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Enhanced antitrust enforcement extends to scrutiny of interlocking directorates

BY CYNTHIA RICHMAN

Much of the increasingly aggressive rhetoric around antitrust enforcement has centred on ambitious efforts to fashion novel legal theories, regulations and laws to address competition in areas like employee hiring, 'big tech' and healthcare. But in outlining its enforcement priorities, the federal government has recently expressed renewed interest in section 8 of the Clayton Act, an oft-overlooked (or ignored) statute which prohibits interlocking directorates.

Interlocking directorates arise when two competing corporations share one or more directors or officers in common. A 'direct' interlock occurs when the same individual serves as a director or officer of competing corporations. An 'indirect' interlock can arise where different individuals serve as directors or officers of competing corporations, but both have been 'deputised' to act on behalf of the same third entity.

The law has certain safe harbour exceptions based on the size of the corporations and the magnitude of the 'competitive sales' of the corporations – i.e., "products and services sold by one corporation in competition with the other". In assessing whether there is direct competition under section 8, courts focus not only on the degree of actual interchangeability of use between the products of alleged competitors, but also on evidence concerning: (i) the extent to which the industry and its customers recognise the products as separate or competing; (ii) the extent to which production techniques for the products are similar; and (iii) the extent to which the products can be said to have distinctive customers.

An interlocking directorate raises antitrust concerns because of the perceived risk that the officer or director may serve as the conduit for an anticompetitive agreement or information exchange. One commentator explained: "when an individual simultaneously serves as an officer or director of two *competing* companies, he or she stumbles into a prime opportunity for collusion – for example, coordination of pricing, marketing, or production plans of the two companies".

According to *U.S. v. Sears, Roebuck & Co* (1953), the purpose of section 8 is therefore to "nip in the bud incipient violations of the antitrust laws by removing the opportunity or temptation to such violations through interlocking directorates". Violations of section 8 are per se violations, meaning that a lack of competitive injury will not excuse

the parties from liability unless one of the exemptions in the statute applies.

In an April 2022 speech, Jonathan Kanter, assistant attorney general for the Department of Justice's (DOJ's) Antitrust Division, pledged to increase enforcement of section 8, explaining the Division was "committed to litigating cases using the whole legislative toolbox that Congress has given us to promote competition". He warned that the DOJ is "ramping up efforts to identify violations across the broader economy" and "will not hesitate to bring section 8 cases to break up interlocking directorates".

This is not the first time the federal antitrust agencies have threatened close scrutiny of interlocks, but in raising the spectre of litigation, it does reflect a more aggressive approach. In 2019, the Federal Trade Commission (FTC) published a blog post, 'Interlocking Mindfulness', reminding companies of the need to avoid director interlocks, particularly where mergers or spin offs are involved. This followed a 2017 post advising that companies "[h]ave a plan to comply with the bar on horizontal interlocks". By referencing the possibility of DOJ lawsuits, Mr Kanter's statements are a significant departure from the FTC's 2017 guidance stating that the FTC "relie[s] on self-policing to prevent section 8 violations".

The penalties for violating section 8 typically do not involve monetary fines; rather, the statute requires that the parties eliminate the interlock if a violation is found to have occurred. Enforcement actions against interlocking directorates under section 8 may be brought by governmental enforcement agencies, such as the FTC, the DOJ or state attorneys general. There is also a private right of action for a section 8 claim, although to date private plaintiffs have not been successful in obtaining monetary relief and have only obtained injunctions to stop overlapping directors from serving. The principal remedy for a violation of section 8 is elimination of the interlock, and relief may include prohibition of future interlocks.

The law provides for a one-year grace period, such that a person who was not initially prohibited from serving as an officer or director may continue to serve until one year after the corporations become competitors and the competitive sales exceed the relevant threshold. And there are several safe harbours to consider when assessing whether a violation might exist. As noted, section 8 contains exceptions for competing sales that are below certain thresholds. These thresholds include: (i) the competitive sales of either company are less than 2 percent of that company's total sales; (ii) the competitive sales of each company are less than 4 percent of that company's total sales; or (iii) the competitive sales of either company are less than $4,103,400 as of 21 January 2022.

In light of the charged antitrust enforcement environment, corporations would be well-advised to take proactive steps to detect interlocks before they occur and monitor existing ones to ensure they comply with current section 8 safe harbours.

Corporations whose directors or officers are being considered for an outside position should first evaluate the position for potential section 8 concerns. Where a corporation's director or officer holds an outside position at another firm subject to a safe harbour due either to a lack of competition or a de minimis overlap, counsel should reevaluate the relationship periodically to ensure marketplace developments do not cause the position to run afoul of section 8. Particularly in dynamic markets, competitive relationships can change rapidly with evolving technology and shifting business strategies and product lines. This can occur because of growing sales in existing overlaps or entry into new lines of business. Periodic checks on interlocks can be incorporated as part of existing director and officer independence analyses.

Additionally, corporations engaged in financial transactions, such as acquisitions or spin offs where the parent's directors or officers may hold positions at the spin off, should check whether the parent and the spin off may compete in any line of business and evaluate potential section 8 issues. In the context of mergers or partial acquisitions, the government may require parties to restructure a deal to avoid a section 8 violation.

Interlocking directorate issues arise with some regularity in the context of private equity firms which acquire board seats across a diverse portfolio of companies and may be likely to encounter section 8 issues via a merger or acquisition. For that reason, private equity firms holding board seats or appointing leadership in multiple portfolio companies should evaluate carefully whether any could be considered 'competitors' for section 8 purposes.

Corporations should also be mindful of interlocks arising from subsidiaries. Although the law is somewhat unsettled, in the event an interlock involves a corporation that competes with the subsidiary of another corporation, a court generally examines whether the business of the subsidiary can be attributed to that subsidiary's parent.

On one final note, other antitrust statutes, particularly section 1 of the Sherman Act (which prohibits agreements that unreasonably restrain trade), continue to apply even if the interlock is within the section 8 safe harbours. In addition, section 5 of the FTC Act may also reach interlocks that do not technically meet section 8's requirements but violate the policy against horizontal interlocks expressed in section 8. For example, section 5 can reach interlocks involving banks, which are exempt from section 8, and competing non-bank corporations. Thus, even beyond section 8 compliance, there is good reason for companies to monitor their directors' and officers' board membership. ■

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