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Client Alert

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Shareholder Activists Should Be Mindful of DOJ's Renewed Focus on Interlocking Directorates When Assembling Their Slates

On October 19, 2022, the Department of Justice (the "DOJ") announced in a press release (the "DOJ Press Release") that seven directors from five separate public U.S. companies had resigned from their board positions in response to concerns by the DOJ Antitrust Division (the "Division") that their roles violated the Clayton Act's prohibition on interlocking directorates among competitors.[1] This announcement signals that the Division is following through on its recently stated intention to enforce Section 8 of the Clayton Act (15 U.S.C. § 19) ("Section 8"), a seldom-enforced antitrust statute designed to prevent competitors from having overlapping directors or officers. In light of the DOJ's reinvigorated Section 8 focus and enforcement, shareholder activists should redouble their efforts to conduct the requisite due diligence and analysis necessary to ensure that none of their director candidates serves as a director or officer of a competitor of the target corporation absent an applicable safe harbor.

Section 8 of the Clayton Act

Section 8 prohibits the same person from serving simultaneously as a director or officer of two competing corporations (known as "interlocking directorates" or "director interlocks"), subject to specified exceptions. As a *per se* statute, Section 8 is designed to prevent competitors from having interlocking directorates regardless of whether anticompetitive activities actually occur. The interlocking directorate can also be indirect based on a *deputization* theory, which can occur when different individuals serve as a director or officer of competing corporations while acting on behalf, or at the discretion, of a single firm or entity.

The purpose of Section 8 and its enforcement is to decrease the opportunities for the exchange of sensitive information between

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[1] https://www.justice.gov/opa/pr/directors-resign-boards-five-companies-response-justice-department-concerns-about-potentially.

competitors and the risk of anticompetitive behavior. As further articulated by the Division in the DOJ Press Release, "competitors sharing officers or directors further concentrates power and creates the opportunity to exchange competitively sensitive information and facilitate coordination – all to the detriment of the economy and the American public."[2] By removing the opportunity for interlocking directors to coordinate in this manner, Section 8 prevents or "nips in the bud" anticompetitive behavior before it occurs.

Section 8 contains a *jurisdictional* (or minimum size) threshold that excludes from its restrictions two competing corporations alleged to have board interlocks if either corporation has capital, surplus, and undivided profits aggregating less than $41,034,000 (adjusted annually). Even if the *jurisdictional* threshold is met by the competing corporations, there are three *de minimis* exceptions to the Section 8 prohibitions that permit the interlocks for both companies where:

1. either corporation's "competitive sales" are less than $4,103,400 for the most recent completed fiscal year (adjusted annually);

2. either corporation's "competitive sales" are less than 2% of that corporation's "total sales" for the most recent completed fiscal year; or

3. each corporation's "competitive sales" are less than 4% of that corporation's "total sales" for the most recent completed fiscal year.[3]

The *de minimis* exceptions are intended to permit interlocks that involve innocuous competitive overlaps. For the purposes of these exceptions, "competitive sales" means the gross revenues for all products and services sold by one corporation in competition with the other, determined on the basis of annual gross revenues for such products and services in that corporation's last fiscal year, and "total sales" means the gross revenues for all products and services sold by the corporation over its last fiscal year.

The DOJ Announcement

Historically, Section 8 has rarely been enforced and authorities have relied on "self-policing" to prevent violations. The DOJ Press Release however, alongside further public comments from DOJ officials over the past several months, signal that the self-policing era may be coming to an end.

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[2] *Id.*
[3] 15 U.S.C. § 19(a)(2).

The Division stated that the DOJ will be "undertaking an extensive review of interlocking directorates across the entire economy" for the purpose of enforcing Section 8. Similarly, at the 2022 Spring Enforcers Summit in April, the Division underscored that enforcement against interlocked boards will be one of its priorities, and that it "will not hesitate to bring Section 8 cases to break up interlocking directorates."[4]

As part of these renewed efforts to enforce and deter violations of Section 8, the DOJ announced that seven directors had resigned from five U.S. public companies in response to the Division's concerns. Shareholder activists should take note that some of the directors who resigned did so due to the Division's apparent concerns based on a *deputization* theory of violation. For example, in response to the Division's concerns with alleged directorate interlocks at Solarwinds Corp. ("Solarwinds") and Dynatrace, Inc., three directors who were allegedly representatives of Thoma Bravo, an investment firm, resigned from the Solarwinds board. One of the three Thoma Bravo representatives served simultaneously on the boards of both corporations. Through this director, according to the Division, Thoma Bravo effectively served on and represented the interests of Thoma Bravo on the boards of both corporations.

Takeaways for Shareholder Activists

The DOJ's reinvigorated focus on director interlocks is highly relevant to shareholder activists and their process for assembling their slates:

- Shareholder activists must be thorough in vetting potential director nominees to ensure that their election would not create a director interlock as a result of an existing directorship or management position at a competing corporation. This can be best achieved by asking prospective nominees to complete an appropriate questionnaire.

- Shareholder activists should avoid circumstances under which the activist could be deemed a director of two competing corporations under a *deputization* theory in violation of Section 8 by virtue of one or more of its principals or employees serving on the boards of these corporations or potentially another individual outside the activist's organization who, based on the facts and circumstances, could otherwise be deemed to represent the interests of the activist on these boards.

- Even if a directorate interlock is exempt under Section 8, other rules, such as Section 1 of the Sherman Act (which prohibits agreements that unreasonably restrain trade) could be construed to

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[4] https://www.justice.gov/atr/page/file/1494606/download.

prohibit the improper exchange of information among competitors. The flow of information between a shareholder activist and one or more of its representatives on the boards of competing corporations could increase its risk of being accused of violating these rules and potentially subject the activist to substantial fines and criminal penalties.

- Alleged Section 8 violations are typically addressed by way of a director resignation that eliminates the interlock. Losing a director representative on the board of a portfolio company under these circumstances could be extremely detrimental to the activist, who may have previously spent significant time and resources to obtain board representation.

- A determination of whether a corporation is a "competitor" of another under Section 8 or what constitutes "competitive sales" and "total sales" under the *de minimis* exceptions may not be straightforward. Shareholder activists should consult with counsel experienced in this area of law to assist with this assessment.

- It would not surprise us to see defense law firms advise corporations to further expand their already onerous D&O questionnaires to require dissident nominees to disclose even more information regarding the nominees' past, present and future positions at corporations on the pretext that they are necessary in light of the DOJ's renewed focus on potential Section 8 violations.

Please contact the Olshan attorney with whom you regularly work or one of the attorneys listed below if you would like to discuss further or have questions with respect to this matter.

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