Cooley

Biden Justice Department Continues Focus on Interlocking Directorates

March 29, 2023

The Department of Justice recently **announced that five directors had resigned from four corporate boards**, and one company declined to exercise board appointment rights in the face of the Antitrust Division's stepped-up enforcement of antitrust rules against interlocking directorates.

These resignations come just months after the **DOJ announced that seven directors had resigned from five company boards**, signaling that the DOJ is continuing to scrutinize interlocking directorates.

The most recent actions affected companies from a variety of sectors, including software, transportation and insurance. Private equity firms' board appointment rights – with different representatives on competing firms' boards – were at the center of three of the interlocks, while a fourth involved three competing IT companies sharing a common director.

Meanwhile, the chair of the Senate Judiciary Committee recently called on the Federal Trade Commission (FTC) to scrutinize interlocks in the pharmaceutical industry.

DOJ actions have only resulted in resignations

The DOJ's recent Section 8 enforcement initiative has resulted only in voluntary board resignations, not consent agreements or civil penalties. This has allowed the DOJ to claim success, but the actions are not precedential and have not changed the legal scope of Section 8.

The DOJ can enter into consent orders with companies – and has in the past. It even successfully sought a court order prohibiting a company from hiring as an officer any individual who was a director of one of the interlocked corporations if, at the same time, a director of the second interlocked company was employed by the defendant. However, Section 8 does not provide the DOJ with authority to seek civil penalties or other monetary relief, though a violation of a consent decree entered into in a Section 8 case could be enforced by the DOJ through a contempt proceeding where the DOJ could seek costs, attorneys' fees and other monetary relief.

DOJ remains committed to 'representation' theory

On its face, Section 8 clearly prohibits, subject to de minimis exceptions, the same person from serving on the boards of two competitors. But the DOJ is going further, and directors have resigned where two different individuals – associated with the same private equity or venture capital firm – serve on the boards of competing companies. In its recent announcements, the DOJ has touted the resignations of different board members appointed by the same investment firm.

No court has found a violation of Section 8 based on this theory. However, in *Reading International, Inc. v. Oaktree Capital Management LLC*, the US District Court for the Southern District of New York denied a motion to dismiss a claim where an investment firm owned minority positions in competing movie theater groups.

Importantly, however, the court held that the plaintiffs would need to show more than common employment by the investment firm. They would need to demonstrate that "their service on the boards is not in their individual capacities" but as "puppets or instrumentalities of the corporation's will, such that it can legitimately be said that" the investment firm – not the individuals as separate persons – sits on the two boards.

The court's analysis leaves room to argue that different individuals serving on boards are not engaged in the type of coordination that Section 8 is designed to prohibit – especially if they have adopted measures to prevent the exchange of competitively sensitive information.

When are corporations considered 'competitors' for purposes of Section 8?

The language of Section 8 prohibits an officer or director of one corporation from serving as an officer or director of another corporation if they are "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." This leaves open the question of whether an agreement between the two corporations would constitute an antitrust violation.

Securities disclosures

In its recent enforcement push, the DOJ has relied in large part on corporations' Securities and Exchange Commission (SEC) filings to identify competing corporations. In most of the resignations announced by the Biden DOJ, at least one of the companies identified the other as a competitor in its SEC filings.

Merger investigations

Some of the recent actions appear to have arisen from merger investigations, where a company likely identified the other firm as a competitor in internal documents submitted with a merger filing.

Horizontal relationship

Courts have typically required interlocks to be between companies in the same line of business at the same stage of production. Involvement in different aspects of the same industry has not been sufficient to establish the competitive relationship for a Section 8 interlock. For example, one court found that an agent for producers of television programming was not in competition with the producer-owners of the programming because only the latter had the authority to make pricing decisions. The companies could not fix prices or allocate markets as required by the statute.

Seeking to sell similar products to same customers

Courts have looked to the market definition analyses to see if companies have "common sales in the same product and geographic market." Thus, courts have questioned whether two products can be said to compete because they are reasonably interchangeable with respect to the uses to which they can be put and whether two products are competitive because there is a high elasticity of demand on the part of customers.

Other courts, however, have said that relying on interchangeability of use and cross-elasticity of demand may be too restrictive, especially "[i]n a developing industry in which product variation is just beginning and customer needs are not yet standardized." Thus, courts also have relied on evidence that companies sought to sell similar products to the same prospective customers.

Section 8 has not been applied to potential competitors

In a **report on interlocking directorates**, the FTC in fact stated that Section 8 "leaves unchallenged interlocking directorates between corporations, both large and small, that have not been competitors in the past but might become so in the future." Courts have followed this guidance, reasoning that a corporation's "plans or intentions to engage in the production of [the relevant product] d[id] not … make it a competitor … within the meaning of Section 8," and therefore Section 8 "is not violated by [the director's] membership on the boards of both companies."

Statutory de minimis exemptions

Even if companies are competitors, Section 8 does not condemn all interlocks.

The FTC adjusts de minimis thresholds annually, and it did so earlier this year. Now, both corporations' net assets must exceed $45.257 million.

Further, the competitive sales of the companies must exceed $4.5257 million in each firms' last fiscal year.

The competitive overlap also is considered de minimis if the competitive sales of either corporation are less than 2% of that corporation's total sales, or if the competitive sales of each corporation are less than 4% of that corporation's total sales.

For assessing whether your board is Section 8-ready, see our November 2022 client alert on boardroom antitrust scrutiny, which lays out suggested steps for companies to take.

Key Contacts

Megan Browdie Washington, DC	mbrowdie@cooley.com +1 202 728 7104
Howard Morse Washington, DC	hmorse@cooley.com +1 202 842 7852
Parker Erkmann Washington, DC	perkmann@cooley.com +1 202 776 2036

Dee Bansal Washington, DC	dbansal@cooley.com +1 202 728 7027
Ethan Glass Washington, DC	eglass@cooley.com +1 202 776 2244
Beatriz Mejia San Francisco	mejiab@cooley.com +1 415 693 2145
David Burns Washington, DC	dburns@cooley.com +1 202 728 7147
Sharon Connaughton Washington, DC	sconnaughton@cooley.com +1 202 728 7007
Samantha Kirby Palo Alto	skirby@cooley.com +1 650 843 5319

This information is a general description of the law; it is not intended to provide specific legal advice nor is it intended to create an attorney-client relationship with Cooley LLP. Before taking any action on this information you should seek professional counsel.