains on the firm to show that the statements are false, not vice versa.[283]

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[280] Courts have generally established the rights of corporations to bring defamation suits. *See* Pullman Standard Car Mfg. Co. v. Local Union No. 2928 of USW, 152 F. 2d 493 (7th Cir. 1945); Brayton v. Crowell-Collier, 205 F. 2d 644 (2d Cir. 1953); Willfred Coal Co. v. Sapp, 193 Ill. App. 400 (1915) (highlighting actionable defamation suits regarding false claims that a corporations violated the law); Louis J. Bloomfield, *Defamation of Corporations*, 13 CLEV. ST. L. REV. 95, 97 (1964) ("The general rule has also been established that a corporation may be defamed by false statements as to its efficiency or other business character").

[281] Corporations are separate legal entities, and as such are afforded applicable rights of their own. *See, e.g.,* Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 636 (1819) (defining the corporation as "an artificial being, invisible, intangible, and existing only in contemplation of law"); Robert W. Hamilton, *The Corporate Entity*, 49 TEX. L. REV. 979, 980 (1971) ("The notion that a corporation is a fictional person or legal entity distinct from its shareholders also appears in early American decisions"); Susan Watson, *How the Company Became an Entity: A New Understanding of Corporate Law*, 120 J. BUS. L. 1 (2015) (discussing the development of the idea of a corporation as a separate legal entity, specifically after *Salomon*); Salomon v Salomon & Co Ltd [1897] AC 22. Corporations have long asserted right-claims, including constitutional rights like freedom of speech and due process. *See, e.g.,* Citizens United v. Federal Election Commission*,* 558 U.S. 310 (2010) (prohibiting restrictions on corporate political speech); Minneapolis & St. Louis Ry. Co. v. Beckwith*,* 129 U.S. 26, 28 (1889) (recognizing corporate property rights and the ability to challenge infringement of these rights); Brandon L. Garrett, *The Constitutional Standing of Corporations*, 163 U. PA. L. REV. 95, 97 (2014) ("Corporations and other types of organizations have long exercised a range of constitutional rights, including those found under the Contracts Clause, Due Process Clause, Fourteenth Amendment Equal Protection Clause, First Amendment, Fourth Amendment, Fifth Amendment Takings and Double Jeopardy Clauses, Sixth Amendment, and Seventh Amendment").

[282] RESTATEMENT (SECOND) OF TORTS § 581A (1977); Melinda J. Branscomb, *Liability and Damages in Libel and Slander Law*, 47 TENN. L. REV. 814 (1980) ("Truth is an absolute defense to this cause of action"); Garrison v. Louisiana, 379 U.S. 64 (1964).

[283] *See, e.g.*, Philadelphia Newspapers v. Hepps, 475 U.S. 767 (1986); Marc A. Franklin & Daniel J. Bussel, *The Plaintiff's Burden in Defamation: Awareness and Falsity*, 25 WM. & MARY L. REV. 825, 851 (1984) ("In addition to establishing that the defendant was aware of his statement's defamatory meaning, the plaintiff also must show that the defamatory statement is false").

Finally, we highlight a possible tool utilized in particular situations of defamation to protect good-faith parties: the qualified privilege defense. Qualified privilege protects parties in certain situations who make potentially defamatory statements towards their counterpart with no intent of malice. For example, qualified privilege is often utilized to protect former employers who provide negative references of their former employees in the labor market.[284] In the case of director resignation, the qualified privilege defense could serve useful in protecting good faith directors who wish to alert the public as to misgivings within the firm. It can assist in balancing the interests of firms against false outspokenness while simultaneously encouraging good-faith actors to utilize their ability to resign in protest.

Legislators ought to consider expanding tort and corporate law provisions to provide qualified privilege defenses to resigning directors who publicize their disagreements in good faith. Firms can show that departing officers publicized false, bad-faith statements and defend their reputations, but good-faith directors are not hampered by malicious suits from the firm. This serves to protect the departing officer's personal interests while also protecting the firm's right to its good name and the shareholder's right to be informed.

CONCLUSION

Directors are essential figures in corporate governance. They serve as watchdogs on behalf of shareholders and advise senior executives on the firm's business strategy. Due to the agency relationship between shareholders and management, information asymmetries arise and inhibit the ability of shareholders to understand the condition of the firm. Shareholders, typically passive equity holders, cannot properly exercise oversight of management, and thus enlist directors to bridge between the parties. As a result, the function of the board, specifically as a monitor, is essential to ensure that shareholders receive material information regarding the firm's condition.

One rare opportunity to convey such information to shareholders is through outspoken resignations. Here, directors publicly disclose misgivings regarding the firm, allowing shareholders and the public to promptly react and remedy the relevant issues. To ensure this market reaction, disclosures of director resignations must properly convey the disagreements between the departing director and the firm.

However, as we show in our empirical analysis, this condition is not met. The absolute majority of director resignations are "silent," minimizing the ability of shareholders to respond to potential misconduct within the firm. Directors may be limited in their desire or ability to resign in protest for several reasons, including fear of liability

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[284] RESTATEMENT (SECOND) OF TORTS § 595 (1977); Pamela G. Posey, *Employer Defamation: The Role of Qualified Privilege*, 30 WM. & MARY L. REV. 469, 471 (1989) ("Employers enjoy a qualified privilege when discussing most matters related to employment with individuals having a corresponding interest or duty").

for breach of fiduciary duties, personal reputational concerns, structural biases, and negative financial incentives. Similarly, firms may prefer to minimize the frequency of "outspoken" disclosures due to various financial, reputational, and legal incentives.

To mitigate this issue, we offer several potential solutions that may increase the frequency of good-faith outspoken resignations. These include expanding firm disclosure requirements, increasing SEC enforcement of individual disclosure violations, and creating a concrete legal framework governing the relationship between director resignation and fiduciary duties. To protect firms against bad-faith resignations, we emphasize the ability of firms to file defamation suits, with certain possible restrictions that may balance the interests of shareholders and directors. With these steps and further research into director departure, policymakers will be able to more effectively consider the balance between the interests of shareholders, directors, and management alike.