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PICKING THE LOCKS: RECENT DOJ ENFORCEMENT OF CLAYTON ACT'S PROHIBITIONS ON INTERLOCKING DIRECTORATES

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The business community was put on notice last week after the Department of Justice (DOJ) announced the resignations of seven directors from five corporate boards following what DOJ called the "first in a broader review of potentially unlawful interlocking directorates."[1]

Section 8 of the Clayton Act (15 U.S.C. § 19) prohibits one person from serving as director of two or more corporations when those corporations are direct (horizontal) competitors, subject to limited exceptions.

The question becomes: is DOJ's recent action its typical decennial reminder of Section 8's prohibitions, or is this the beginning of a new focus on enforcement? Time will tell. In the meantime, it is important to keep Section 8's prohibitions in mind and address potential risks before DOJ comes knocking.

BACKGROUND

This century-old law seeks to protect against competitors sharing competitively sensitive information and coordinating their businesses by prohibiting an individual from serving as an officer or director of two competing companies.

Specifically, Section 8 provides that "[n]o person shall, at the same time, serve as a director or officer in any two corporations (other than banks, banking associations, and trust companies)" if:

1. the "capital, surplus, and undivided profits" of each corporation exceeds $41,034,000[2]
2. each corporation is "engaged in whole or in part in commerce"; and,
3. each corporation is "by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the antitrust laws."

Despite its relatively long existence, its infrequent enforcement leaves many unanswered questions around its application. Clarity around Section 8 is also muddled by DOJ's practice of accepting parties' voluntary resignations to eliminate interlocks rather than filing a complaint in federal court—as DOJ did last week.

TAKEAWAYS

Firms must be mindful of DOJ's interpretation of "persons"

DOJ takes the position that corporations and associations are "persons" under the statute, and have forced resignations when firms have different representatives serving on the boards of two competing corporations, notwithstanding that the representatives are not the same person.

DOJ's action last week reaffirms this approach. The recently announced resignations included two individuals representing an investment firm on the boards of competing companies. Similarly, three individuals representing a private equity firm on a single company's board resigned due to another individual from the firm holding a board position with a competing company.

Section 8's application to non-corporate entities remains unclear

DOJ has signaled in recent years that Section 8 should apply to interlocks involving non-corporate entities, such as LLCs, because "the harm can be the same regardless of the form of the entities."[3]However, DOJ's recent actions all involved corporate entities, and there has not yet been enforcement against interlocks involving non-corporate entities.

Corporations and Investors must evaluate existing and contemplated interlocks and ensure compliance with Section 8

Private equity firms holding board seats or appointing leadership in multiple portfolio companies should carefully evaluate whether any companies in which they have investments could be considered "competitors" for Section 8 purposes.

It is equally important to monitor competitive changes to investment portfolio companies with existing interlocks to ensure the companies do not become "competitors" in any line of business. Additionally, firms should consider Section 8's prohibitions when contemplating an acquisition in which the firm proposes to acquire board seats.

In the context of both acquisitions and spin-offs, Section 8 contains a safe-harbor allowing one-year for the individual—or representative—to resign from one of the corporate boards. However, this safe-harbor does not apply to newly appointed board members; it is aimed at providing those already on a board with time to resolve an interlock that arises after their appointment.

Monitor annual thresholds against corporate assets

Each January, the Federal Trade Commission announces minimum thresholds for application of Section 8.

Currently, Section 8 applies when each interlocked company's "capital, surplus, and undivided profits" exceed $41,034,000, while an exception to Section 8 exists when the competitive sales of either corporation total less than $4,103,400.

Antitrust enforcers are prioritizing and actively reviewing potential interlocks

DOJ's recent action makes good on its promises over the last several years to reinvigorate enforcement of Section 8. Private equity and other investment firms must evaluate and address existing interlocks before they are caught in the sights of antitrust enforcers.

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[1] Press Release, Directors Resign from the Boards of Five Companies in Response to Justice Department Concerns about Potentially Illegal Interlocking Directorates, available at https://www.justice.gov/opa/pr/directors-resign-boards-five-companies-response-justice-department-concerns-about-potentially.

[2] Inflation-adjusted threshold set annually by the Federal Trade Commission. See Federal Trade Comm'n, Revised Jurisdictional Thresholds for Section 8 of the Clayton Act, January 24, 2022, https://www.ftc.gov/legal-library/browse/federal-register-notices/revised-jurisdictional-thresholds-section-8-clayton-act-20.

[3] Assistant Attorney General Makan Delrahim Delivers Remarks at Fordham University School of Law, available at https://www.justice.gov/opa/speech/assistant-attorney-general-makan-delrahim-delivers-remarks-fordham-university-school-law.

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