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DOJ Investigating "Interlocking Directorates" in PE Industry

In its latest step to elevate antitrust scrutiny of private equity, DOJ launches a series of investigations of board seats under Section 8 of the Clayton Act.

The US Department of Justice (DOJ) recently began sending confidential investigation letters to private equity (PE) sponsors and portfolio companies regarding "interlocking directorate" issues under Section 8 of the Clayton Act (Section 8). In several cases, the DOJ has sent major PE sponsors "civil investigative demands" (subpoenas) for documents and information regarding the sponsor's structure, holdings, and board representations, without limitation as to any particular transaction.

The full scope of the DOJ's efforts is not yet clear, but these investigations will likely be far-reaching given the DOJ's public comments over the last six months regarding PE sponsors, and the DOJ's increased focus on Section 8 issues in merger investigations during that same period.

Why It Matters

Section 8 prohibits a person who is an officer or director of one company from acting as an officer or sitting on the board of a direct competitor of that company (an "interlocking directorate"), with some exceptions. Section 8 aims to prevent officers and board representatives from acting as conduits among competitors, either purposefully or inadvertently.

Section 8 has a number of technical provisions, and the law's boundaries are not always clear. Companies, investors, and board and officer candidates often need to make judgment calls about whether and how the law applies to their particular situation. With the DOJ scrutinizing these issues, now is a good opportunity for sponsors and portfolio companies in the PE sector to run a check on their Section 8 compliance.

Key Considerations

Three main factors inform a Section 8 analysis: whether the companies in question are "competitors," whether the interlock involves the same "person," and whether technical thresholds or exemptions apply. While simple to articulate, in practice each of these factors raise special considerations for PE sponsors, operating companies, and board and officer candidates:

Competitors	"Same Person"	Thresholds and Exemptions
Section 8 defines "competitors" practically: would an agreement that eliminates horizontal competition between two vendors violate the antitrust laws? If so, those vendors are competitors. The boundaries of when firms compete are not always clear, however (e.g., two firms may sell similar products but use different business models). Corporate structure also plays a factor: for example, two firms controlled by a common parent are incapable of conspiring with each other, so an interlock between them would not violate Section 8. Other holding structures may warrant similar treatment depending on the circumstances.	On its face, Section 8 only applies when an individual would sit on the board or act as an officer of two direct competitors. DOJ interprets Section 8 broadly, though, to mean that *different* individuals cannot sit on competitors' boards or serve as officers if those individuals are under the direction of a common entity (e.g., a company cannot appoint one director to Competitor A and a different director to Competitor B). No court has yet adopted this so-called "representative" theory.	Section 8 requires each corporation have "capital, surplus, and aggregated profits" in excess of $41 million (this threshold updates annually). Section 8 does not apply if: • The competitive sales of either company are below $ 4.1 million (threshold updated annually). • The competitive sales are less than 2% of either corporation's sales. • The competitive sales are less than 4% of both companies' sales.

The most common remedy when the DOJ identifies an interlocking directorate is to remove the individual in question from the competitor board or officer position. If the DOJ were to discover that a board member or officer was actually conveying competitively sensitive information between two competitors, though, the DOJ could in principle investigate those information exchanges as civil or criminal antitrust law violations.

Private plaintiffs have a private right of action under Section 8. (Damages technically might be available to private litigants, but they have never been awarded.)

The extraterritorial boundaries of Section 8 have never been tested by the DOJ, but the DOJ is likely to take the position that any interlock between companies that compete in the US is subject to Section 8's restrictions.

Latham & Watkins will continue to report on the DOJ's focus on Section 8 issues and other developments in this area.

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