
WHY NOT A CEO TERM LIMIT?

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In this Essay, I ask: Why not require a mandatory CEO term limit? My purpose is not to advocate a term limit (although, as a stalking horse, I include a proposal in this Essay), but rather to ask why CEO term limits are out of bounds – not addressed within the corporate governance scholarship – when they have long been recommended for directors and, more recently, implemented for public company auditors.

The traditional answer has been that CEOs are agents of the corporation, subject to control by the board, which holds primary responsibility for the firm’s business and affairs. Senior officers are largely shielded from outside interference, permitting them to execute consistent, long-term business strategies under board oversight. Variations in governance can be privately ordered among shareholders, directors, and officers, but in most circumstances, corporate law defers to the board in how it directs the CEO.

Recent regulation has called that deference into question, as private ordering gives way to a new understanding of how shareholders, directors, and officers interact. New laws – in particular, the Sarbanes-Oxley Act and the Dodd-Frank Act – have begun to regulate director and officer conduct in response to the real possibility that long-term CEOs can control the board (rather than the other way around). No doubt, board-CEO relations can vary from firm to firm, raising concern over the costs of a one-size-fits-all approach to governance. Nevertheless, in weighing those costs against questions of board effectiveness, there may still be a shift in how officers are controlled – including an acceptance of regulation, such as a CEO term limit, that supplements or supersedes board oversight.

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INTRODUCTION

Undercover Boss, a CBS television series, follows CEOs and other executives as they work incognito alongside staff in their own companies. It is a show for our times: spanning the divide between America's public and its most powerful business leaders, who like Mark Twain's King Arthur¹ must learn to grapple with the most humbling of jobs.²

The series also highlights two points that are well-known to corporate law scholars. First, how well a CEO does her job is critical to how well the firm performs. Not surprisingly, the series shadows CEOs, not directors. A firm's success or failure often turns on the CEO's decisions – more so than on decisions of the board.³ Second, CEOs can lose touch with the business. A CEO can become “stale” over time,⁴ unable to adapt to a dynamic business environ-

¹ See MARK TWAIN, *A CONNECTICUT YANKEE IN KING ARTHUR'S COURT* 211-303 (Oxford Univ. Press 1997).

² Fellow employees are told the “new worker” is being filmed for a documentary. See Adam Cohen, *Unreality TV: If the Boss Only Knew, He Would Do Something*, N.Y. TIMES, Mar. 20, 2010, at A16; Susanne Craig & Randall Smith, *TV's Next “Undercover Boss” May Come From Wall Street*, WALL ST. J., Apr. 14, 2010.

³ Modern CEOs can wield enormous power over how a company is managed. See Lyman P.Q. Johnson & David Millon, *Recalling Why Corporate Officers Are Fiduciaries*, 46 WM. & MARY L. REV. 1597, 1599 (2005); see also Marianne Bertrand & Antoinette Schoar, *Managing with Style: The Effect of Managers on Firm Policies*, 118 Q. J. ECON. 1169, 1172 (2003) (finding that top managers and different management “styles” significantly affect corporate behavior and performance); Ulrike Malmendier & Geoffrey Tate, *Superstar CEOs*, 124 Q. J. ECON. 1593, 1633 (2009) (finding that increased CEO status distorts CEO behavior and decreases subsequent firm performance). A firm's CEO is often more powerful than its Chairman of the Board. See J. Richard Harrison et al., *The Changing of the Guard: Turnover and Structural Change in the Top-Management Positions*, 33 ADMIN. SCI. Q. 211, 228-30 (1988) (finding, from empirical studies, that CEOs generally possess more power than the chairman of the board and often seek to oust the Chairman to consolidate CEO power); see also John C. Coates IV & Reinier Kraakman, *CEO Tenure, Performance and Turnover in S&P 500 Companies 2* (Eur. Corp. Gov't Inst., Fin. Research Paper No. 191/2007, 2010), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=925532 (describing the structural power dynamic of modern corporations in which non-CEO board chairs are often prematurely forced out by the CEO so that the CEO can ensure her position as CEO).

⁴ See Bruce Walters et al., *CEO Tenure, Boards of Directors, and Acquisition Performance*, 60 J. BUS. RES. 331, 337 (2007) (noting that, although companies can benefit from longer CEO tenure, those benefits are outweighed by the high probability the CEO will become strategically rigid). Over time, senior managers may also grow increasingly naive about a company's operations, since important information, especially if it is negative, can be withheld by lower-level employees who fear retaliation or believe their efforts at communication will be futile. See Linda Klebe Trevino, *Out of Touch: The CEO's Role in Corporate Misbehavior*, 70 BROOK. L. REV. 1195, 1208-10 (2005).

ment.⁵ With longevity, however, she can also cultivate close ties with directors, making it difficult for the board to objectively assess her performance.⁶ Board independence can decline, in part because the decision to retain a CEO gives her leverage she can use to limit future board discretion.⁷ The result is an increase in agency costs, as CEOs use their longevity to increase control over the board, potentially benefiting personally at shareholder expense.⁸ In particular, as director tenure shortens,⁹ a longer-term CEO can

⁵ See Andrew D. Henderson et al., *How Quickly Do CEOs Become Obsolete? Industry Dynamism, CEO Tenure, and Company Performance*, 27 STRATEGIC MGMT. J. 447, 458 (2006) (contending that the obsolescence period for CEOs varies with the dynamics of the industry); Danny Miller & Ming-Jer Chen, *Sources and Consequences of Competitive Inertia: A Study of the U.S. Airline Industry*, 39 ADMIN. SCI. Q. 1, 3-4 (1994) (noting that successful CEOs can become complacent over time because they perceive fewer threats to their power and become wed to strategies and methods that produced past successes). A survey of 1,925 CEOs found that over half believed they were at their most productive three to five years after becoming CEO. Only eight percent believed it was between five and ten years, dropping to two percent after ten years in office. See Jae Yang & Adrienne Lewis, *CEOs Say They're at Their Best After Three Years*, USA TODAY, Aug. 24, 2006, available at <http://www.scribd.com/doc/28922302/USA-TODAY-Collegiate-Case-Study-Business-Leaders> (describing a Korn/Ferry International Executive survey).

⁶ See Sam Allgood & Kathleen A. Farrell, *The Effect of CEO Tenure on the Relation between Firm Performance and Turnover*, 23 J. FIN. RES. 373, 389-90 (2000) (using empirical data to demonstrate the inverse relationship between CEO tenure and turnover rate); Rick Geddes & Hrishikesh D. Vinod, *CEO Tenure, Board Composition, and Regulation*, 21 J. REG. ECON. 217, 219 (2002); see also Byoung-Hyoun Hwang & Seoyoung Kim, *It Pays To Have Friends*, 93 J. FIN. ECON. 138, 139 (2009) (finding that social ties between directors and CEOs can significantly increase CEO influence over board determinations). This is particularly true if the CEO is also Chairman of the Board. See Vidham K. Goyal & Chul W. Park, *Board Leadership Structure and CEO Turnover*, 8 J. CORP. FIN. 49, 65 (2002) (noting that a key function of the board is determining who should be CEO and that combining the CEO and Chairman positions deprives the board of independent leadership to carry out this function).

⁷ See Benjamin E. Hermalin & Michael S. Weisbach, *Endogenously Chosen Boards of Directors and Their Monitoring of the CEO*, 88 AM. ECON. REV. 96, 97 (1998); see also *infra* note 55 and accompanying text.

⁸ See Donald C. Langevoort, *Resetting the Corporate Thermostat: Lessons from the Recent Financial Scandals About Self-Deception, Deceiving Others and the Design of Internal Controls*, 93 GEO. L. J. 285, 290-92 (2004) (describing how management, including the CEO, captures the board). CEO pay, for example, increases with tenure, suggesting growing influence over the board over time. See Lucian A. Bebchuk et al., *Lucky CEOs and Lucky Directors*, 65 J. FIN. 2363, 2390-93 (2010) (suggesting that senior managers often use the grant of opportunistically timed options to control outside board members, particularly when the company lacks a majority of outside directors or has a long-tenured CEO); James W. Frederickson et al., *A Model of CEO Dismissal*, 13 ACAD. MGMT. REV., 255, 258 (1988) (noting generally that increased tenure usually affords a CEO increased power to co-opt the board); Charles W.L. Hill & Phillip Phan, *CEO Tenure as a Determinant of CEO Pay*, 34

bargain over time for a less independent and more malleable board, further reinforcing her position within the firm.¹⁰ The costs to shareholders can be substantial. An underperforming CEO can cause a substantial drop in share price and a significant loss of firm value.¹¹

The principal response has been to strengthen board oversight. Proxy contests, hostile takeovers, independent directors, concentrated share ownership, and hedge fund and other activist investors have each been identified, at one time or another, as the most effective response.¹² None has directly targeted CEOs. Instead, if board oversight improves, the presumption has been that CEO performance will also fall into place.¹³ Yet, the CEO of a

ACAD. MGMT. J. 707, 715-16 (1991).

⁹ See *infra* notes 22-23 and accompanying text.

¹⁰ See Renée B. Adams et al., *The Role of Boards of Directors in Corporate Governance: A Conceptual Framework and Survey*, 48 J. ECON. LIT. 58, 65-67 (2010) (presenting a survey of the literature on boards of directors, focusing on board actions). The growing disparity in tenure between CEOs and directors is discussed *infra* at notes 101-104 and accompanying text.

¹¹ See Lucian A. Taylor, *Why Are CEOs Rarely Fired? Evidence from Structural Estimation*, 65 J. FIN. 2051, 2078-80 (2010) (finding that CEO entrenchment makes a board less likely to dismiss a CEO even though it would maximize shareholder value). An entrenched CEO, fearing for her job, is also more likely to resist an attractive acquisition offer. See David S. North, *The Role of Managerial Incentives in Corporate Acquisitions: The 1990s Evidence*, 7 J. CORP. FIN. 125, 138, 146 (2001) (noting that the tendency of managers to resist an acquisition offer is especially noticeable when senior managers own sizeable blocks of company stock or the company has a long-tenured CEO).

¹² See Stephen M. Bainbridge, *Responses: Director Primacy and Shareholder Disempowerment*, 119 HARV. L. REV. 1735, 1741 (2006) (suggesting that the risk of managerial abuse of its power is limited by the recent increase in shareholder litigation and the widespread implementation of rules concerning director independence and other corporate governance matters); Jens Dammann, *Corporate Ostracism: Freezing Out Controlling Shareholders*, 33 J. CORP. L. 681, 689 (2008) (noting that the presence of controlling shareholders, who do not face the same collective action problem as small, isolated shareholders, subjects managers to increased scrutiny); Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 STAN. L. REV. 1465, 1520-40 (2007) (explaining that greater independence among directors resulted from a shift in primary corporate objectives to shareholder value and greater informativeness of stock market prices); Robert W. Hamilton, *Corporate Governance in America 1950-2000: Major Changes but Uncertain Benefits*, 25 J. CORP. L. 349, 353-64 (2000) (describing how several recent developments, including the rise of institutional investors and leveraged buyouts, have worked to reform American corporate governance); Marcel Kahan & Edward Rock, *Embattled CEOs*, 88 TEX. L. REV. 987, 995-1037 (2010) (chronicling the movement towards increased board independence and the beneficial effects on shareholder value).

¹³ See JONATHAN R. MACEY, CORPORATE GOVERNANCE – PROMISES KEPT, PROMISES BROKEN 52-53 (2008); see also Adams et al., *supra* note 10, at 69-74 (surveying literature

large firm – by virtue of her position as CEO – can, and often does, enhance her own authority.¹⁴ Although subject to fiduciary duties,¹⁵ she has substantial discretion within broad limits to consolidate and reinforce her position – potentially at corporate (and shareholder) expense.¹⁶ Thus, even as board scrutiny has increased¹⁷ and average CEO tenure has dropped,¹⁸ underperforming CEOs, on average, have still been able to keep their jobs: only about 2 to 2.25 percent of CEOs at large U.S. corporations are forced out each year,¹⁹ a rate that is lower than what would occur among well-functioning

on board assessment of the CEO).

¹⁴ See Jens Dammann, *How Embattled Are U.S. CEOs?*, 88 TEX. L. REV. *SEE ALSO* 201, 206-07 (2010), <http://www.texasrev.com/seealso/vol/88/responses/dammann> (using the ubiquity of poison pills during the 1980s as an example of managers' tendency to employ new devices or strategies to blunt the potential loss of CEO influence or job security); Melvin Aron Eisenberg, *The Architecture of American Corporate Law: Facilitation and Regulation*, 2 BERKELEY BUS. L.J. 167, 170-76 (2005) (noting that top managers, due to their influence and control, are more likely than ordinary agents to increase power at the principal's expense).

¹⁵ See Johnson & Millon, *supra* note 3, at 1605-11; Leo E. Strine, Jr., *Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America*, 119 HARV. L. REV. 1759, 1762 (2006).

¹⁶ See Eisenberg, *supra* note 14, at 170-71.

¹⁷ See Chuck Lucier et al., *The Era of the Inclusive Leader*, STRATEGY + BUS., Summer 2007, at 12 (explaining how increased board engagement and active shareholder involvement have combined to limit CEO discretion).

¹⁸ See Steven N. Kaplan & Bernadette Minton, *How Has CEO Turnover Changed?* 2 (Nat'l Bureau of Econ. Research, Working Paper No. W12465, Aug. 2008), available at <http://faculty.chicagobooth.edu/steven.kaplan/research/km.pdf> (finding that average CEO tenure has dropped to just under six years). Global performance-related turnover is also reportedly on the rise. See Gordon, *supra* note 12, at 1531-32. A recent Booz Allen study reports that globally, among the 2,500 largest public companies, performance-related CEO turnover in 2006 was 4.6 percent. See Lucier et al., *supra* note 17, at 4. Note, however, that the same Booz Allen study found that the average tenure of North American CEOs in 2006 was 9.8 years, the longest since 1995. See *id.* at 5.

¹⁹ See Dirk Jenter & Fadi Kanaan, *CEO Turnover and Relative Performance Evaluation* 2, 18 (Nat'l Bureau of Econ. Research, Working Paper No. 12068, 2006), available at <http://www.nber.org/papers/w12068.pdf> (providing empirical analysis of CEO turnover rates at 2,548 firms from 1993 to 2001); Kaplan & Minton, *supra* note 18, at 23. Estimating the rate of firings is difficult, since firms may not disclose the precise reason why a CEO has stepped down. See Jenter & Kanaan, *supra*, at 18; see also *infra* note 85 and accompanying text. Moreover, they may not include CEOs who choose to sell the company rather than face the risk of an unfavorable board evaluation. See Coates & Kraakman, *supra* note 3, at 16-17. Nevertheless, the projected CEO firing rate, in the absence of CEO entrenchment, is substantially greater than actual rates, even taking into account departures that mask actual terminations. See Taylor, *supra* note 11, at 2054.

boards.²⁰ CEOs, instead, often are fired only after an extended period of poor performance.²¹

In this Essay, I pose a question at the heart of CEO authority: If agency costs increase with tenure, why not require a mandatory CEO term limit? My purpose is *not* to propose a CEO term limit, but rather to ask why term limits for CEOs are out-of-bounds when they have long been advocated for others. Director term limits²² are increasingly common,²³ and public company auditors

²⁰ See Taylor, *supra* note 11, at 2053 (contending that CEO entrenchment limited the willingness of boards to fire poorly-performing CEOs even though dismissal would have maximized shareholder value). Among other reasons, directors are unlikely to terminate a CEO if doing so violates corporate norms. See Taylor, *supra* note 11 at 2052-53, 2083, 2085 (suggesting that adherence to the industry norm relates to the general distaste of many directors for firing CEOs). Director reluctance may also be due, in part, to ties with the CEO or the directors' interest in being nominated to other boards. See Hermlin & Weisbach, *supra* note 7, at 98-99. There is some indication that independent directors "behave differently" than inside directors when deciding whether or not to replace a low-quality CEO, but the incremental turnover effect is relatively small. See Sanjai Bhagat & Bernard Black, *The Uncertain Relationship Between Board Composition and Firm Performance*, 54 BUS. LAW. 921, 924-26 (1999).

²¹ See Jerold B. Warner et al., *Stock Prices and Top Management Changes*, 20 J. FIN. ECON. 461, 487-88 (1988) (noting that, even in the face of a string of poor performances, management is often absolved of factors the board deems outside of management's control); see also Jenter & Kanaan, *supra* note 19, at 36. In fact, for most CEOs, poor performance does not constitute a basis for just-cause termination. See Stewart J. Schwab & Randall S. Thomas, *An Empirical Analysis of CEO Employment Contracts: What Do Top Executives Bargain For?*, 63 WASH. & LEE L. REV. 231, 249 (2006) (finding, from an analysis of 375 CEO employment contracts, that less than four percent of CEO contracts listed incompetence as grounds for just-cause termination). More recently, some CEOs have been pushed out due to concerns over prospective performance – after boards and activist investors questioned the CEO's ability to perform well in the future. See Lucier et al., *supra* note 17, at 11.

²² Calls for director term limits have gone on for almost twenty years. See, e.g., Martin Lipton & Jay W. Lorsch, *A Modest Proposal for Improved Corporate Governance*, 48 BUS. LAW. 59, 68 (1992) (suggesting that the imposition of term limits for independent directors would ensure that a nominally independent director would not fall under senior manager influence).

²³ See USC/CENTER FOR EFFECTIVE ORG., HEIDRICK & STRUGGLES, 10TH ANNUAL CORP. BOARD EFFECTIVENESS STUDY 2006-2007, at 12 (2006), available at http://www.boardmember.com/Article_Details.aspx?id=1431 (noting that twenty-two percent of companies surveyed in 2007 had term limits for directors, more than double the number in 2000). Although Institutional Shareholder Services does not affirmatively recommend the adoption of director term limits, its general policy is to "scrutinize boards where the average tenure of all directors exceeds fifteen years for independence from management and for sufficient turnover to ensure that new perspectives are being added to the board." RISKMETRICS GROUP, 2010 U.S. PROXY VOTING GUIDELINES SUMMARY 18, 22 (2010), available at http://www.issgovernance.com/files/RMG_2010_US_SummaryGuidelines201

are required to be rotated – in effect, a term limit – every five years.²⁴ The question, sometimes raised in the popular press,²⁵ has largely escaped academics – a noticeable gap, in light of the vast amount of scholarship on CEO entrenchment.²⁶

The answer, at first glance, is fairly straightforward. U.S. corporate law strives to strike a balance between managers' discretion in running a business and their accountability to shareholders. Within that framework, CEOs are agents of the corporation, subject to control by the board, which has primary responsibility for overseeing the firm's business and affairs.²⁷ Senior officers, therefore, are largely shielded by the board from outside interference, permitting them to execute consistent, long-term business strategies without close external scrutiny. Variations in governance can be privately ordered

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²⁴ See Sarbanes-Oxley Act of 2002 § 203, 15 U.S.C. § 78j-1(j) (2006); see also Robert Charles Clark, *Corporate Governance Changes in the Wake of the Sarbanes-Oxley Act: A Morality Tale for Policymakers Too*, 22 GA. ST. U. L. REV. 251, 262-63 (2005) (providing a general description of the Sarbanes-Oxley ACT's (SOX's) requirements concerning a company's use and rotation of independent auditors).

²⁵ See, e.g., Thomas W. Harvey, *Been a CEO for Ten Years? Your Time's About Up*, BUS. INS., Apr. 16, 2007, at 11; Barbara Kellerman, *CEO Term Limits*, WASH. POST, May 26, 2009, <http://views.washingtonpost.com/leadership/panelists/2009/05/ceo-term-limits.html>; Steve Mader, *CEO Term Limits*, FORBES, Nov. 14, 2006, available at http://www.forbes.com/2006/11/14/leadership-governance-boardroom-lead-ceo-cx_bh_1114termlimits.html; Mike Myatt, *Should CEOs Have Term Limits?*, N2GROWTH.COM (Feb. 3, 2011), <http://www.n2growth.com/blog/ceo-term-limits>.

²⁶ The only academic paper of which I am aware that analyzes the question of CEO term limits is Matthias Benz & Bruno S. Frey, *Corporate Governance: What Can We Learn from Public Governance?*, 32 ACAD. MGMT. REV. 92, 97-98 (2007). Other papers have drawn parallels between CEOs and presidents, but have not considered the question of term limits. See, e.g., Richard A. Epstein, *Executive Power in Political and Corporate Contexts*, 12 U. PA. J. CONST. L. 277, 282-84 (2010) (describing similarities between the modern CEO and the U.S. President). I exclude mandatory retirement policies from my analysis of CEO term limits. Firms often consider sixty-five years to be the normal retirement age for senior executives, including the CEO – to assist in better planning CEO successions, rather than to address entrenchment. See Murali Jagannathan & Yee Cheng Loon, *Why Do CEO Retirement Policies Affect Firm Value?* 1-4 (Dec. 2010), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1536588.

²⁷ See *In re The Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 774 n.570 (Del. Ch. 2005), *aff'd* 906 A.2d 27 (Del. 2006). The principal that officers are agents of the corporation, and not agents of the board only, is well-established. See, e.g., JOSEPH K. ANGELL & SAMUEL AMES, A TREATISE ON THE LAW OF PRIVATE CORPORATIONS AGGREGATE 162-63 (1832); see also I THOMAS W. WATERMAN, A TREATISE ON THE LAW OF CORPORATIONS OTHER THAN MUNICIPAL 169-70 (1888).

among shareholders, directors, and officers, but in most circumstances, corporate law defers to the board in how it directs the CEO.²⁸

Recent regulation, however, has called that deference into question. Federal law has long regulated discrete aspects of corporate governance,²⁹ but regulating a firm's internal affairs – the relationship among its shareholders, directors, and officers – has traditionally been left to the states.³⁰ That separation is eroding. New laws, principally at the federal level,³¹ directly regulate director and officer conduct³² – moving beyond the “enabling” feature of state corporate statutes³³ to draw bright-line rules around corporate conduct that encroach on substantive areas traditionally beyond federal reach.³⁴ No doubt, part of the shift was a reaction to the corporate scandals of the late 1990s and, more recently, the financial crisis that began in 2007. However, the shift also reflects the real possibility that long-term CEOs can control the board (rather than the other way around)³⁵ – requiring a change in the standard

²⁸ See *infra* notes 37-42 and accompanying text.

²⁹ See Robert S. Karmel, *Realizing the Dream of William O. Douglas: The Securities and Exchange Commission Takes Charge of Corporate Governance*, 30 DEL. J. CORP. L. 79, 80 (2005) (noting that federal regulations concerning corporate governance usually are confined to specific issues or practices implicated by high-profile scandals).

³⁰ See Sean J. Griffith & Myron T. Steele, *On Corporate Law Federalism: Threatening the Thaumatrope*, 61 BUS. LAW. 1, 4-6 (2005); see also *infra* notes 43-51 and accompanying text.

³¹ See Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 591-92 (2003) (noting that, in the wake of the Enron and WorldCom scandals, the federal government has brought fundamental issues relating to corporate governance under federal regulation); see also Griffith & Steele, *supra* note 30, at 1-2.

³² See William B. Chandler III & Leo E. Strine, Jr., *The New Federalism of the American Corporate Governance System: Preliminary Reflections of Two Residents of One Small State*, 152 U. PA. L. REV. 953, 959, 973 (2003). Those new laws are described *infra* at notes 58-71 and accompanying text.

³³ See Bernard Black & Reinier Kraakman, *A Self-Enforcing Model of Corporate Law*, 109 HARV. L. REV. 1911, 1921 (1996) (describing state enabling laws as a series of default rules from which the parties can contractually deviate); John C. Coffee, Jr., *The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role*, 89 COLUM. L. REV. 1618, 1626-27 (1989) (highlighting the need, on the part of legislators, courts, and academics, to strike the proper balance between mandatory and enabling laws in modern corporate statutes).

³⁴ See Chandler & Strine, *supra* note 32, at 973-76; Robert B. Thompson & Hillary A. Sale, *Securities Fraud as Corporate Governance: Reflections upon Federalism*, 56 VAND. L. REV. 859, 886 (2003) (contending that SOX expressed Congress's clear intention to regulate the conduct of corporate officers as it relates to the duties of care, loyalty, and good faith).

³⁵ See Johnson & Millon, *supra* note 3, at 1613-22; see also *infra* notes 52-57 and accompanying text.

framing of the firm, as the traditional conception of how shareholders, directors, and officers interact gives way to a new understanding of that relationship.

Board-CEO relations, of course, can vary from firm to firm, raising concerns over the costs of a one-size-fits-all approach to corporate governance. A key question is whether a mandatory requirement, even if detrimental for some firms, would benefit the economy as a whole. There are important benefits to a system that permits oversight to vary based on the particular requirements of each individual firm. Yet, there is also a risk that a CEO, by virtue of her ability to influence the board, will throw off control altogether. That tension is at the heart of the recent trend in corporate governance. The new approach continues to rely generally on the board to oversee senior managers, but also reflects a shift in how officers are controlled – including a growing acceptance of regulation that supplements or supersedes traditional board oversight.³⁶

Part I describes the traditional deference that corporate law gives to the board in managing the CEO, as well as the more recent federal regulation of how directors and CEOs interact. The new approach reflects the ability of long-term CEOs to significantly influence the board and limit effective oversight. Part II then introduces – solely as a stalking horse – what a CEO term limit could look like, assesses the key strengths and weaknesses of such a limit, and considers whether evolving attitudes toward regulating corporate activity may prompt change in how CEOs are managed. This Part also raises the possibility that new regulation, such as a CEO term limit, may begin to take the place of traditional deference to the board.

I. REGULATING CEOs

A basic tenet of U.S. corporate law is that the board controls the firm.³⁷ The board oversees the firm's business and reviews its financial objectives, major plans, and auditing and accounting principles.³⁸ As companies have grown, the board has also become responsible for appointing professional managers – specialized experts who devote their time solely to running the firm and its

³⁶ See *infra* notes 118-130 and accompanying text.

³⁷ See E. Norman Veasey, *Corporate Governance and Ethics in the Post-Enron WorldCom Environment*, 38 WAKE FOREST L. REV. 839, 842 (2003) (arguing that boards should actively engage in developing and executing the company's strategic business plan); see also Strine, *supra* note 15, at 1770. Almost 150 years ago, one court concluded, “[t]he president and directors of a bank, instead of being mere servants, are really the controlling power of the corporation, – the representatives, standing and acting in the place of the interested parties. . . . The directors derive all of their power and authority from the charter and laws, and none from the stockholders.” *Goodspeed v. The E. Haddam Bank*, 22 Conn. 530, 540-41 (1853).

³⁸ See DEL. CODE ANN. tit. 8, § 141(a) (2010); AMERICAN LAW INSTITUTE, PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 3.02 (1994).

business.³⁹ Thus, in addition to performing other high-level duties, the board selects, compensates, reviews, and where appropriate, replaces senior executives,⁴⁰ delegating to the CEO and others, as fiduciaries, the authority to act on the company's behalf.⁴¹ Many directors limit their involvement in the business to advising senior managers, directly managing only in times of crisis or during significant developments affecting the company and its affairs, but otherwise leaving day-to-day decisions to the CEO and her team.⁴²

Interfering with the director-officer relationship can be costly to firms and shareholders. It can dilute the benefits of centralized management⁴³ and discourage innovation, entrepreneurship, and beneficial risk-taking.⁴⁴ Interference can also compromise the ability of shareholders, directors, and officers to privately order their own affairs, which they typically do through the firm's charter and by-laws and by contract,⁴⁵ thus potentially imposing a less-efficient, less-flexible, one-size-fits-all model of corporate governance on

³⁹ See Margaret M. Blair, *Locking in Capital: What Corporate Law Achieved for Business Organizers in the Nineteenth Century*, 51 UCLA L. REV. 387, 393-94 (2003) (contending that separating legal and equitable interests was crucial in bringing together skilled managers and establishing long-term relationships between the company and its suppliers and customers); Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 J.L. & ECON. 301, 301-09 (1983) (noting that vesting the power to make corporate decisions in some group other than the residual risk claimants permits a degree of specialization that is ultimately beneficial). Alfred Chandler described the contribution of managerial hierarchies to the rapid U.S. business expansion of the mid-1800s in ALFRED D. CHANDLER, JR., *THE VISIBLE HAND: THE MANAGERIAL REVOLUTION IN AMERICAN BUSINESS* 6-8 (1977).

⁴⁰ See AMERICAN LAW INSTITUTE, *supra* note 38, at § 3.01.

⁴¹ See *id.* § 3.01; see also Johnson & Millon, *supra* note 3, at 1601-02, 1605-08. As Joseph Angell and Samuel Ames described in the first comprehensive U.S. treatise on corporate law: "The power of electing both officers and members . . . [is] incident . . . to every corporation," a power that was naturally vested in the shareholders, but "could be taken from the body at large, and reposed in a body or directors, or any other select body." See ANGELL & AMES, *supra* note 27, at 63; see also CHARLES T. BOONE, *A MANUAL OF THE LAW APPLICABLE TO CORPORATIONS* 184-85 (1882).

⁴² See MYLES L. MACE, *DIRECTORS: MYTH AND REALITY* 38-40 (1971); MACEY, *supra* note 13, at 53-54.

⁴³ See Bainbridge, *supra* note 12, at 1745-46.

⁴⁴ See Troy A. Paredes, *A Systems Approach to Corporate Governance Reform: Why Importing U.S. Corporate Law Isn't the Answer*, 45 WM. & MARY L. REV. 1055, 1101-02 (2004).

⁴⁵ See *id.* at 1077-78; see also David F. Larcker et al., *The Market Reaction to Corporate Governance Regulation 1* (Rock Ctr. for Corp. Gov't at Stanford Univ., Working Paper Series No. 82, Oct. 14, 2010) (forthcoming J. FIN. ECON.), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1650333.

organizations with vastly different needs and characteristics.⁴⁶ In light of the potential drawbacks, corporate law has provided little affirmative direction as to what officers must do. Instead, it has shielded them from direct shareholder influence,⁴⁷ invested in them a great deal of discretion,⁴⁸ and deferred to the board, as the firm's plenary authority, in overseeing their conduct.⁴⁹ The board, consequently, has two principal functions – to oversee the firm's affairs, and perhaps more importantly, to monitor senior managers and remove poor performers.⁵⁰ If shareholders are unhappy with the outcome, the remedy is to vote out the board or simply sell their stock.⁵¹

The foregoing presumes that boards monitor and control the CEO. In fact, the opposite has often been more accurate, with CEOs exercising significant control over the board and its decision-making process.⁵² For example, until recently, CEOs strongly influenced – if not controlled – board composition, often causing directors to feel a keen sense of loyalty toward senior managers.⁵³ The rapid rise in CEO pay over the past thirty years can also be explained, in part, by the CEO's influence over the board.⁵⁴ In some cases,

⁴⁶ See Martin Lipton & William Savitt, *The Many Myths of Lucian Bebchuk*, 93 VA. L. REV. 733, 748-49 (2007) (contending that overly stringent corporate governance regulation threatens to antagonize the relationship between the board and management and limits the board's ability to effectively monitor senior managers); see also Chandler & Strine, *supra* note 32, at 978-81; Strine, *supra* note 15, at 1763.

⁴⁷ See Bainbridge, *supra* note 12, at 1735 (contending that the modern corporation is partially defined by the decision to limit the power and influence of shareholders and instead choosing to grant primacy to the board); Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 844-46, 848 (2005) (suggesting that the extent to which U.S. corporate law limits the shareholders' ability to manage or intervene in corporate affairs distinguishes it from the corporate law of most other developed countries).

⁴⁸ See Strine, *supra* note 15, at 1762.

⁴⁹ See MACEY, *supra* note 13, at 51-52; Thompson & Sale, *supra* note 34, at 886. So ingrained is the director-officer relationship, U.S. courts have found for at least 150 years that any attempt by an outsider to remove an officer would be "an improper exercise of . . . authority. The officers . . . [are] the private agents of the company [R]emoval . . . is a right which belongs to the corporation alone." Neall v. Hill et al., 16 Cal. 145, 149 (1860).

⁵⁰ See MACEY, *supra* note 13, at 53-55.

⁵¹ See *In re The Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 698 (Del. Ch. 2005), *aff'd* 906 A.2d 27 (Del. 2006) ("The redress for failures that arise from faithful management must come from the markets, through the action of shareholders and the free flow of capital, and not from this Court."); Bainbridge, *supra* note 12, at 1749-51; Strine, *supra* note 15, at 1764; see also *supra* notes 6-10 and accompanying text.

⁵² See MACEY, *supra* note 42, at 72-85, 190-94; Johnson & Millon, *supra* note 3, at 1613-20 (describing de facto officer control of the corporation).

⁵³ See Gordon, *supra* note 12, at 1496.

⁵⁴ See Bebchuk et al., *supra* note 6, at 2390-93; Lawton W. Hawkins, *Compensation Representatives: A Prudent Solution to Excessive CEO Pay*, 72 BROOKLYN L. REV. 449,

directors were also “captured” by the CEOs they selected – associating with a CEO’s decisions, feeling responsible for the results and, consequently, becoming less willing to remove her.⁵⁵ Board control eroded as directors deferred to CEOs in setting objectives, strategies, and policies.⁵⁶ That decline in control, in turn, hampered the board’s ability to monitor the CEO on behalf of shareholders.⁵⁷

Corporate scandals in the 1990s and, more recently, the financial crisis that began in 2007 prompted a federal regulatory response. Much of the new regulation bypasses corporate law’s traditional deference to the board and instead – by requiring managers to undertake certain tasks and, in some cases, certify their compliance – manages important aspects of how directors and officers interact.⁵⁸

First, new regulation has enhanced the role of independent directors.⁵⁹ The Sarbanes-Oxley Act of 2002 (SOX) requires a public company to establish an audit committee comprised of independent directors,⁶⁰ as do New York Stock Exchange (NYSE) and NASDAQ Stock Market (NASDAQ) regulations.⁶¹

453-54 (2007); Kahan & Rock, *supra* note 12, at 1036-37; Carola Frydman & Dirk Jenter, *CEO Compensation 1* (Rock Ctr. for Corp. Gov’t at Stanford Univ., Working Paper Series No. 77, Nov. 2010), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1582232 (surveying recent literature on CEO compensation and finding managerial power and market competition to be important, but not exclusive, determinants).

⁵⁵ See MACEY, *supra* note 12, at 58-61; Langevoort, *supra* note 6, at 294-95.

⁵⁶ See MACEY, *supra* note 42, at 41-42. In addition, board decisions are typically based on company-prepared data, which a CEO can color in favor of the projects she supports. See Renée B. Adams & Daniel Ferreira, *A Theory of Friendly Boards*, 62 J. FIN. 217, 217-19 (2007) (noting that a CEO has an incentive to withhold information from the board because the more that is provided, the greater the probability of board intervention in the decision-making process).

⁵⁷ See MACEY, *supra* note 13, at 57; William H. Donaldson, Chairman, Sec. & Exch. Comm’n, Remarks at the 2003 Washington Economic Policy Conference, National Association for Business Economics (Mar. 24, 2003), available at <http://www.sec.gov/news/speech/spch032403 whd.htm>.

⁵⁸ See Chandler & Strine, *supra* note 32, at 979-80.

⁵⁹ See Gordon, *supra* note 12, at 1482-83, 1538-40 (noting that the increased emphasis on director independence not only relates to board composition but also more rigorous standards of independence).

⁶⁰ See Sarbanes-Oxley Act of 2002 § 301, 15 U.S.C. § 78j-1 (2006).

⁶¹ See NASDAQ, Inc., Stock Market (NASDAQ) Rule 5605(c)(2)(A) (2009); NYSE, Inc., Listed Company Manual (NYSE Manual) § 303A.07(b) (2004). The definitions of “independence” vary between NASDAQ and NYSE. Compare NASDAQ Rule 5605(b)(1) with NYSE Manual § 303A.01-.02. NYSE also requires each listed firm to create independent compensation and nominating committees, see NYSE Manual § 303A.04-.05, and NASDAQ requires a nominating or compensation committee, if one is formed, to consist entirely of independent directors, see NASDAQ Rule 5605(d)-(e).

Both NYSE and NASDAQ further require a majority of directors to be independent⁶² and independent directors to regularly conduct their own separate meetings.⁶³ In addition, prompted by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank),⁶⁴ the Securities and Exchange Commission (SEC) adopted new Rule 14a-11,⁶⁵ requiring public companies to include in their proxy materials the director nominees of qualified shareholders for up to twenty-five percent of the board.⁶⁶

Second, new regulation has shaped CEO incentives by mandating new compensation arrangements.⁶⁷ SEC disclosure requirements rely on public scrutiny to compel firms to develop pay practices that link compensation to long-term performance.⁶⁸ In addition, Dodd-Frank requires each public firm to

⁶² See NASDAQ Rules 5605(a)(2), 5605(b)(1); NYSE Manual § 303A.01.

⁶³ See NASDAQ Rule 5605(b)(2); NYSE Manual § 303A.03.

⁶⁴ See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 971, 124 Stat. 1376, 1915 (2010) (to be codified at 15 U.S.C. § 78n).

⁶⁵ Implementation of new Rule 14a-11 has been stayed pending the outcome of litigation that has challenged its adoption. See Order Granting Stay of Commission's Facilitating Shareholder Director Nominations Rules, SEC Release No. 9149 (Oct. 4, 2010), available at <http://www.sec.gov/rules/other/2010/33-9149.pdf>.

⁶⁶ See Facilitating Shareholder Director Nominations, 75 Fed. Reg. 56,668 (proposed Sept. 16, 2010) (to be codified at 17 C.F.R. pts. 200, 232, 240, 249).

⁶⁷ Congress earlier turned to the tax code to influence executive pay practices, but with only limited success. See David I. Walker, *The Challenge of Improving the Long-Term Focus of Executive Pay*, 51 B.C. L. REV. 435, 451-53 (2010). The Internal Revenue Code limits the tax deductibility of non-performance-based pay to senior executives to \$1 million annually. I.R.C. § 162(m) (West Supp. 2010). It also restricts corporate tax deductions for excessive payments under a "golden parachute" executive severance package, as well as imposes excise taxes on the recipients. See *id.* § 280G; I.R.C. § 4999 (2006).

⁶⁸ See Executive Compensation and Related Person Disclosure, 71 Fed. Reg. 53,158, 53,160 (Sept. 8, 2006) (to be codified in scattered sections of 17 C.F.R.). The firm's proxy statement must also include a detailed narrative of the objectives and design of its compensation program, including how compensation is determined. In addition, it must include a summary compensation table that sets out a dollar value for each item, as well as total compensation for each of the firm's five senior executives. See 17 C.F.R. § 229.402 (2009). Dodd-Frank also directs the SEC to adopt rules that require each public firm to disclose the relationship between its executives' compensation and the firm's financial performance. See Dodd-Frank § 953(a), 124 Stat. at 1903-04 (to be codified at 15 U.S.C. § 78n). Public firms, in addition, must disclose the median of annual total compensation of all employees (other than the CEO), the annual total compensation of the CEO, and the ratio of those two amounts. See *id.* § 953(b), 124 Stat. at 1903-04 (to be codified at 15 U.S.C. § 78l). Dodd-Frank also directs stock exchanges to require listed companies to create independent compensation committees to assess the firm's compensation consultants and other committee advisers. See *id.* § 952(a), 124 Stat. at 1900-01 (to be codified at 15 U.S.C. § 78j-3).

hold a periodic non-binding shareholder vote (“say-on-pay”) on the compensation paid to top executives.⁶⁹

Third, new regulation has defined portions of the CEO’s job, rather than leaving such decisions to the firm’s discretion. Pursuant to SOX, CEOs must now supervise, assess, and certify the firm’s internal controls, irrespective of what their earlier responsibilities might have been.⁷⁰ SOX and Dodd-Frank also modify executive employment contracts. Listed firms must implement policies that claw back incentive-based executive pay if erroneous reporting occurs that requires the issuer to restate its financial statements.⁷¹

The result has been a shift in corporate governance – from a deference that “does not lightly deprive the stockholders’ chosen representatives of managerial authority”⁷² to a new set of rules that “prescribe the precise means by which directors and officers are to pursue certain ends.”⁷³ Changes in regulation are likely to persist.⁷⁴ Although the shift is too recent to be strongly predictive, future proposals may include separating the CEO and Chairman of the Board positions⁷⁵ and implementing a range of CEO pay requirements that

⁶⁹ Companies must also provide for a shareholder vote no less frequently than every six years on a separate resolution to determine whether the say-on-pay vote will take place every one, two, or three years. *See* Dodd-Frank § 951, 124 Stat. at 1899-1900 (to be codified at 15 U.S.C. § 78n-1). In addition, as part of any vote to approve a merger, acquisition, or other strategic transaction, the firm must disclose and hold a non-binding shareholder vote on transaction-related compensation that senior executives will receive (a “golden parachute”). *See id.* The SEC has adopted final “say-on-pay” rules in accordance with Dodd-Frank’s requirements. *See* Shareholder Approval of Executive Compensation and Golden Parachute Compensation, 76 Fed. Reg. 6010 (Feb. 2, 2011) (to be codified at 17 C.F.R. pts. 229, 240, 249).

⁷⁰ Sarbanes-Oxley Act of 2002 §§ 302, 404, 15 U.S.C. §§ 7241, 7262 (2006).

⁷¹ 15 U.S.C. § 7241; Dodd-Frank § 954, 124 Stat. at 1904 (to be codified at 15 U.S.C. § 78j-4).

⁷² Chandler & Strine, *supra* note 32, at 979.

⁷³ *Id.*

⁷⁴ *See* Kahan & Rock, *supra* note 12, at 1041-42 (noting that, even when a company retains the ability to roll-back recent voluntary reforms, it is unlikely to do so due to a desire not to antagonize shareholders).

⁷⁵ *See* COMMISSION ON PUBLIC TRUST AND PRIVATE ENTERPRISE, THE CONFERENCE BOARD, FINDINGS AND RECOMMENDATIONS – PART 2: CORPORATE GOVERNANCE 21 (Jan. 9, 2003), available at <http://www.ecgi.org/codes/documents/757.pdf>. Globally, non-Chairman CEOs have an average tenure of 5.6 years, whereas the tenure is 10.3 years when the positions are combined. *See* Lucier et al., *supra* note 17, at 48. The percentage of companies splitting the CEO and Chairman positions has increased significantly. According to a Spencer Stuart survey, forty percent of S&P 500 companies had a separate Chairman and CEO in 2010, up from twenty-three percent in 2000. *See* SPENCERSTUART, 2010 SPENCER STUART BOARD INDEX 20 (25th ed. 2010), available at <http://www.spencerstuart.com/articleview-zmags.aspx?id=85b7e8fc>; *see also* Kahan &

mandate certain types of compensation, perhaps tied to restricted stock.⁷⁶ Regardless of outcome, however, what is apparent is that the traditional deference to the board has begun to wear away. The willingness, through new federal standards, to directly regulate director-CEO relations suggests that change is more likely today than in the past.

II. CEO TERM LIMITS

CEOs typically possess significant discretion in performing their jobs. That discretion can be used to enhance their authority, potentially at shareholder expense.⁷⁷ Recent history suggests that many have done just that.⁷⁸ A mandatory term limit would help level the playing field; CEOs could no longer be assured of holding a special franchise. It could, however, also inject a costly requirement into the traditional director-officer relationship. To help illustrate the potential benefits and drawbacks, a basic term limit proposal is sketched out below:

- Firms whose shares trade publicly on a national securities exchange would be required to introduce a CEO term limit. Doing so would be consistent with the use of listing requirements to set independence standards for listed company boards.⁷⁹ States considering a CEO term limit would face a collective action problem, as those choosing to impose a requirement would potentially lose corporations, and their income, to states choosing not to do so.⁸⁰ By targeting listed firms, the new

Rock, *supra* note 12, at 1030.

⁷⁶ See Walker, *supra* note 67, at 455-56 (outlining different proposals, put forward by the U.S. Treasury Department, judges, academics, and practitioners, that would require some minimum percentage of an executive's compensation to be paid in restricted stock). More recently, executive compensation proposals have also focused on the role of inside debt on corporate managers. See Frederick Tung & Xue Wang, *Bank CEOs, Inside Debt Compensation, and the Global Financial Crisis* 3-5 (Emory Pub. Law Research, Paper No. 10-98, Mar. 13, 2010), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1570161.

⁷⁷ See *supra* notes 15-16 and accompanying text.

⁷⁸ See *supra* notes 52-57 and accompanying text.

⁷⁹ NYSE, for example, requires most boards to consist of a majority of independent directors, as well as requiring them to establish audit, nominating, and compensation committees consisting entirely of independent directors. See Kahan & Rock, *supra* note 12, at 1022-23.

⁸⁰ The agency divide between shareholders and managers may result in sub-optimal levels of regulation among the states. Managers may choose a regime that does not adequately protect shareholder interests. See Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359, 2369 (1998) (excluding broker-dealer regulation from a proposed competitive state-level regime in light of agency problems between owners and customers). A similar point about individual firms that may

requirement would also focus on companies with the most dispersed shareholders and, therefore, those most likely to have the greatest agency costs.⁸¹

- The CEO would be selected by the board, remain subject to continuing board oversight, and be removable by the board at any time during her term in office. Generally, directors are better able than shareholders to assess a CEO's performance and the actual causes of any (rise or) decline in firm value.⁸² A board is also more likely than any individual shareholder to take account of the interests of shareholders as a whole in making business-related decisions.⁸³
- Upon being selected, the CEO would remain in office for a specified period of time, to be determined by the board, but no greater than the time period permitted by the listing requirement. The outer limit could be set at six years, consistent with the current average CEO tenure.⁸⁴ A six-year limit is also in line with a recent study indicating that many CEOs who "retire" during their first six years in office have, in fact, been fired.⁸⁵

choose to adopt a CEO term limit is discussed *infra* at note 122 and accompanying text.

⁸¹ See Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 309, 344-45 (1976).

⁸² Shareholders often lack sufficient information on which to make informed decisions, such as separating firm performance from industry and market effects. Consequently, firms tend to rely on authority-based decision-making structures in lieu of direct shareholder oversight. See KENNETH J. ARROW, *THE LIMITS OF ORGANIZATION* 68-70 (1974). Note, however, that CEOs – in particular, underperforming CEOs – are more likely than before to be removed following poor firm performance, even when firms in the same industry have also declined, suggesting that a board's assessment of CEO performance may not completely filter out the influence of industry and market shocks. See Jenter & Kanaan, *supra* note 19, at 1, 5, 33-34 tbl.8.

⁸³ See Lynn A. Stout, *The Mythical Benefits of Shareholder Control*, 93 VA. L. REV. 789, 792-98 (2007); Ray Fisman et al., *Governance and CEO Turnover: Do Something or Do the Right Thing?* 3-5 (Harvard Bus. Sch., Working Paper No. 05-066, 2005), available at <http://www.hbs.edu/research/pdf/05-066.pdf>.

⁸⁴ See Kaplan & Minton, *supra* note 18, at 2. A six-year limit would also be generally consistent with CEO estimates of their own effectiveness. See Yang & Lewis, *supra* note 5. Note, however, that a recent Booz Allen study found that the average tenure of North American CEOs in 2006 was 9.8 years, the longest since 1995. See Lucier et al., *supra* note 17, at 5.

⁸⁵ See Coates & Kraakman, *supra* note 3, at 16-17, 25-26 (extrapolating, from empirical data, that many CEOs, especially those in their fourth or fifth year as CEO, will choose to voluntarily resign or sell the company rather than face a formal dismissal by the board). For a discussion of whether founder CEOs should be treated differently, see *infra* note 118.

The analysis of a CEO term limit is informed, in part, by the U.S. debate over term limits for public officials.⁸⁶ There are, of course, significant differences between CEOs and politicians, and so one must tread carefully in analogizing the two.⁸⁷ Yet, to the extent a CEO term limit addresses similar concerns – potential entrenchment and abuse of power – the scholarship on public term limits may be helpful.⁸⁸

Beginning with Thomas Jefferson, proponents have favored term limits to keep public officials in check, limit the risk of tyranny, and ensure the continued vitality of the chief executive.⁸⁹ Any resulting loss of power, they have argued, is likely to be offset by other perks of the job, so it would continue to attract the best candidates.⁹⁰ Those arguments have parallels in the corporate world. A term limit would directly address problems of CEO tenure by periodically introducing a new CEO with a fresh perspective on the job.⁹¹

⁸⁶ See James Fanto, *Whistleblowing and the Public Director: Countering Corporate Inner Circles*, 83 OR. L. REV. 435, 513 n.239 (2004).

⁸⁷ See M. Todd Henderson, *The Nanny Corporation*, 76 U. CHI. L. REV. 1517, 1556-57 (2009) (noting that CEOs are subject to a more constant evaluation, through changes in a firm's market price, compared to politicians who are elected at fixed intervals); Strine, *supra* note 15, at 1763-64 (noting that the most salient difference is that citizens cannot diversify away the risks of poor or incompetent politicians, but investors can diversify the risk that company management will adopt sub-optimal business strategies by investing in multiple companies).

⁸⁸ See Tamar Frankel, *Fiduciary Law*, 71 CALIF. L. REV. 795, 807 (1983) (noting that courts, in considering the scope and character of fiduciary law, have analogized fiduciary relations with other functionally similar relationships – such as that between union officials and union members). Arguments for and against director term limits may also be relevant, although there are important differences between a director's role and a CEO's. See *supra* notes 37-42 and accompanying text.

⁸⁹ See BERNARD BAILY, *THE IDEOLOGICAL ORIGINS OF THE AMERICAN REVOLUTION* 171-72 (1967) (discussing the potential for tyranny in viewing representatives as “independent of the people” and arguing that representation should shift with the composition of the population); GORDON S. WOOD, *THE RADICALISM OF THE AMERICAN REVOLUTION* 243-46 (1992); see also *THE FEDERALIST* No. 57, at 310-11, No. 62, at 333 (James Madison) (J.R. Pole ed., 2005); JOHN PHILLIP REID, *THE CONCEPT OF REPRESENTATION IN THE AGE OF THE AMERICAN REVOLUTION* 28-30 (1989); Thomas Jefferson, Letter to the Vermont Legislature (Dec. 10, 1807), in *THE EVOLVING PRESIDENCY* 76-77 (Michael Nelson ed., 3d ed. 2008). More recently, term limit proponents have argued that long-serving legislators, assured of being re-elected, can become captured by special interests rather than represent the populace at large. See Linda Cohen & Matthew Spitzer, *Term Limits*, 80 GEO. L.J. 477, 479-81 (1992); Steven F. Huefner, *Term Limits in State Legislative Elections: Less Value for More Money?*, 79 IND. L.J. 427, 434 (2004).

⁹⁰ See Elizabeth Garrett, *Term Limitations and the Myth of the Citizen Legislator*, 81 CORNELL L. REV. 623, 626 (1996).

⁹¹ A similar argument has been made in favor of director term limits. See Charles M. Elson & Christopher J. Gyves, *The Enron Failure and Corporate Governance Reform*, 38

More frequent CEO turnover is associated with a significantly higher level of innovation.⁹² In addition, new CEOs can “clean house,”⁹³ restructuring a lower-performing company⁹⁴ and writing down⁹⁵ and selling poorly-performing operations.⁹⁶ Knowing she will step down, a CEO is also less likely to hold a proprietary interest in her office.⁹⁷ Directors, instead, would periodically consider new CEO candidates, both within and outside of the firm,

WAKE FOREST L. REV. 855, 882 (2003) (describing institutional investors’ rationale for director term limits).

⁹² See Frederick L. Bereskin & Po-Hsuan Hsu, *New Dogs New Tricks: CEO Turnover, CEO-Related Factors, and Innovation Performance*, EUR. FIN. MGMT. (forthcoming 2011) (manuscript at 3), available at <http://efmaefm.org/0EFMSYMPOSIUM/Toronto-2011/papers/bereskin.pdf> (finding, from an empirical analysis of CEO turnover data, that innovation – as defined by a company’s patent counts and patent citations – increased over a three-to-five-year period following a change in CEO).

⁹³ Although evidence is mixed on the impact of inside and outside successors, the consensus is that forced CEO turnover improves corporate performance. Compare Rakesh Khurana & Nitin Nohria, *The Performance Consequences of CEO Turnover* 23-26 (Working Paper, 2000), available at <http://ssrn.com/abstract=219129> (reporting that the forced departure of a CEO with an outside successor improves company performance, whereas an inside successor has no effect), with Wei Shen & Albert A. Cannella, Jr., *Revisiting the Performance Consequences of CEO Succession: The Impacts of Successor Type, Postsuccession Senior Executive Turnover, and Departing CEO Tenure*, 45 ACAD. MGMT. J. 717, 728-29 (2002) (finding that forced senior executive turnover improves firm performance when successors are insiders, but is detrimental in cases of outside succession).

⁹⁴ See David J. Denis & Diane K. Denis, *Performance Changes Following Top Management Dismissals*, 50 J. FIN. 1029, 1030 (1995).

⁹⁵ See Kevin J. Murphy & Jerold L. Zimmerman, *Financial Performance Surrounding CEO Turnover*, 16 J. ACCT. ECON. 273, 312 (1993); John S. Strong & John R. Meyer, *Asset Writedowns: Managerial Incentives and Security Returns*, 42 J. FIN. 643, 659 (1987) (noting that the most important determinant of a firm’s decision to announce a writedown is whether it has recently changed senior management). The writedown of assets, and reduction in income, may be driven by a new CEO’s interest in reducing reported results during her first year, followed by an increase in earnings in the subsequent year. See Strong & Meyer, *supra*, at 644; see also Susan Pourciau, *Earnings Management and Nonroutine Executive Changes*, 16 J. ACCT. & ECON. 317, 334 (1993).

⁹⁶ See Michael S. Weibach, *CEO Turnover and the Firm’s Investment Decisions*, 37 J. FIN. ECON. 159, 186 (1995) (noting that CEO turnover often results in divestitures of poorly performing assets in an attempt to reverse managerially-motivated acquisitions).

⁹⁷ See Tamar Frankel, *Fiduciary Duties as Default Rules*, 74 OR. L. REV. 1209, 1271-75 (1995) (noting that property rights in management positions are problematic because they incentivize managers to act contrary to shareholder interests). In addition, a mandatory term limit would override any contractual assurances of continued employment a CEO could negotiate with the board. See Schwab & Thomas, *supra* note 21, at 246-47 (describing the tendency of CEOs to contract around at-will termination clauses in employment contracts through the use of definite-term employment agreements).

creating a deep bench of potential successors. Among those interested in a public firm,⁹⁸ the pay, power, and prestige of being CEO would still be likely to attract the best candidates.⁹⁹ The resulting benefits to shareholders would be tangible: stock prices typically run up after the announcement of a new CEO, so long as the transition is anticipated, orderly, and fully disclosed to the firm's investors.¹⁰⁰

Some have argued that public term limits weaken the President's power relative to Congress. The President is subject to term limits – thus facing a “lame duck” problem toward the end of her second term – while members of Congress are not.¹⁰¹ Interestingly, in the corporate context, this concern may provide another argument in *favor* of a CEO term limit. As director term limits become more common,¹⁰² there is a growing likelihood that CEO tenure will lengthen relative to the board's – the mirror image of the President and Congress. Evidence suggests that an increase in relative tenure corresponds to greater influence.¹⁰³ A CEO's compensation, for example, is significantly higher if the CEO was appointed before the chair of the board's compensation committee.¹⁰⁴ Thus, the need for a CEO term limit could be driven, in part, by an increasing reliance on director term limits. Over time, as board tenures

⁹⁸ CEO candidates may choose to work in private firms and so avoid the risk of a short-term tenure. A similar interest in positions at firms that were taken private arose following the passage of SOX. See Emily Thornton, *Going Private: Hotshot Managers Are Fleeing Public Companies for the Money, Freedom and Glamour of Private Equity*, BUS. WK., Feb. 27, 2006, at 52.

⁹⁹ See Langevoort, *supra* note 6, at 297. Successful CEO candidates are also more likely to believe they will do an exceptional job, and therefore, as described more fully in the additional condition relating to term extensions set forth below, *see infra* notes 105-111 and accompanying text, expect to continue on as CEO even after the initial six-year period has ended. See Langevoort, *supra* note 6, at 299-302.

¹⁰⁰ See Randolph P. Beatty & Edward J. Zajac, *CEO Change and Firm Performance in Large Corporations: Succession Effects and Manager Effects*, 8 STRATEGIC MGMT. J. 305, 313, 316 (1987); *see also* Lucier et al., *supra* note 17, at 48-49. Note, however, that there has been little empirical support for a relationship between director term limits and a firm's financial performance or risk. See Paul Rose, *The Corporate Governance Industry*, 32 J. CORP. L. 887, 902 (2007) (describing a report, issued by Institutional Shareholder Services in November 2006, in which it concluded there was no link between a company's policies regarding director term limits or a mandatory retirement age and performance).

¹⁰¹ See, e.g., William P. Marshall, *Eleven Reasons Why Presidential Power Inevitably Expands and Why It Matters*, 88 B.U. L. REV. 505, 520 (2008).

¹⁰² See *supra* note 23 and accompanying text.

¹⁰³ See *supra* notes 6-10 and accompanying text.

¹⁰⁴ See Brian G.M. Main et al., *The CEO, the Board of Directors and Executive Compensation: Economic and Psychological Perspectives*, 4 INDUS. & CORP. CHANGE 293, 323 (1995). Moreover, longer-term CEOs can influence director selection, creating a strong sense of loyalty to the CEO. See *supra* note 53 and accompanying text.

continue to decline, directors may be placed at a disadvantage relative to longer-tenured CEOs.

The arguments against public term limits were first framed by Alexander Hamilton. A mandatory term limit, in Hamilton's view, would force needless change in leadership. The public would also lose the benefits of the most experienced leaders.¹⁰⁵ Those concerns apply equally to a mandatory CEO requirement. To address them, a proposal could include the following additional provision:

- Upon completion of her six-year term, the board could elect to nominate the CEO for an additional term in office. That term would be shorter than the original six years – perhaps three years – and CEOs would again be eligible for re-election at the end of each successive period. For her to remain as CEO, she would need the affirmative vote of fifty percent of the outstanding shares. A retiring CEO would not be barred from becoming a CEO or director of another company.

Requiring shareholder approval would be consistent with the trend toward greater shareholder influence over corporate managers¹⁰⁶ – evidenced, in part,

¹⁰⁵ See THE FEDERALIST NO. 72, at 388-89 (Alexander Hamilton) (J.R. Pole ed., 2005). A similar argument has been made in connection with director term limits. See Clark, *supra* note 24, at 274-75.

¹⁰⁶ See Kahan & Rock, *supra* note 12, at 1039 (discussing how institutional investors and hedge funds have made it more difficult for CEOs to insulate the corporate agenda from investor influence). There is a possibility, under this arrangement, that large shareholders could begin to dominate the day-to-day management of the firm. In France, for example, for a majority of firms, shareholders can revoke the appointment of the board of directors (conseil d'administration) at any time. See Klaus J. Hopt, *Comparative Corporate Governance: The State of the Art and International Regulation*, 59 AM. J. COMP. L. 1, 22, 32 n.181 (2011). In addition, the shareholders can remove the président directeur général (PDG), who is also conseil president, acts as the CEO, and traditionally has decided who else will be on the board. See Brian R. Cheffins & Bernard S. Black, *Outside Director Liability Across Countries*, 84 TEX. L. REV. 1385, 1452 (2006). Large shareholders, therefore, can control how the firm is managed, either directly through control of the PBG and the board or indirectly by threatening to remove the firm's senior managers. See Martin Gelter, *The Dark Side of Shareholder Influence: Managerial Autonomy and Stakeholder Orientation in Comparative Corporate Governance*, 50 HARV. INT'L L.J. 129, 156-58 (2009) [hereinafter Gelter, *Dark Side*]. The German system, by contrast, is intended to insulate managers from direct shareholder oversight. Under a two-tier structure, the management board is controlled by a supervisory board, which can only terminate a management board member for cause and with a vote of no-confidence by the shareholders. Supervisory board members, in turn, are selected by the shareholders, but can only be terminated with a three-quarters vote. Managers, therefore, are insulated from shareholder control, although large shareholders are still able to influence how the firm is managed. See Martin Gelter, *Tilting the Balance Between Capital and Labor? The Effects of Regulatory Arbitrage in European Corporate Law on Employees*, 33 FORDHAM INT'L L.J. 792, 835-38

by the new proxy access rule¹⁰⁷ and “say-on-pay” voting requirement.¹⁰⁸ Directors would continue to have primary control over the CEO through their ability to terminate her or not extend her term. By requiring shareholder approval, however, the board’s decision would more likely accord with shareholder interests than if made by the board alone.¹⁰⁹ A majority voting requirement would give shareholders an inexpensive means to remove the CEO – by simply withholding their votes so that the majority requirement is unmet.¹¹⁰ The rise of institutional shareholder activists and the prominence of proxy advisory firms would also act as a check against CEO dominance of the re-election process.¹¹¹

(2010). No doubt, a CEO term limit would permit greater direct oversight by controlling shareholders. Under this Essay’s proposal, shareholders could vote on whether or not to extend a CEO’s term. The board, however, would also continue to oversee senior managers and retain the right, on its own, to terminate the CEO. Consequently, while greater shareholder control of the CEO would be possible, the board would remain actively involved in overseeing CEO performance. Moreover, concentrated share ownership is less a characteristic of the United States than of Western European countries like France and Germany, *see* Ronald J. Gilson, *Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy*, 119 HARV. L. REV. 1641, 1645-50 (2006), suggesting less of a controlling influence by shareholders over U.S. corporate management than in those countries, *see* Gelter, *Dark Side*, *supra*, at 176.

¹⁰⁷ *See supra* notes 65-66 and accompanying text.

¹⁰⁸ *See supra* note 69 and accompanying text.

¹⁰⁹ *See* Bebchuk, *supra* note 47, at 869-70.

¹¹⁰ *See* Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 VA. L. REV. 675, 703 (2007) (discussing the practice of withholding votes in director elections and its equivalence to voting against a candidate); Kahan & Rock, *supra* note 12, at 1020-21. Individual shareholders are unlikely to gather information if the cost of doing so outweighs the benefits. *See* Bainbridge, *supra* note 12, at 1745-46 (explaining why a rational shareholder often lacks incentives to gather the information necessary to participate in corporate matters in an informed manner). Shareholders, however, could gather information about a CEO’s performance at relatively low cost, based on her prior six-year track record, and rely on that information in casting their votes.

¹¹¹ *See* Stephen Choi et al., *The Power of Proxy Advisors: Myth or Reality?*, 59 EMORY L.J. 869, 905-06 (2010) (discussing the significance of voting recommendations issued by proxy advisory services); Kahan & Rock, *supra* note 12, at 995-1007. It is also possible that greater shareholder oversight will have little direct effect on CEO selection. In the United Kingdom, directors who are also senior managers of the company (referred to as “executive directors”) are employed by the firm pursuant to service contracts, *see* STEPHEN GIRVIN ET AL., CHARLESWORTH’S COMPANY LAW 384 (18th ed. 2010), typically on an annual basis, *see* FIN. REPORTING COUNCIL, REVISIONS TO THE UK CORPORATE GOVERNANCE CODE (FORMERLY THE COMBINED CODE) 4 (2010), *available at* <http://www.frc.org.uk/images/uploaded/documents/May%202010%20report%20on%20Code%20consultation.pdf>. Notwithstanding the shareholders’ ability to vote out an executive director, only nineteen directors (executive and non-executive) from nine companies on the FTSE All Share Index

Reflecting another of Hamilton's concerns, a term limit could also cause CEOs to become short-sighted – maximizing returns in the short term and passing longer-term problems on to a successor.¹¹² Concerns of this kind, however, are not new to the corporate world. CEOs are often criticized for pursuing short-term gains at the expense of long-term share value.¹¹³ The problem, therefore, would likely result as much from an existing bias toward short-term outcomes as from a mandatory term limit.¹¹⁴ One response has been to craft compensation to better align shareholder and manager interests.¹¹⁵ A CEO's wealth can be tied to the long-term outcomes of her performance – for example, by awarding restricted stock that a CEO must hold after she

(approximately ninety-eight percent of the U.K. market capitalization, *see FTSE All Share Index Factsheet*, FTSE.COM, http://www.ftse.com/Indices/UK_Indices/Downloads/FTSE_All-Share_Index_Factsheet.pdf) lost a vote between 2000 and 2009. *See* FIN. REPORTING COUNCIL, *supra*. The U.K. example, therefore, may indicate that increased control by shareholders will not significantly affect the outcome of CEO selection. Note, however, that although U.K. shareholdings are more dispersed than in France or Germany, *see supra* note 106, share ownership in the United Kingdom has historically been more concentrated than in the United States. Part of the U.K. model, therefore, may be driven by the ability of large shareholders, through coordinated action, to implicitly influence how firms are managed. Accordingly, for U.K. firms, the need for explicit control – for example, by voting out a managing director – may also be less important than in the United States. *See* Gelter, *Dark Side*, *supra* note 106, at 186-90. Note, however, that institutional share ownership of the largest 1,000 U.S. public companies has increased significantly in recent years, from forty-six percent in 1987 to seventy-three percent in 2009. *See* THE CONFERENCE BOARD, THE 2010 INSTITUTIONAL INVESTMENT REPORT: TRENDS IN ASSET ALLOCATION AND PORTFOLIO COMPOSITION 27 tbl.13 (2010), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1707512&. Like the U.K. model, the rise of U.S. institutional shareholders may also limit the need for explicit control.

¹¹² Hamilton was concerned that, with a term limit, a chief executive would have little incentive to pursue longer-term projects whose benefits accrue to her successors, opting instead to focus on short-term plans and individual gains. *See* THE FEDERALIST NO. 72, *supra* note 105, at 387-88; *see also* Cohen & Spitzer, *supra* note 89, at 492-94, 510-11; David A. Crockett, "An Excess of Refinement": *Lame Duck Presidents in Constitutional and Historical Context*, 38 PRESIDENTIAL STUD. Q. 707, 713-14 (2008). Recent commentators have similarly argued that, by inducing rapid turnover, legislators have less interest to work cooperatively with others, focusing instead on personal and special interests. *See* Cohen & Spitzer, *supra* note 89, at 508; Crockett, *supra*, at 712.

¹¹³ *See, e.g.*, John R. Graham et al., *Value Destruction and Financial Reporting Decisions*, FIN. ANALYSTS J., Nov.-Dec. 2006, at 27, 31 (reporting, from a survey of nearly 400 senior managers, that managers are more than willing to alter investment decisions for the sake of hitting short-term earnings targets).

¹¹⁴ *See* Kent Greenfield, *Reclaiming Corporate Law in a New Gilded Age*, 2 HARV. L. & POL'Y REV. 1, 12-13 (2008) (describing the tendency of CEOs to engage in corporate downsizing solely to inflate stock prices).

¹¹⁵ *See* Walker, *supra* note 67, at 467-71.

leaves office.¹¹⁶ Retiring CEOs also would have an incentive to manage for the longer term in order to maintain their reputation if they planned to later seek office at another firm. Moreover, even with a term limit, CEOs may be interested in longer-term results if re-election remains a possibility.¹¹⁷

Capping CEO employment, of course, would be costly for some firms. By directly addressing tenure, and its associated problems, it would also be valuable for others. A key question is whether a mandatory requirement, even if detrimental for some, would benefit the economy as a whole.¹¹⁸ For every Steve Jobs (Apple's CEO)¹¹⁹ that could be lost, a CEO term limit would ensure

¹¹⁶ See Sanjai Bhagat & Roberta Romano, *Reforming Executive Compensation: Focusing and Committing to the Long-Term*, 26 YALE J. ON REG. 359, 363 (2009); Walker, *supra* note 67, at 468-70.

¹¹⁷ Hamilton argued that if a president could not stand for re-election, there would be little else to positively influence her behavior while in office. See THE FEDERALIST NO. 72, *supra* note 105, at 388.

¹¹⁸ Jeff Gordon has raised a similar question about the costs and benefits of imposing independent director requirements on public firms. See Gordon, *supra* note 12, at 1469. There is, in addition, the question of whether founders should be treated differently. Eleven percent of the largest public U.S. firms are headed by its founder. See Rüdiger Fahlenbrach, *Founder-CEOs, Investment Decisions, and Stock Market Performance*, 44 J. FIN. & QUANT. ANAL. 439, 439 (2009). A number of studies indicate that founder CEOs have a positive effect on corporate performance, including outperforming successor-CEO firms with respect to firm valuation, investment behavior, and stock market performance. See, e.g., Ronald C. Anderson & David M. Reeb, *Founding-Family Ownership and Firm Performance: Evidence from the S & P 500*, 58 J. FIN. 1301, 1303 (2003); Fahlenbrach, *supra*, at 439-41; Lerong He, *Do Founders Matter? A Study of Executive Compensation, Governance Structure and Firm Performance*, 23 J. BUS. VENTURING 257, 257-58 (2008); Daniel L. McConaughy et al., *Founding Family Controlled Firms: Efficiency and Value*, 7 REV. FIN. ECON. 1, 2 (1998). A founder-run firm, therefore, may not incur the same agency costs as a non-founder firm. In addition, founders may choose not to go public in order to avoid becoming subject to a mandatory term limit requirement. Thus, notwithstanding the potential benefits of a CEO term limit, there is an open question whether such a requirement should apply equally to founder CEOs. One possibility is to exclude founder CEOs from a term limit requirement. Doing so, however, implies that founder CEOs are less likely to engage in self-serving behavior than non-founder CEOs, which is unlikely to always be the case. An alternative would be to require founder CEOs, like others, to rely on the possibility of re-election at the end of their term. See *supra* notes 105-111 and accompanying text. Founder CEOs, in that case, would need to take into account a mandatory term limit in deciding to access the public market, just as they would need to consider the other costs and benefits of doing so. See Ronald J. Gilson & Charles K. Whitehead, *Deconstructing Equity: Public Ownership, Agency Costs, and Complete Capital Markets*, 108 COLUM. L. REV. 231, 255-57 (2008) (discussing the costs and benefits of accessing the public capital market).

¹¹⁹ See Philip Elmer-Dewitt, *Steve Jobs Is the No. 4 "Wealth Creator"*, CNNMONEY.COM (Dec. 20, 2010, 5:51 PM), <http://tech.fortune.cnn.com/2010/12/20/steve->

a review and vote by shareholders of a Jimmy Cayne (Bear Stearns' former CEO).¹²⁰ But, if term limits are valuable, why have shareholders not imposed them directly? One answer may be that CEO-dominated boards are reluctant to adopt a mandatory requirement. In a company with dispersed shareholders, power already resides with the board, which therefore may have little incentive to reduce the CEO's role.¹²¹ Another answer may be that shareholders would face a collective action problem if they tried to impose a term limit on their own. Faced with two equal opportunities – but one with, and the other without, a term limit – an attractive CEO candidate is likely to pick the unrestricted office. Thus, for shareholders, the cost of individual action may be prohibitive. Even if a CEO term limit is the better outcome, it is unclear how the transition would occur. Mandating a term limit for all CEOs would minimize that cost.¹²²

The more intriguing question is why CEO term limits never entered the corporate governance debate in the first place. The answer historically lies in the traditional deference given to directors. U.S. corporate law has tended to balance two sometimes-competing interests: the directors' interest in leeway to steer the firm, and the shareholders' interest in ensuring the firm is run for their benefit. On balance, it has tended to favor managerial discretion – reflecting the concern that tying down the board could hurt firms (and shareholders) and limit overall economic growth.¹²³

jobs-is-the-no-4-wealth-creator/ (highlighting Jobs' thirty-one-place jump in the 2010 *Chief Executive* magazine rankings).

¹²⁰ See William D. Cohan, *The Rise and Fall of Jimmy Cayne*, CNNMONEY.COM (Aug. 25, 2008, 3:39 PM), http://money.cnn.com/2008/07/31/magazines/fortune/rise_and_fall_Cayne_cohan.fortune/index.htm (describing how Cayne, as CEO of Bear Stearns, "had not changed; the world around him had").

¹²¹ See Oliver Hart, *Corporate Governance: Some Theories and Implications*, 105 *ECON. J.* 678, 687 (1995) (providing theoretical frameworks for corporate governance and applying them to proposals for reform).

¹²² Similar problems and solutions face voters in public elections. See Einer Elhauge, *Are Term Limits Undemocratic?*, 64 *U. CHI. L. REV.* 83, 86, 114-21 (1997). It is, of course, also possible that a CEO term limit would simply result in a less efficient governance structure and a decline in shareholder wealth. See *infra* notes 131-132 and accompanying text.

¹²³ See Stephen M. Bainbridge, *The Board of Directors as Nexus of Contracts*, 88 *IOWA L. REV.* 1, 31-33 (2002) (conceding that discretionary authority within the modern corporation creates agency costs, but that those are outweighed by the significant benefits of doing so); Black & Kraakman, *supra* note 33, at 1920-21 (contending that corporate law should be context-specific, since uniform rules may prohibit the use of critical managerial discretion to adapt to changing needs and conditions); see also *supra* notes 43-46 and accompanying text. Managers who can eschew short-term thinking in favor of longer-term projects potentially benefit society by supporting non-investor constituencies like employees and the communities in which they do business. See Strine, *supra* note 15, at 1769.

New regulation reflects a changing approach to governance. Not content to rely on boards alone, Congress – as evidenced by SOX and Dodd-Frank – has begun to regulate areas traditionally left to director discretion, including compensation¹²⁴ and job descriptions.¹²⁵ Corporate governance now includes affirmative requirements, imposed by regulation, which the CEO must satisfy.

Perhaps, therefore, we are entering a crossroads – a time when it is appropriate, based on the realization that boards cannot always control CEOs, to consider how much of the CEO's role should be regulated from the outside. Balanced against heightened regulation are the benefits of the traditional board-CEO relationship, which remains fundamentally private. There are – for both the company and society – important benefits to insulating the CEO from external oversight or universal standards.¹²⁶ The risk is that, given too much discretion, an entrenched CEO will throw off control altogether.¹²⁷ That tension is at the heart of the recent trend in corporate governance. New regulation has targeted specific CEO functions, but continues to rely generally on the board to oversee senior managers. A CEO term limit, therefore, may be most effective within a management framework that combines both.¹²⁸

None of the foregoing is intended to suggest that boards have abandoned their monitoring responsibilities. To the contrary, recent well-known examples include the forced resignations of Douglas Ivester (Coca-Cola)¹²⁹ and Robert Nardelli (Home Depot).¹³⁰ A mandatory term limit, however, would ensure that *all* public company CEOs are subject to a minimum level of scrutiny. The result would be a system, consistent with SOX and Dodd-Frank, that maintains primary control with the board, but more directly regulates the most problematic aspects of the CEO function. That balance may, in turn, more closely reflect today's understanding of how shareholders, directors, and officers interact.

¹²⁴ See *supra* notes 67-69, 71, and accompanying text.

¹²⁵ See *supra* note 70 and accompanying text.

¹²⁶ See Strine, *supra* note 15, at 1769; see also *supra* notes 43-46 and accompanying text.

¹²⁷ See *supra* notes 16, 52-57, and accompanying text.

¹²⁸ Striking a balance between control and discretion is a key ingredient for ensuring the corporate form can adapt to changes in the environment. See Katharina Pistor et al., *The Evolution of Corporate Law: A Cross-Country Comparison*, 23 U. PA. J. INT'L ECON. L. 791, 796 (2002) (finding that the historical challenge of corporate law has been to develop a set of rules that permit the flexibility necessary for businesses to thrive while, at the same time, controlling agency costs).

¹²⁹ See Betsy Morris & Patricia Sellers, *What Really Happened at Coke*, FORTUNE, Jan. 10, 2000, available at http://money.cnn.com/magazines/fortune/fortune_archive/2000/01/10/271736/index.htm.

¹³⁰ See Parija B. Kavilanz, *Nardelli Out at Home Depot*, CNNMONEY.COM (Jan. 3, 2007), http://money.cnn.com/2007/01/03/news/companies/home_depot/index.htm.

CONCLUSION

This Essay has considered the evolving regulation of CEOs – a shift from deference to the board to more direct, external control – by analyzing a mandatory CEO term limit. An external requirement, like a term limit, would have had no place within the traditional framing. Yet, direct regulation of the CEO may be increasingly possible as corporate governance evolves.

Perhaps, however, a CEO term limit goes too far. The decline in average CEO tenure suggests that CEO power is already on the wane, making additional regulation unnecessary, in particular as momentum from recent changes continues to limit CEO authority.¹³¹ Moreover, in a recent study, proposals to cap or regulate executive pay, increase shareholder access to the company's proxy statement, and eliminate staggered boards were viewed by shareholders, on the whole, as value-decreasing.¹³² Consistent with such findings, new regulation has targeted only discrete aspects of the CEO's job and has been much less intrusive than a mandatory cap on tenure.

Yet, as history has shown, a CEO is able to use her position within the firm to enhance her own status. Precisely because the average tenure has dropped, now may be the best time – with the least resistance – to implement a market-wide term-limit requirement that extends to all public firms, including those whose CEOs' terms have not declined. In addition, as director tenures continue to shorten, longer-term CEOs may begin to use their relative longevity to their own personal advantage, potentially at shareholder expense. Equalizing terms in office may be necessary simply to level the playing field. The costs of doing so can be prohibitive – and, at this stage, those costs are difficult to ascertain. Nevertheless, as perceptions of the corporation continue to evolve, the benefits of a CEO term limit – or other regulation that minimizes the costs of tenure – may increasingly favor a new approach.

¹³¹ See Kahan & Rock, *supra* note 12, at 1051.

¹³² See Larcker et al., *supra* note 45, at 4-6 (empirically finding that proposed new corporate governance regulation would negatively affect shareholder wealth).