The assumption underlying the literature is that shareholders desire to maintain their directors (and indirectly their managers) but need to monitor them to guarantee that their agents' interests align with their own. Moreover, the literature analyzes how capital, labor, and product markets help detect situations in which shareholders need to replace their agents. Thus, the market for corporate control, for example, assists shareholders by identifying takeover opportunities when management under-performs. When management under-performs, the shares' prices decline and the corporation may become a target for a hostile takeover. The new owner identifies a business opportunity to increase corporate performance by replacing the board and its management.[164]

When shareholders want to end the agency relationship, however, no technique can minimize agency costs and align the interests of directors (and indirectly the managers) with that of shareholders as well as removal can.[165] Similarly, while the markets help detect under-performing agents, this should supplement rather than replace shareholders' ability to terminate the agency relationship altogether.[166] We should not force corporations to change ownership to achieve a change of directorial and managerial personnel. In other words, shareholders of publicly-held corporations generally suffer from collective action, rational apathy and free ride problems that prevent them from closely monitoring the actions of their agents. When these difficulties are overcome and shareholders conclude they want to remove their board, they should be able to do so.[167] Shareholder removal power is required under a law and economics approach that seeks to align directors' interests with those of the shareholders. Staggering the board and protecting directors from removal for long periods of time runs contrary to law and economics' most basic principles.

My proposed solution, developed in the last Part, in favor of distinguishing shareholder removal power from the damages that may be accorded directors in unjustified removals, is fully supported under a law

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ownership and control can be an efficient form of organization).

[164]*See* Bainbridge, *supra* note 4, at 796; Easterbrook & Fischel, *supra* note 49, at 698 ("Substitution of one set of managers for another, for example, often produces gains because assets increase in value under better management, and would-be managers offer payments to shareholders to compete for the right to manage the firm's pool of assets").

[165]For support, see Strine, *supra* note 2.

[166]"Shareholders and society generally will benefit from a mechanism that replaces the firm's incumbent managers well before the firm succumbs to competitive forces." Gordon, *supra* note 159, at 124.

[167]*See* discussion *supra* Part III.A.3.

and economics theory of efficient breach.[168] It rests on the premise that it may be cheaper, under certain circumstances, for the corporation to dismiss the director and pay the full fees due to the director for the balance of his term.

E. *Comparative Law*

In this section, I will demonstrate that other countries generally distinguish shareholder removal power from the remedies that may result in unjustified removals. Even where the country's statute requires cause for removal, it usually pertains only to damages, not entrenchment in office. Moreover, many countries treat shareholders' power to remove directors as a mandatory rule that cannot be waived. This may indicate that such countries believe the markets have failed to adopt an efficient solution on their own.[169]

It is especially insightful to compare American and British corporate laws since the underlying capital and corporate structures in the U.S. and U.K. are similar. Both enjoy well-developed capital markets, and their typical public corporation is held by dispersed shareholders.[170] Under

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[168]For a definition of efficient breach, see ROBERT COOTER & THOMAS ULEN, LAW AND ECONOMICS 290 (1st ed. 2000) ("[A] breach of contract is more efficient than performance of the contract when the costs of performance exceed the benefits to all the parties.") (emphasis omitted). *See also* Charles J. Goetz & Robert E. Scott, *Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach*, 77 COLUM. L. REV. 554, 558 (1977) ("[An efficient breach] induces a result superior to performance, since one party receives the same benefits as performance while the other is able to do even better.").

[169]For a suggestion that market failure may justify mandatory rules dealing with "positional conflicts" (including entrenchment) between shareholders and directors in publicly-held corporations, regardless of whether the entrenchment devise was adopted mid-stream or at the initial public offering stage, see, for example, Eisenberg, *supra* note 92, at 1473.

In fact, despite the prevalence of the contractarian theory of corporate law, a study of the RMBCA revealed that many—if not most—of its provisions are mandatory. *See* John A. MacKerron, *A Taxonomy of the Revised Model Business Corporation Act*, 61 UMKC L. REV. 663, 689 (1993). *Cf.* Lucian A. Bebchuk, The Myth of the Shareholder Franchise (Oct. 2005), *available at* http://ssrn.com/abstract=829804. In this recent work, Bebchuk has suggested enhancing shareholder removal power, too. *Id.* at 22-27. He suggests that empirically shareholders rarely contest incumbent candidates because of existing legal rules. *Id.* at 13-22. Contesters bear all the extremely heavy expenses associated with such a proxy contest but share the benefits (if they win) with other shareholders. *Id.* at 15. He suggests granting shareholders a potent ability to replace all directors every two to three years by granting them reimbursement if contesters win support of a third of the shareholder vote. *Id.* at 23-26. He offers this new regime as the default rule. *Id.*

[170]*See* Zohar Goshen, *The Efficiency of Controlling Corporate Self-Dealing: Theory Meets Reality*, 91 CAL. L. REV. 393, 429-32 (2003) (discussing the compatibility of the two legal systems for comparison purposes); Rafael La Porta et al., *Corporate Ownership Around the*

British law, as under U.S. corporate law, directors oversee the corporation's business.[171] Nonetheless, shareholders of British corporations can always remove their directors, even if the board is staggered or appointed for a fixed term.[172] Thus, staggered boards do not play an important role in British corporations.

Moreover, British law protects shareholders' removal power more than it does their appointment power. While shareholder removal power is protected by law and cannot be waived, the law "requires neither that directors be elected by the shareholders in general meeting nor that they submit themselves periodically to re-election by the shareholders."[173] Since the law provides shareholders with broad removal powers, it assumes there is no real danger of shareholders' exclusion from the appointment process.[174]

Directors may be entitled to damages for removal without cause, however. They are also entitled to notice and a hearing before removal by the general meeting.[175] Since section 368 of the Companies Act empowers holders of ten percent of the voting shares to request an extraordinary meeting of the company, "[i]n the U.K. . . . control of the majority of the votes feeds through directly into control of the board."[176]

However, two qualifications on shareholder removal power can prove especially potent: (1) damages can be formidable in the case of executive directors who are removed, and this might deter shareholders from removing the director altogether; and (2) the company may grant a

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World, 54 J. FIN. 471, 491-98 (1999) ("[Ninety] percent of the large U.K. firms [and] 80 percent of the large U.S. firms . . . remain widely held.").

[171] Table A of the Companies Act 1985 provides in article 70 that "[s]ubject to the provisions of the Act, the memorandum and the articles and to any directions given by special resolution, the business of the company shall be managed by the directors who may exercise all the powers of the company." *See* Companies Act 1985, app. 2, tab. A, *available at* http://www.formationsdirect.com/includes/tablea.pdf.

[172] Under section 303(1) of the Companies Act, shareholders have a statutory right to remove directors. "A company may by ordinary resolution remove a director before the expiration of his period of office, notwithstanding anything in its articles or in any agreement between it and him . . . ." 7(I) HALSBURY'S LAWS OF ENGLAND, Companies Act 1985, § 639 (4th ed. 1996).

[173] PAUL L. DAVIES, GOWER AND DAVIES' PRINCIPLES OF MODERN COMPANY LAW 307 (7th ed. 2003). In fact, "shareholders could be wholly written out of the appointment process." *Id.* at 309.

[174] *Id.* at 310.

[175] *Company Law in the United Kingdom*, *in* COMPANY LAW IN EUROPE, DIV. O, § 305, at 112 (Richard L. Thomas ed., Apr. 2005).

[176] Paul Davies, *Shareholder Value, Company Law, and Securities Markets Law: A British View*, *in* CAPITAL MARKETS AND COMPANY LAW 265-66 (Klaus J. Hopt & Eddy Wymeersch eds., 2003). This power of the shareholders is unwaivable. *Id.* It applies "notwithstanding anything in the articles of a company." Companies Act 1985, § 368 (Eng.).

director's shares additional weight in any resolution to dismiss him or her.[177] Corporations listed on the U.K. stock exchange are forbidden, however, from adopting similar arrangements under the listing requirements.[178]

This was not always the law in Britain. Before the passage of the Companies Act in 1948, shareholders were unable to remove directors before the expiration of their term in office without cause unless the articles of association provided otherwise. Nor could the directors resign preserving reciprocity.[179] Thus, Delaware's current statutory law resembles the law in Britain prior to 1948 and has become ill-suited to modern corporate conditions.[180]

In France, as well, though the board oversees the business of the corporation and may be elected for a term as long as six years, shareholders may always remove directors, notwithstanding any other provision in the company's documents or agreements.[181] Moreover, shareholders need not wait for the next annual meeting to replace directors. Instead, holders of ten percent of the voting shares are entitled to call for a special meeting of

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[177]Company Act 1985, §§ 311-13. In fact, in *Bushell v. Faith*, [1970] AC 1099, [1970] 1 All ER 53, HL, the House of Lords upheld a loading of voting rights (a golden share) in favor of a director threatened with removal, thus effectively enabling him to outvote the other shareholders regarding his removal. This decision, however, should be understood in the context in which it was given—a private corporation that functioned as semi-partnership in which the bylaw provision intended to protect a shareholder right to participate in the control over the corporation as well as provide him with employment. In other words, this decision would be especially relevant to private companies, where the ownership structure may be more akin to partnership than to public corporation, and, thus, removal of a director may deprive him or her of control over a substantial portion of his or her property.

[178]*See* Deborah A. DeMott, *The Figure in the Landscape: A Comparative Sketch of Directors' Self-Interested Transactions*, 62 LAW & CONTEMP. PROBS. 243, 250 n.32 (1999).

[179]EARL OF HALSBURY, THE LAWS OF ENGLAND § 389, at 242 (1910). But even then the court would not have enforced an agreement that a director should be irremovable. *Id.* Instead, if the company had in general meeting resolved that a director must retire, the court would not have compelled it to retain the director. *Id.*

[180] For a description of Delaware law, see *supra* Parts I & III.B.

[181]Under Article L225-18 of the Commercial Code directors "may be dismissed at any time by the routine shareholders' meeting. Any appointment made in breach of the preceding provisions shall be null and void . . . ." COMMERCIAL CODE, art. L225-18, *available at* http://195.83.177.9/code/liste.phtml?lay=ck&c=32&r=30001#art12293. Additionally, under Article L225-105, though a general meeting may deliberate only on matters included in its agenda, "[i]t may nevertheless remove one or more supervisory board members from office and replace them, in any circumstances." *Id. See also* James A. Fanto, *The Role of Corporate Law in French Corporate Governance*, 31 CORNELL INT'L L.J. 31, 75 (1998) (writing that French shareholders may remove directors "without cause at a shareholders' meeting").

the corporation.[182] Nor are shareholders required to provide notice to the director. A director may, however, sue for damages if the removal was "unfair or offensive."[183]

Similarly, in Italy, shareholders may always remove directors, though the company, or even the shareholders in some cases, may be liable for damages if the removal was without cause.[184] In the words of Michael Poole:

> [In the case of the SpA (la societa per azioni) the revocation must be at a properly constituted ordinary shareholders' meeting.] A revocation without just cause will still be valid, but the director may seek damages against the company and in certain cases against particular members. In the case of the Srl [la societa a responsabilita limitata], there is no legal requirement of just cause and so damages can only be sought on removal without just cause if so provided by the company memorandum and articles. . . . [In the case of the SapA (la societa in accomandita per azioni), removal from office] . . . must occur through an extraordinary shareholders' meeting. In the absence of just cause damages may be sought.[185]

The legal requirement of "just cause" pertains only to a director's entitlement to damages; the removal of a director is always valid regardless of whether the "cause" requirement is satisfied. Thus, though directors in Italy are generally appointed for a three-year renewable term, this in itself

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[182]Five percent of the shareholders may call a general meeting but ten percent are required for a special meeting. COMMERCIAL CODE, art. L225-103. *Cf. Company Law in France*, *in* COMPANY LAW IN EUROPE, *supra* note 175, at Div. D, §§ 163-164, 167, at 66-67 (Patrick Beauvisage & Laurent Jaeger eds., Apr. 2005) ("In principle, general meetings are convened by the Board of Directors. If the Board of Directors fails to do so, they may be convened . . . on the request of . . . one or more shareholders holding one-fifth of the issued share capital . . . ."). *Id.* § 167.

[183]*Id.* § 324. In France, too, management determines directors' appointment more so than shareholders do. *See* Fanto, *supra* note 181, at 53. Directors frequently represent management's interests more than shareholders' interests. *Id.*

[184]*See* C.C. art. 2383 (Italy) (addressing shareholder meeting's power to remove the board).

[185]*Company Law in Italy*, *in* COMPANY LAW IN EUROPE, *supra* note 175, at Div. H, §§ 308-309, at 114-15 (Michael Poole ed., Apr. 2005).

Note that the SpA is a joint stock company in which liability is limited by shares. *Id.* § 3, at 2. In the Srl, members' liability is limited by quotas. *Id.* The SpA is a joint stock company in which shareholders who are also directors are liable jointly and severally to the corporation's debts while other shareholders are liable only to the extent of their contribution to share capital. *Id.*

does not entrench directors in office in contrast to their counterpart American staggered board members, which are effectively entrenched.[186]

In Australia, the Australian Associated Stock Exchanges, as early as 1951, required listed companies to include in their articles of association a provision that the company, in an ordinary or extraordinary meeting, may by ordinary resolution remove a director before the expiration of his or her term in office.[187]

German corporate law takes a different approach. In the German close limited liability corporation, the Gesellschaft mit beschränkter Haftung (GmbH), shareholders may usually remove a managing director by a simple majority, but the articles of association or a Co-Determination Act may qualify this power when removal is without cause.[188] In an Aktiengesellschaft (AG), there is a two-tier board structure—the Vorstand, the Board of Management, which usually consists of top management, and an Aufsichtsrat, the supervisory board, which oversees the management and represents the shareholders.[189] A person cannot sit on both boards simultaneously. Under the Co-Determination Act, employees of companies numbering 2,000 or more are entitled to elect up to half of the members of the supervisory board.[190] The chairman of the board, however, who is usually elected by the shareholder representatives, casts the tie breaking vote.[191] Shareholders and employees elect members of the supervisory board for four- to five-year terms.[192] A member of the Board of Management may be removed by the supervisory board only for cause.[193] A vote of no confidence by the general meeting of shareholders, however,

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[186]*See* Giorgio Brunello et al, *CEO Turnover in Insider-Dominated Boards: The Italian Case*, 27 J. BANKING & FIN. 1027, 1031 (2003).

[187]Jean J. du Plessis, *Some Peculiarities Regarding the Removal of Company Directors*, 27 AUST. B. L. REV. 6, 8 (1999).

[188]*Company Law in Germany*, *in* COMPANY LAW IN EUROPE, *supra* note 175, Div. E, §§ 321-322, at 89 (Hans-Christian Albrecht & Jan Graf von Spee eds., Apr. 2005). Normally, a GmbH governance structure is composed of two tiers: shareholders and managing directors. It, however, may resemble the three-tier structure of an AG when a Co-Determination Act applies as further explained in the text.

[189]Klaus J. Hopt, *The German Two-Tier Board (Aufsichtsrat) A German View on Corporate Governance in* COMPARATIVE CORPORATE GOVERNANCE: ESSAYS AND MATERIALS 3 (Klaus J. Hopt & Eddy Wymeersch eds., 1997). In Germany, all publicly traded companies are AGs, but not all AGs are publicly traded.

[190]*Id.* at 4-5.

[191]*Id.*

[192]KRAAKMAN ET AL., *supra* note 146, at 62-63; *see also* Hopt, *supra* note 189, at 4-5.

[193]Albrecht & von Spee eds., *supra* note 188, § 362. *See also* Katharina Pistor et al., *The Evolution of Corporate Law: A Cross-Country Comparison*, 23 U. PA. J. INT'L ECON. L. 791, 816-17 (2002).

may sometimes be sufficient cause for his or her removal.[194] Holders of three-quarters of the voting shares may remove shareholder representatives on the supervisory board.[195] It seems that, in Germany, shareholder power to remove the board is restricted to protect the interests of third parties, primarily the employees. This, in turn, reflects both the policy of German law to require employee representation on the board and the related duty of the board to act in the best interests, not only of its shareholders, but also of its employees.

Until lately, Netherlands stood out for its restrictive protection of shareholder appointment and removal rights. Its regime was characterized as "[a]lone in the worldwide menagerie of corporate forms."[196] While in the majority of Dutch corporations shareholders elected their directors, members of the supervisory board elected their own successors under the "structure regime" of certain medium to large local companies.[197] If shareholders or employees objected to certain selections, the Enterprise Chamber of the Amsterdam Court of Appeal was the final decision maker. The court could have overruled them if their objection was unfounded.[198] Shareholders could have removed members of the supervisory board only for cause and after a court hearing.[199]

The supervisory board appointed the managing directors. It is interesting to note that even under this highly restrictive structure regime, shareholders could have removed supervisory directors for cause. In July 2004, Parliament passed an act that amended the Dutch Civil Code. The new act became effective as of October 1, 2004. Under the new provisions, the supervisory board has the right to nominate candidates in accordance

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[194]Hopt, *supra* note 189, at 4-5.

[195]KRAAKMAN ET AL., *supra* note 146, at 37 (stating that this is a default rule). *See also* Hopt, *supra* note 189, at 5 (noting that shareholder representatives may be removed by three-fourths of the votes or by the court for a "compelling reason").

[196]KRAAKMAN ET AL., *supra* note 146, at 36.

[197]*Id.* Generally, the structure regime applies to companies that employ on average one hundred employees in the Netherlands; its issued capital and reserves amount to at least EUR 16 million (in the past EUR 13 million); and it has a works council in place mandated by law. It is not intended to regulate small or international corporations and thus various exemptions may apply. BAKER & MCKENZIE, DOING BUSINESS IN THE NETHERLANDS 30-31, *available at* http://www.bakernet.com/NR/rdonlyres/BDFC517A-DD15-4420-BEED-A2B5587B7680/0/int8D.pdf; Martha Meinema, *Mandatory and Non-Mandatory Rules in Dutch Corporate Law*, 6 ELEC. J. COMP. L. 117, 158 (Dec. 2002), *available at* http://www.ejcl.org/64/art64-10.html.

[198]KRAAKMAN ET AL., *supra* note 146, at 36 n.11.

[199]*Id.*

with a "profile" presented to the general meeting and the works council.[200] While the supervisory board nominates candidates, the general meeting of shareholders appoints the supervisory directors. The general meeting may reject the nominations by a simple majority of the votes cast representing at least one-third of the issued capital. If the quorum requirement is not met, a simple majority is sufficient at a second meeting.

The works council has the right to recommend one-third of the supervisory board. If the supervisory board and the works council are deadlocked, the Enterprise Chamber makes the final decision. If the supervisory board accepts the works council's recommendation, the general meeting may nonetheless reject the nominee. Even under the new Act, the supervisory board still appoints and dismisses the managing directors.[201]

In addition, shareholders have the right to dismiss the entire supervisory board as distinguished from individual members. They may do so by a simple majority of the votes cast representing at least one-third of the issued capital. The works council, however, must be granted the opportunity to respond before such dismissal. In case of dismissal, the Enterprise Chamber appoints temporary supervisory directors who nominate candidates to be appointed by the general meeting. If the general meeting wishes to expel individual members, it must appeal to the Enterprise Chamber.[202]

The general meeting, the works council, and the supervisory board may agree to deviate from the statutory structure regime regarding the nomination and appointment of supervisory board members, but they may not opt out of the general meeting's right to reject a supervisory board nomination by a simple majority.[203] Thus, following this comprehensive late reform, even in the Netherlands, with regard to its most compulsory statutory two-tier structure regime, shareholders have potent rights to both appoint and remove directors. Such rights are mandatory and may not be

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[200]De Brauw Blackstone Westbrock, *Change of "Structure Regime"—Statutory Basis for Corporate Governance Code*, LEGAL ALERT 2 (July 7, 2004), *available at* http://www.debrauw.com/NR/rdonlyres/213302DE-0895-44FD-8749-CA0DDCBE0B75/0/LegalalertChangeofstructureregime.pdf, at 2.

[201]*See id.* at 4. *See also* Baker & McKenzie, *supra* note 197, at 30 (stating that supervisory directors advise and supervise the managing directors but do not participate in the company's management).

[202]De Brauw, *supra* note 200, at 6. Interestingly, Vice Chancellor Leo E. Strine of the Delaware Court of Chancery has recently suggested reforming corporate elections so that shareholders will have a potent power to replace, periodically, the entire board. Strine, *supra* note 2, at 1781. He emphasizes that boards often act unanimously and thereby share responsibility, and it is better to contest a full slate than target a few directors thus potentially causing friction on the board. *Id.*

[203]De Brauw, *supra* note 200, at 5.

waived. The Netherlands has moved from striking out its shareholders from the appointment process to mandating their involvement in both appointment and removal.

Therefore, with the exception of Germany, in all of the jurisdictions examined, shareholders may always remove directors from office, although they might be liable for damages if their removal is found to be unjustified. Moreover, some countries treat shareholder removal power as even more important than their appointment power. This may align with current U.S. corporate practice in which shareholders are generally passive about appointing directors, and thus it may be more advisable to enhance their power to remove directors. Even in Germany, where shareholder removal power is restricted to guarantee the rights of employees, shareholders' dissatisfaction may amount to "cause" for removal. Delaware law, however, neither shares this commitment to employee representation nor recognizes shareholders' dismay as "cause" for removal of staggered board members. Consequently, a comparative analysis finds that Delaware law on staggered boards falls behind corporate law development in other countries and is even biased in favor of the board.

F. *Constitutional Analogy*

Corporate scholars increasingly borrow arguments from constitutional governance and apply them in the corporate context.[204] Specifically, supporters of staggered boards have often relied on the political experience with staggered terms or entrenchment mechanisms to justify their use in the corporate context.[205] They argue that staggered terms are common in governmental bodies in general and point to the U.S. Senate in particular, claiming entrenchment mechanisms are as appropriate in the corporate setting as they are in government. This article next examines each of these arguments in turn and reveals why even they fail to legitimize entrenched staggered boards.

1. Independent Agencies

In a leading article on staggered boards from 1999, Koppes, Ganske, and Haag suggest that "[t]he benefits derived from the use of classified

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[204] *See, e.g.*, Bebchuk, *supra* note 16, at 890-91 (comparing shareholder initiatives to political referenda).

[205] *See, e.g.*, Marcel Kahan & Edward B. Rock, *Corporate Constitutionalism: Antitakeover Charter Provisions as Precommitment*, 152 U. PA. L. REV. 473, 473 (2003); Koppes et al., *supra* note 79.

boards apply, not only to corporations, but to government institutions and other non-corporate entities as well."[206] Is this so?

In the public arena, staggered terms are typical of independent agency boards.[207] For example, members of the Consumer Product Safety Commission (CPSC) serve seven-year staggered terms,[208] as do members of the Federal Trade Commission.[209] Members of the Federal Election Commission (FEC) serve six-year staggered terms.[210] Similar staggered provisions exist for the Federal Reserve Board,[211] as they did for the Interstate Commerce Commission,[212] among other examples. Moreover, not only do members of independent agencies serve staggered terms, they can only be removed for cause.[213] They thus enjoy a status similar to that of directors of staggered boards in Delaware.

Interestingly, however, when courts construe statutes dealing with independent agencies, it is not the statutory provisions for staggered terms and for-cause removal that determine their status as independent agencies, but rather the reverse. The courts have stated that whether Congress can "condition the [president's] power [of removal] by fixing a definite term and precluding a removal except for cause will depend upon the character of the office."[214]

For quasi-legislative and quasi-judicial agencies, the court would recognize limitations on the presidential removal power to ensure the independence of the agency.[215] If it is a quasi-executive agency, on the other hand, despite staggered terms and removal-for-cause provisions, the court would allow the president to remove members of the agency at his or

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[206]Koppes et al., *supra* note 79, at 1051.

[207]"The independent agency generally has multiple member boards with staggered terms . . . ." George E. Fraley, Note, *Is the Fox Watching the Henhouse?: The Administration's Control of FEC Litigation Through the Solicitor General*, 9 ADMIN. L.J. AM. U. 1215, 1263 (1996).

[208]15 U.S.C. § 2053(b)(1) (2005).

[209]*Id.* § 41.

[210]2 U.S.C. § 437c(a)(2)(A) (2005).

[211]12 U.S.C. § 242 (2005). The governors serve fourteen-year nonrenewable staggered terms.

[212]49 U.S.C. § 10301(c) (1995). This section was omitted when the Commission was dismantled in 1995. *See* Interstate Commerce Commission Termination Act of 1995, Pub. L. No. 104-88, 109 Stat. 803 (1995) (codified as amended in scattered sections of 49 U.S.C.).

[213]*See, e.g.*, 15 U.S.C. § 41 (2005) (allowing removal only "by the President for inefficiency, neglect of duty, or malfeasance in office"); *id.* § 2053(a) ("Any member of the Commission may be removed by the President for neglect of duty or malfeasance in office but for no other cause.").

[214]Humphrey's Ex'r v. United States, 295 U.S. 602, 631 (1935).

[215]*Id.* at 629.

her discretion.[216] Thus, staggered terms and removal-for-cause provisions are the start rather than end point of statutory interpretation. In the United States Supreme Court's words:

> The authority of Congress, in creating quasi legislative or quasi judicial agencies [sic] to require them to act in discharge of their duties independently of executive control cannot well be doubted; and that authority includes, as an appropriate incident, power to fix the period during which they shall continue [in office,] and to forbid their removal except for cause in the meantime.[217]

The rationale for the Court's approach is that staggered terms and removal-for-cause provisions isolate members of the appointed body from the control of the appointing authority.[218] Though the executive appoints members of independent agencies, they are not its agents but rather servants of the general public. To protect their independence, staggered terms and removal-for-cause provisions are adopted. But even in this seemingly legitimate context, the independence of such agencies is a much-contested issue.[219]

Moreover, staggered terms create independence, not only by protecting officers from removal, but also by preventing the concentration of appointing power in one person or group of persons. Thus, for example, if the president is elected every four years, but members of independent agencies serve staggered terms that are longer than four years, then it is impossible for a president to determine the full board of an independent

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[216]While independence may be desirable in some situations, in others it may frustrate constitutional governance. For example, in *Morrison v. Olson*, 487 U.S. 654 (1988), Congress sought to isolate the independent counsel from possible removal by the president. *Id.* at 677. It believed that if he or she were not independent, the counsel would not investigate criminal charges against high-ranking executives because of the inherent conflict of interests involved in a body investigating itself. *Id.* In contrast, the Court previously held that the president cannot properly perform his or her constitutional tasks if he or she cannot remove executive officers such as postmasters at will. Myers v. United States, 272 U.S. 52, 132-34 (1926). Thus it is the nature of the office, rather than the existence of staggered terms and "for-cause" removal provisions, that determines whether we should protect members of the agency from removal at will by the appointing authority.

[217]*Humphrey's Ex'r*, 295 U.S. at 629.

[218]"Once an officer is appointed, it is only the authority that can remove him, and not the authority that appointed him, that he must fear and, in the performance of his functions, obey." Synar v. United States, 626 F. Supp. 1374, 1401 (D.D.C. 1986), *aff'd sub nom.* Bowsher v. Synar, 478 U.S. 714 (1986).

[219]*See, e.g.*, Geoffrey P. Miller, *Independent Agencies*, 1986 SUP. CT. REV. 41 (1986) (examining the executive removal power with regard to independent agencies).

agency, at least not in one term. This tends to lend a non-partisan flavor to the independent agency.[220]

How do these considerations play out in the corporate field? Since staggered boards in Delaware enjoy protection against removal without cause, board members are isolated from shareholder control. Moreover, assuming ownership of the corporation changes constantly in publicly-held firms, there is rarely a situation in which the same group of shareholders can determine the composition of the entire board. Both results might be desirable if directors had to serve the interests of third parties, parallel to the "general public" that independent agencies are intended to serve. But as I have already discussed,[221] directors should be regarded doctrinally, and from a law and economics perspective, as the agents of the shareholders.[222] Therefore, we should enhance, rather than weaken, the dependence of directors on shareholders. The justification for isolating independent agencies from removal does not apply to staggered boards in corporations.

2. The U.S. Senate

Many corporate law treatises explain that the method of electing directors to staggered boards is similar to the election to the U.S. Senate and serves similar functions.[223] Just as U.S. senators are elected for six-year staggered terms, directors are typically elected to three-year staggered terms.[224] Even as staggered terms enable senators to focus on long-term benefits to the country, so they enable directors to plan for the long haul. Staggered terms also isolate both from the transitory pressures of their constituents.

This analysis fails to take into account, though, the fact that the U.S. Senate serves as a second chamber. It supplements the functions of the first chamber which is chosen in full at the same time that one-third of the Senate is elected. As such, the Senate can be more isolated from the

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[220] *See, e.g.*, Philip D. Oliver, *Systematic Justice: A Proposed Constitutional Amendment to Establish Fixed, Staggered Terms for Members of the United States Supreme Court*, 47 OHIO ST. L.J. 799, 800-01 (1986) (proposing to adopt staggered terms for Justices of the Supreme Court to guarantee that every president is entitled to nominate at least some members of the Supreme Court).

[221] *See supra* Part III.C.-D.

[222] In fact, no one has suggested that staggered boards are desirable because we want to isolate directors from shareholder control. Supporters of staggered boards claim that they isolate directors from management control. *See supra* Part III.A. For a rebuttal of this claim, see *supra* Part III.A.3.

[223] *See, e.g.*, FRANKLIN A. GEVURTZ, CORPORATION LAW 187 (2000).

[224] FLETCHER ET AL., *supra* note 6, § 334.10.

people's control and serve as part of the "checks and balances" between branches of government. That this figured large in the Framers' minds when writing the Constitution is evident from Hamilton's words in Federalist No. 61 regarding the first chamber. Hamilton explained that the Framers opted for election of the entire House of Representatives, preferring even less frequent elections of the entire house to more frequent staggered elections:

> I allude to the circumstance of uniformity in the time of elections for the federal House of Representatives. It is more than possible that this uniformity may be found by experience to be of great importance to the public welfare, both as a security against the perpetuation of the same spirit in the body, and as a cure for the diseases of faction. If each State may choose its own time of election . . . [t]he consequence of this diversity would be that there could never happen a total dissolution or renovation of the body at one time. If an improper spirit of any kind should happen to prevail in it, that spirit would be apt to infuse itself into the new members, as they come forward in succession. The mass would be likely to remain nearly the same, assimilating constantly to itself its gradual accretions. . . . I am inclined to think that treble the duration in office, with the condition of a total dissolution of the body at the same time, might be less formidable to liberty than one third of that duration subject to gradual and successive alterations.[225]

By way of contrast, in Federalist No. 63, when discussing a second chamber, Madison explained the need for continuity and long-term perspective, rather than accountability, to balance the functions of the lower house.[226]

Thus, corporate staggered boards should not be so readily compared to the U.S. Senate, as its reason for existence is very different. U.S. boards are unicameral. When the board is staggered, its members are isolated from shareholder influence during their term in office, and there is no

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[225]THE FEDERALIST NO. 61, at 375 (Clinton Rossiter ed., 1961). Note that Bebchuk's, Coates', and Subramanian's observation that triennial elections to the board may be preferable to staggered elections aligns with the sentiment expressed in this Federalist Paper. *See supra* text accompanying notes 31-34.

[226]THE FEDERALIST NO. 63, *supra* note 225, at 383-84.

compensatory mechanism similar to the House of Representatives to offset this.

3. Constitutional Entrenchment

In a well-received December 2003 article, Kahan and Rock argue that a shareholder decision to entrench decision-making power in the board by staggered terms should be respected.[227] This commitment *ex ante* may improve shareholder position *ex post* by allowing the board to obtain better takeover premiums in case the company is sold. In fact, these authors argue the board may be better able than shareholders to implement selling strategies that would benefit shareholders.[228]

Kahan and Rock also argue that empirical evidence does not support either shareholder choice (Jacksonian regime) or board veto (Hamiltonian regime), and that, therefore, a shareholder decision regarding their governance, including the decision to entrench board power (Madisonian regime), should likewise be respected.[229] Different governance regimes may be optimal for different corporations depending on a variety of factors, including agency costs and informational advantages of the board. Current Delaware law respects these shareholder choices.[230]

The two authors claim that entrenchment choices may be more justified in the corporate than in the constitutional context:

> Corporate constitutionalism raises fewer theoretical difficulties than political constitutionalism. In the corporate context, as opposed to the political context, the justification of the legitimacy of the constitutional document can more convincingly rest on a straightforward contractarian argument because consent is actual not constructive. Investors need not buy shares of a company in an IPO or secondary market if they do not like the charter. Likewise, claims of constructive

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[227]Kahan & Rock, *supra* note 205, at 475. Kahan and Rock suggest that a board's defensive tactics should be treated according to the governance structure adopted by the firm. *Id.* at 510-15. When a firm opts for an effective staggered board by including staggered terms in its charter, the court should respect that decision and the board's attempt to implement that structure, i.e., by appointing directors to fill vacancies on the board. Conversely, if staggered terms are included in the bylaws, directors' attempt to entrench themselves should be treated with suspicion. *Id.* However, this assumes what needs to be proven. The question remains whether shareholders intended entrenchment even if they included staggered board provisions in the charter.

[228]*Id.* at 484-89.

[229]*Id.* at 475.

[230]*Id.* at 521.

> consent to midstream developments based on the possibility of exit are more convincing in the corporate context than in the political context because dissatisfied shareholders have a more realistic exit option than dissatisfied citizens do. . . . As a result, the possibility of exit imposes more significant constraints on managers and controlling shareholders than on governments.[231]

While their article is a significant application of constitutional considerations to the corporate context, their argument that entrenchment is desirable or even logical in the corporate context is disputable. In support of the contractual nature of entrenchment, they point to the entry and exit strategies available to shareholders dissatisfied with entrenchment.[232] They do not justify, however, the problematic nature of the entrenchment: why can a majority of current shareholders not undo the entrenchment from a contractual perspective? If parties made a contract, the same parties may consent to change the contract and form a new contract. This is basic contract law. Why should the same not apply to staggered terms? If a majority of shareholders may contract for all shareholders and bind them to entrenched staggered terms, why can a majority not undo the entrenchment, thus formulating a new contract? In particular, this should be the case in light of the fact that corporate law treats bylaws and charter provisions as contracts between shareholders. Third parties, including directors, are thus on notice that the terms of the contract may change without their consent.[233]

Moreover, Kahan and Rock take too literally the concept of the "social contract" as the underlying rationale for constitutional law. Even adherents of constitutional entrenchment do not believe that it is contract law that provides legitimacy to the entrenched nature of the constitution. In other words, social contract is not contract law.[234] Rather, Kahan and Rock recognize that there must be a way to overcome corporate entrenchment. They thus suggest that courts should be allowed to intervene if the board abuses its power by acting for entrenchment purposes, i.e., to preserve themselves in office rather than serve shareholder interests.[235] But

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[231]Kahan & Rock, *supra* note 205, at 491.

[232]*Id.* at 494-97.

[233]DEL. CODE ANN. tit. 8, §§ 109, 242 (2005). *See, e.g.*, *Roven*, discussed *supra* text accompanying note 118.

[234]JEAN-JACQUES ROUSSEEAU, ON THE SOCIAL CONTRACT 143-45 (Maurice Cranston trans., 1968).

[235]Kahan & Rock, *supra* 205, at 517-18.

if they trust the courts to undo entrenchment, why not trust the shareholders who initially instituted it or consented to it?

Perhaps the most difficult aspect of this article is that the authors rely on their analogy to constitutional law to make their case that "pre-commitment" is sometimes desirable in the corporate context.[236] Pre-commitment in constitutional law, however, is discussed in the context of content provisions rather than the entrenchment of personnel in staggered terms for directors.[237] Moreover, in constitutional law the majority imposes limitations upon itself to protect the rights of minorities, but staggered boards sacrifice the rights of minority shareholders.[238]

Further, constitutional scholars struggle with the "counter-majoritarian" difficulty.[239] How can it be justified from a democratic perspective that past majorities dictate the choices of current majorities? In other words, constitutional discourse has long focused on how to overcome entrenchment and allow the current majority to decide constitutional law. Many have suggested that, despite constitutional entrenchment, current majorities may change the constitution.[240] Should corporate law, though, develop the way constitutional law has when there is the opportunity to avoid this? We should especially be cautious about borrowing justifications for entrenchment from constitutional law, since the underlying rationale for it is economic activity under corporate law, as distinguished from political rights under constitutional law.

Moreover, Kahan and Rock borrow from constitutional law without having the protective mechanisms in place to balance against entrenchment. In constitutional governance, there are different institutions—for example,

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[236]*Id.* at 572.

[237]In constitutional law, it is usually discussed regarding the difficulty to amend the constitution. *See, e.g.*, RESPONDING TO IMPERFECTION: THE THEORY AND PRACTICE OF CONSTITUTIONAL AMENDMENT (Sanford Levinson ed., 1995).

[238]*See* discussion *supra* Part III.C.2.

[239]For the classic discussion of the difficulty, see ALEXANDER M. BICKEL, THE LEAST DANGEROUS BRANCH: THE SUPREME COURT AT THE BAR OF POLITICS (2d ed. 1986).

[240]Thus, for example, Bruce Ackerman and Akhil Amar have suggested that the Constitution may be amended outside Article V procedures. *See, e.g.*, 1 BRUCE ACKERMAN, WE THE PEOPLE: FOUNDATIONS (1991) [hereinafter ACKERMAN, FOUNDATIONS]; 2 BRUCE ACKERMAN, WE THE PEOPLE: TRANSFORMATIONS (1998) [hereinafter ACKERMAN, TRANSFORMATIONS] (describing a "dualist model" under which constitutional amendments have occurred—including the 13th, 14th, and 15th Amendments—despite violating Article V procedures); Akhil Reed Amar, *Philadelphia Revisited: Amending the Constitution Outside Article V*, 55 U. CHI. L. REV. 1043, 1066-71 (1988); Akhil Reed Amar, *The Consent of the Governed: Constitutional Amendment Outside Article V*, 94 COLUM. L. REV. 457, 457 (1994) ("We the People of the United States have a legal right to alter our government—to change our Constitution—via a majoritarian and populist mechanism akin to a national referendum, even though that mechanism is not explicitly specified in Article V.").

the House of Representatives, the Senate, the President, and the Judiciary in the United States—competing with each other for authority to speak for the people.[241] But no one competes with the board for authority to speak for the shareholders. Thus, shareholders must retain the power to supervise their representatives and remove them if necessary.

IV. CONCLUSION

As discussed, under current understanding, even when a majority of shareholders desire to remove members of staggered boards or wish to undo the provisions of staggered boards altogether, they may be unable to effect their will. Delaware law restricts the removal of staggered boards to "for-cause" situations unless otherwise provided in the certificate, and certificates can be repealed only with the board's approval. Certificates also typically require that staggered board provisions be repealed by a "supermajority" vote of shareholders.[242] Thus, corporate democracy is frustrated. This is all the more serious, given that shareholders are often passive participants in the nomination of directors.[243]

We have seen no offsetting benefits to entrenched staggered boards. They curtail shareholders' choice, rather than enhance it, and usually sacrifice, rather than protect, minority interests.[244] Moreover, the limitation on removal of directors does not follow general principles of agency law, nor does it match the development of corporate law in other jurisdictions.[245] Even the law on independent agencies, which enjoys similar protections of staggered terms and "for-cause" removal, suggests the appointing authority should have the power to remove its appointees unless they were appointed to serve the interests of third parties.[246] A more focused look at Delaware statutory history suggests that, though the restriction on removal of staggered board members intended to codify the rationale of a judicial

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[241] ACKERMAN, FOUNDATIONS, *supra* note 240; ACKERMAN, TRANSFORMATIONS, *supra* note 240.

[242] *See supra* Part I.

[243] *See supra* Part III.A.

[244] *See supra* Part III.C.2. This is especially so in light of the availability of poison pill protection, which effectively imposes a deterring premium on prospective purchasers by diluting their stake. Because of the poison pill, it is the current shareholders, rather than the "raiders," who own a majority of the shares at the time of the meeting deciding the fate of the staggered board. In addition, the board has time to present its case to the shareholders, including its opinion on a prospective tender offer. Bebchuk et al., *supra* note 11.

[245] *See supra* Parts III.C. & E.

[246] *See supra* Part III.F.

opinion, the drafters both misinterpreted and applied an invalid judicial decision on the subject.[247]

How then should staggered board members be treated? Delaware currently treats staggered board members' term of office under a property rule. Shareholders may not remove staggered board members before the expiration of their term without their consent. This article, however, suggests that we treat staggered board members' entitlement to office under a liability rule. Shareholders should be able to remove them subject to fair pay.[248] Absent consent, such fair pay will be determined by the courts.

This approach aligns with distributional considerations that seek to maximize shareholders', rather than directors' (and indirectly managers'), wealth. If by removing directors from office and replacing an inefficient board with an efficient one shareholders may increase corporate wealth, protecting staggered directors' entitlement to office by a property rule enables the board to extract a large portion of the surplus created by such a removal. They would not agree to be removed until paid that share of the surplus agreeable to them as precondition for leave. Conversely, under a liability rule regime, absent consent, the courts would determine the compensation due the directors for early leave. This collective valuation may be easily ascertained based on the pay directors expected to receive for their full term. Collective valuation thus does not entail prohibitive costs. Moreover, Delaware courts are experts in corporate matters and are well equipped to deal with such evaluation.

This result is efficient as well. Currently, directors cannot be removed without their consent, and some may hold-out to extract a better price for their leave. A liability rule increases the likelihood that efficient removals will occur. This approach is supported by policy-consistency considerations as well. As elaborated, such a liability approach is prevalent in other similar fields of law, like agency, and consistent choices of law are more efficiently enforced.[249]

The solution proposed in this article has two aspects: (1) a strategy for shareholders to adopt, and (2) a policy for courts to adopt. Shareholders and courts should reinterpret a statute such as Delaware's—allowing "for-

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[247] *See supra* Part III.B.

[248] For the classic distinction between property and liability rules, see Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972).

[249] *Id.* at 1103-04. The various complementary rules enhance one another and compliance is simpler when people do not have to distinguish between the various rules.

cause" removal—as allowing removal-for-cause without compensation.[250] If the removal is not for cause, however, then it should nevertheless be sustained as an exercise of inherent removal power, and damages should be awarded to the removed director.[251] This is not the current interpretation of Delaware statutory law accepted by the courts.[252] However, Delaware courts may achieve it without amending legislation. The inherent power to remove directors may be derived from doctrines recognized under agency, contract, and even constitutional law, as discussed above.[253] In light of the direct and personal fiduciary relationship between directors and shareholders, such a relationship cannot be irrevocable. In such relationships, the law distinguishes between the inability to force the relationship on an unwilling principal and the monetary remedy awarded for breach of the relationship.

Alternatively, shareholders may argue that their dissatisfaction with the performance of directors should be recognized as "cause" for their removal. While most Western jurisdictions examined in this article recognize a general removal power for shareholders, even in Germany, which does not recognize such power, shareholders' dissatisfaction with directors may be recognized as sufficient reason for their removal.[254] For the policy and doctrinal reasons advanced in this article, courts should uphold removals that have been made for cause according to appropriate shareholder procedures, even if the cause is later found to have been insufficient. If the cause for removing a director is found to have been sufficiently substantial to validate the vote of removal, as a matter of corporate governance, yet insufficient as a contractual matter between the director and the company, the remedy should be the traditional remedy for breach of contract: money damages, not reinstatement.[255]

The mechanics of such removal would be the same as would be available to shareholders if the board were not staggered. Thus, if shareholders are authorized by state law, a corporation's certificate, or its

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[250]This aligns with general principles of contract law. When directors are removed for cause, they cannot sue under their contract because they are deemed to have breached their contract. Roger G. Bailey, *Shareholder Control Over Management: The Removal of Directors*, 20 MCGILL L.J. 85, 96-97 (1974).

[251]If the staggered board was installed for the protection of a class of shareholders, however, then it should be subject to the limitations on removal as provided under § 141(k)(2) of the Delaware Code. *See* discussion *supra* Part III.C.2.

[252]*See supra* Part I, especially *supra* notes 6-9 and accompanying text.

[253]*See supra* Parts III.C., D. & F.

[254]*See supra* Part III.E.

[255]*See also* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 131 (2003) (writing that specific performance is an exceptional contractual remedy under Anglo-American law).

bylaws, to call for a special meeting or act by written consent—as authorized in Delaware[256]—then they may be able to effect their will immediately. Otherwise, it is expected that they would have to wait for the next annual election and hold a proxy contest challenging the entire board (rather than just a third of it).[257]

This interpretation accords with the statutory history of the Delaware provision.[258] It also aligns with general principles of contract and agency law, trends in comparative corporate law, and even constitutional law.[259] Most importantly, it serves the purposes for which statutory divisions of power between shareholders and directors are designed.

When the Delaware Court of Chancery decided *Essential Enterprises*, it was unclear whether shareholders could remove directors without cause even if the board was not staggered.[260] The common law rule at the time was that directors had a vested right in their office. Their powers were considered a grant from the state rather than a delegation from the shareholders.[261] Shareholders had an "inherent" and inalienable right to remove directors but only for cause.[262] This, however, no longer reflects how we view directors. Today, almost no one disputes that directors should serve the interests of shareholders; rather, the dispute concentrates around the questions of whether and to what extent directors should

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[256]DEL. CODE ANN. tit. 8, § 228(a) (2005). This section permits a majority of the shareholders to act immediately and without prior notice to the minority to remove a director unless the certificate provides otherwise. However, many public companies opt-out of this arrangement in their charter. *Cf.* MODEL BUS. CORP. ACT § 7.04 (a) (2005) (requiring unanimous written consent in lieu of a general meeting). *See* Michael P. Dooley & Michael D. Goldman, *Some Comparisons Between the Model Business Corporation Act and the Delaware General Corporation Law*, 56 BUS. LAW. 737, 759 (2000-2001).

[257]See also the SEC's proposal to grant shareholders more access to the ballot *supra* note 2, at 60,284.

[258]*See supra* Part III.B.

[259]*See supra* Part III.C., E. & F.

[260]*See supra* Part III.B.

[261]In fact, historically, corporations began as entities with individual charters granted by the state. Lipton & Rosenblum, *supra* note 84, at 192-93. General incorporation statutes date from the late nineteenth century.

[262]*See* MODEL BUS. CORP. ACT § 8.08, cmt. "Yet the feeling of the courts has been that a director once elected is like a public official, not a mere employee, and that the statutory scheme for corporate government contemplates his serving until the expiration of his term and the qualification of his successor." Joe G. Davis, Jr., *Corporations—Stockholder's Right to Remove Directors*, 7 BAYLOR L. REV. 313, 317 (1955). *See also supra* Part III.B.

Courts also treated directors as trustees, rather than agents; thus, they could not be removed but for cause. William H. Dye, *Corporations—Removal of Officers and Directors*, 8 KAN. L. REV. 154, 154 (1959).

additionally take into account other constituencies' interests.[263] Further, contrary to the statute existing when *Essential Enterprises* was decided, the Delaware statute today explicitly recognizes shareholder removal power.[264]

Moreover, the current treatment of staggered boards does not reflect the status of public officials. Even in the public arena, an appointing authority usually has the power to remove an appointee. Removal power is considered the corollary of appointment power. Even when it is not, as with independent agencies, a dismissed officer is only able to get damages. It is only his or her pecuniary interest that is protected. Thus, no president has ever been required to reinstate an independent officer whom he removed.[265] Instead, officers, protected under a "for-cause" provision but nevertheless removed without cause, were awarded damages.[266]

This approach also aligns with general principles of contract and agency law. In contract law, when dealing with contracts for personal service, courts usually do not order "specific performance"; rather, they award damages for breach.[267] This policy is based on two rationales: (1) it would amount to a servitude to require a person to perform a service that he or she does not wish to perform, and (2) it would create friction between the two parties.[268]

The first rationale is reflected in a director's right to resign despite any contract to the contrary, including staggered terms.[269] The second rationale should be relevant when shareholders wish to remove a director, as it would cause friction to force a prolonged relationship when the shareholders are dissatisfied with the director. Similarly, as we saw under

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[263]*But see* Lipton & Rosenblum, *supra* note 84, at 192-95 (suggesting that we treat corporations as public entities rather than under a private ownership model).

[264]*See supra* Part III.B.

[265]"It is noteworthy that the President has never been judicially compelled to *reinstate* a government official whose removal he ordered." LAURENCE TRIBE, AMERICAN CONSTITUTIONAL LAW 250 n.20 (2d ed. 1988).

[266]Tracey A. Hardin, Note, *Rethinking Independence: The Lack of an Effective Remedy for Improper For-Cause Removals*, 50 VAND. L. REV. 197, 198-200 (1997). Thus, for example, in the landmark case of Humphrey's Executor v. United States, 295 U.S. 602, 632 (1935), the claim was for salary withheld from plaintiff's testator as a Federal Trade Commissioner, from the time when the president wrongfully removed him from office to the time of his death (over a year's worth of salary). The plaintiff was granted the requested salary. *Id.*

[267]*See* POSNER, *supra* note 255, at 131.

[268]*See, e.g.*, ROBERT E. SCOTT & JODY S. KRAUS, CONTRACT LAW AND THEORY 990 (rev. 3d ed. 2000); *but see* Cynthia L. Estlund, *Wrongful Discharge Protections in an At-Will World*, 74 TEX. L. REV. 1655 (1996) (describing how the law has changed regarding discharge of employees for "particular bad reasons," including discrimination).

[269]DEL. CODE ANN. tit. 8, § 141(b) (2005). In fact, outside directors resign easily. *See* Alfred F. Conard, *The Supervision of Corporate Management: A Comparison of Developments in European Community and United States Law*, 82 MICH. L. REV. 1459, 1472-73 (1984).

agency law, a principal may remove his or her agent, though the principal may have to pay damages for breach of contract.[270]

This is also the law of the major jurisdictions examined above, especially Britain, from which the restriction on removal originally comes.[271] In fact, this is exactly how the legal requirement of "just cause" is interpreted in Italy.[272] Regardless of whether cause exists, the removal is valid. If the law requires cause, however, then a director, who has been removed without cause, may seek damages.[273]

Moreover, this aligns with the interests protected under Delaware law. It seems that Delaware intended to protect the pecuniary interest of directors rather than their voting power or their entitlement to office. Courts have usually allowed shareholders to pack boards with new members despite a staggered board provision, reflecting that it is not directors' voting power that is protected.[274] Courts have also allowed shareholders to amend the certificate to enable the removal of incumbent staggered directors, demonstrating that it is not directors' entitlement to office that is protected.[275]

It is also important to note that this interpretation does not require a change in the Delaware statute. In light of states' competition to attract incorporation, it is doubtful whether the Delaware legislature would have amended its statute to remedy the problem of staggered boards.[276] Fortunately, statutory interpretation rather than amendment may suffice to remedy entrenched staggered boards.

While this article's suggestion is intended to solve the problem that entrenched staggered boards pose for corporate governance in general, it

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[270]*See supra* Part III.C.

[271]*See supra* Part III.E.

[272]*Id.*

[273]*See supra* note 184 and accompanying text.

[274]In fact, this is why corporations often protect staggered boards by an explicit provision that restricts the manner in which the board's size may be changed. In the absence of such a provision, courts allow to pack staggered boards with new members. *See* FLEISCHER & SUSSMAN, *supra* note 12, at 6-29.

Shareholder power to pack a staggered board is what motivated the litigation in *MM Cos. v. Liquid Audio, Inc.*, 813 A.2d 1118 (Del. 2003). *See supra* text accompanying notes 120-24. In that case, directors of a staggered board tried to pre-empt shareholders' attempt to pack the board by enlarging the board's size and filling the vacancies with new members. The court invalidated the actions of the board. Similar circumstances existed in *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988). *See supra* note 124.

[275]*See supra* text accompanying note 118 (discussing *Roven v. Cotter*, 547 A.2d 603 (Del. Ch. 1988)).

[276]*See supra* note 98 and accompanying text; *see also supra* Part III.B (discussing the history of Delaware's adoption of the staggered board provision and the shakiness of the statutory basis for entrenched staggered boards).

may also offer a solution to their harsh antitakeover effects when coupled with a poison pill. Since shareholders may remove even directors of staggered boards before the end of their term under this approach, shareholders faced with a desired hostile takeover may elect a new board that will redeem the pill and allow the transaction to take place. Moreover, this may be done, not because we undermine the consensual basis for staggered boards, but because the law should not tolerate the irrevocability of a quasi-agency relationship of the type existing between shareholders and directors. Further, in replacing the board, shareholders do not replace the board's discretion with theirs. Thus, this approach may suggest common ground to the otherwise opposing schools of director versus shareholder primacy in corporate governance.

What are the implications of this suggested approach? Usually, shareholders will not remove directors. As previously noted, shareholders of publicly-held corporations have to overcome collective action, rational apathy, and free-ride problems to remove directors.[277] But when they do overcome those problems due to the importance of the issue at stake, they should be allowed to remove the directors. All they have to do, in the absence of sufficient cause, is pay the directors the fee they would have earned had they remained through the end of their term. Surely, the economic justification for such an approach is straightforward. Typically, directors' fees are not substantial.[278] But the costs imposed on shareholders by forcing them to keep directors they oppose may be formidable. This result has long been justified in contract law as an "efficient breach" we

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[277] *See supra* Part III.A.3. "In practice, obstacles to collective action in large public firms make it extremely unlikely that the shareholders can oust incumbent board members except in extreme cases." Stout, *supra* note 24, at 849 n.12. Furthermore, "it must be remembered that incumbent directors have a large advantage in proxy contests because they can spend the company's money to tell their story and retain important, if not unconstrained, discretion regarding timing." Strine, *supra* note 24, at 865 n.6.

[278] "Over the last four years, median director pay at the 350 largest U.S. companies has increased by nearly fifty percent, rising from $105,000 to $155,000. According to a recent survey, the director average annual cash retainer is $37,250, with an average of $46,942 for New York Stock Exchange companies versus $30,314 for NASDAQ companies." David A. Katz & Laura A. McIntosh, *Corporate Governance: Director Compensation* (Mar. 23, 2006), *available at* http://www.realcorporatelawyer.com/pdfs/wlrk032406.pdf. For discussion of the history of director compensation from a legal norm of no-payment to increasing fees, see Charles M. Elson, *Director Compensation and the Management-Captured Board—The History of a Symptom and a Cure,* 50 SMU L. REV. 127 (1996-1997).

Furthermore, most directors in public corporations have full time positions outside the corporation and may even serve as directors in multiple companies. In recent years, public corporations have tended to nominate a majority of disinterested directors. They do not rely on their pay as directors for income. Olga N. Sirodoeva-Paxson, *Judicial Removal of Directors: Denial of Directors' License to Steal or Shareholders' Freedom to Vote?*, 50 HASTINGS L.J. 97, 142 (1998).

want to encourage.[279] It is time to implement it in corporate law as well. To paraphrase Churchill, in corporate law just as in politics, democracy may not be the ideal form of government, but it is preferable to the alternatives.[280]

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[279] *See* COOTER & ULEN, *supra* note 168, at 289-92; POSNER, *supra* note 255, at 118-35; *cf.* Daniel Friedmann, *The Efficient Breach Fallacy*, 18 J. LEGAL STUD. 1 (1989) (taking issue with the standard analysis of efficient breach).

[280] 7 WINSTON S. CHURCHILL: HIS COMPLETE SPEECHES: 1897-1963, at 7566 (Robert Rhodes James ed., 1974).