An SEC Enforcement Action Could Change the Game for “Without Cause” Firings

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Public boards may find it more difficult to afford favorable treatment to terminated executives following the SEC’s action against McDonald’s.

Boards commonly agree to treat the departure of an executive as “without cause” even when “cause” for termination arguably (or even certainly) exists, thereby allowing the executive to receive severance payments and retain equity compensation and other benefits.

These decisions generally reflect a desire to avoid a messy and costly public “food fight” and are often justified by the uncertain ability to sustain a “for cause” termination and the benefits of securing a release from the departing executive. These pragmatic decisions have traditionally been viewed as a permissible exercise of the board’s business judgment.

In most cases, public disclosures about these executive departures have

The SEC’s Jan. 9, 2023, enforcement action against McDonald’s Corporation may impact this common practice. In that proceeding, the SEC determined that McDonald’s violated the securities laws by failing to disclose the board’s use of discretion in treating its CEO’s termination as “without cause” after learning that he had violated the company’s standards of business conduct. McDonald’s was able to avoid paying a fine based upon the

Commission’s determination that the company had fully cooperated with the agency’s investigation.

The SEC did, however, levy a $400,000 fine against the departed CEO and entered a five-year bar against his service as a public company officer or director. This action was based on his failure to disclose to the company that he had engaged in multiple violations of McDonald’s standards of business conduct before the board made its termination decision. The agency reasoned that the CEO failed to disclose his repeated misconduct with knowledge that his omission would lead to misleading public statements by the company about the circumstances for his departure.

As has become commonplace in recent years, the two Republican appointees to the Commission dissented from these actions, finding that that the Commission’s majority had created a “hiring and firing discussion and analysis” regime that constituted unwarranted regulatory expansion in the guise of enforcement activity.

In the wake of this SEC enforcement action, a public company managing the departure of a senior executive should carefully consider the content of its public disclosures about the departure and whether it is necessary to include an express statement that the board exercised discretion in treating the termination to be without cause and an enumeration of the factors it considered in reaching that decision. Of course, it will be important for the content of any such public disclosure to be consistent with the rationale for the board’s decision, as stated in the minutes of its proceedings.

The need to disclose that a board exercised discretion in reaching a “no cause” termination may, in some cases, alter the board’s decision-making calculus. Depending upon the nature of the underlying reasons for termination, and particularly when “cause” was almost certainly present or the conduct especially egregious, the required disclosure may be inconsistent with the goal of avoiding a public airing of unsavory conduct. Moreover, the board’s decision to allow an executive to retain equity grants and receive substantial settlement payments may risk trading litigation with the departing executive for even more disruptive litigation with shareholders who object to affording what would admittedly be “discretionary” financial benefits to an executive who engaged in misconduct.

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