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Time For A New Look At Interlocking Board Directorate History

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Interlocking board directorates are back in the antitrust hot seat after the U.S. Department of Justice recently announced that seven directors had resigned from the boards of five separate companies after the DOJ raised concerns that their roles violated Section 8 of the Clayton Act.[1]

With the DOJ warning that this was "the first in a broader review of potentially unlawful interlocking directorates,"[2] boards of directors, in-house counsel and history aficionados alike will find it instructive to revisit Section 8's origins and its history of enforcement over the years.

History of Section 8 of the Clayton Act

Impetus and Historical Context

As has been well documented, public outrage to perceived out-of-control monopolies served as a core impetus for the creation of antitrust laws in the United States in the late 1800s. So-called trust busters scored a major victory with the passage of the Sherman Antitrust Act in 1890.

The Sherman Act outlaws a broad set of conduct — "every contract, combination, or conspiracy in restraint of trade," and any "monopolization, attempted monopolization, or conspiracy or combination to monopolize."[3] Trust busters were hopeful that the Sherman Act would break up large companies in industries such as steel, sugar and railroads.

But in the years that followed, many observed that large conglomerates still dominated many sectors of the economy, and some singled out interlocking directorates as barriers to achieving the goals of the Sherman Act. In particular, critics of interlocking directorates believed that they discouraged competition and advancement of new talent on the merits.

In an article published in Harper's Weekly and then in a collection of essays in 1914, soon-to-be Justice Louis Brandeis, an adviser to President Woodrow Wilson, called the practice of interlocking directorates "the root of many evils."[4]

Using the term broadly to include "all intertwined conflicting interests," including a corporation contracting with one of its directors or directors holding positions in two potentially competing companies, Justice Brandeis argued that the practice "tends to the suppression of competition," "to disloyalty" and "to inefficiency."[5]

In a January 1914 address to a joint session of Congress, Wilson denounced the abuses of "interlockings of the personnel of the directorates of great corporations,"[6] explaining that the practice concentrated corporate power among a few privileged masters when what was needed in management was "new men, new energies, a new spirit of initiative, new blood" to "open the field of industrial development."[7]

Wilson also stated that the practice of interlocking directorates encouraged self-dealing among vertically integrated companies, which harmed competition and consumers.[8]

Amid this public debate, a prominent financial firm announced that it would voluntarily withdraw from 30 different boards.[9] This news made it to the front page of The New York Times, and was communicated to Wilson as "an indication that big business is preparing to surrender unconditionally."[10]

In a public statement, the financial firm cited

an apparent change in public sentiment in regard to Directorships …now … warrant[ing] us in seeking to resign from some of these connections. … Indeed it may be, in view of the change in sentiment upon this subject, that we shall be in a better position to serve such properties and their security holders, if we are not Directors.[11]

The concerns about the negative effects of interlocking directorates culminated in the June 1914 passage of the Clayton Antitrust Act,[12] which was intended to supplement and strengthen the Sherman Act, not to replace it.

Section 8 of the act was the response to Wilson's public reproach of interlocking directorates — "to arrest the creation of trusts, conspiracies and monopolies in their incipiency and before consummation"[13] by ensuring that no one person could direct the business operations of more than one company.

It stated that

no person at the same time shall be a director in any two or more corporations, any one of which has capital, surplus, and undivided profits aggregating more than $1,000,000 … if such corporations are or shall have been theretofore, 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 provisions of any of the antitrust laws.[14]

The general prohibition excepted "banks, banking associations, trust companies and common carriers," which were subject to separate regulatory authority.[15]

The bank industry was also specifically addressed earlier in Section 8, reflecting concerns at the time around perceived self-dealing financiers. No person was to

be a director or other officer or employee of more than one bank, banking association or trust company ... either of which has deposits, capital, surplus, and undivided profits aggregating more than $5,000,000

and was followed by lengthy text prohibiting other such overlaps. Similar language remained in the statute through several rounds of amendments until 1990, when it was overhauled and modernized[16] by Congress as discussed below.

Enforcement

Once Section 8 passed, it went largely unenforced. The 1953 U.S. v. Sears, Roebuck & Co. decision in the U.S. District Court for the Southern District of New York notes that "the case is one of novel impression involving the first construction of [Section 8] of the Clayton Act since its passage in 1914."[17]

Later that same year, the U.S. Supreme Court issued an opinion in U.S. v. W. T. Grant Co., noting that "it is only recently that the Government has attempted systematic enforcement of § 8."[18]

In W.T. Grant, the Supreme Court affirmed a district court decision concluding that mere resignation from a board does not render a Section 8 violation moot. Only if a "defendant can demonstrate that 'there is no reasonable expectation that the wrong will be repeated'" will the matter be mooted.[19]

This laid a heavy burden on companies and individuals attempting to defend against Section 8 claims.

The next wave of interest in Section 8 came in the mid-1960s. In 1963, the Federal Trade Commission announced it had installed a computer with the ability to trace interlocking directorates among companies with overlapping product lines.[20]

And two years later, after an FTC Bureau of Economics study revealed a large number of interlocking directorates among the country's thousand largest corporations, the FTC initiated investigations and claimed a number of directorates were voluntarily terminated as a result.[21]

Around the same time, Congress recommended new legislation to broaden Section 8's prohibition, which it concluded was currently ineffective.[22] But this legislation did not pass and the FTC did not take any enforcement action, blunting the surge.

The third cycle of activity occurred shortly after, in the 1970s and 1980s, when the FTC and DOJ led an enforcement campaign that challenged an "unprecedented number of corporate interlocks."[23]

At this time, the agencies "abandoned their former policy of dismissing a case once a director … resigned from all but one of the boards," instead requiring directors and corporations to "enter into formal consent orders [to] terminate the interlock [and] impose certain restrictions on … future board elections."[24]

This wave of enforcement led Congress to revisit Section 8. In particular, the U.S. Court of Appeals for the Ninth Circuit's 1981 TRW Inc. v. FTC decision[25] riled opponents of Section 8 when it concluded that Section 8 did not contemplate a de minimis exception and, thus, applied even if the overlap between the companies in question was insignificant.[26]

Opponents of the decision claimed that this made it difficult to recruit top talent to director

positions.[27] As a result, in 1990, it was amended to add de minimis exceptions "to avoid application when no potential for competitive harm exists."[28]

Companies could seek safe harbor from Section 8 enforcement if the competitive sales of either corporation were less than:

- $1,000,000 as adjusted;
- Two percent of that corporation's total sales; or
- Four percent of that corporation's total sales.[29]

The amendment also expanded Section 8 to cover officers chosen or elected by the board, in addition to directors, and raised the jurisdictional threshold to reflect the modern economy, among other changes.[30] Finally, the amendment struck the lengthy prohibitions specifically addressing the banking industry.

Section 8 Today

Since the early 1990s, Section 8 has gone largely unenforced despite its prohibition remaining the same. A person may not, subject to certain statutory exceptions — e.g., a bank — be a director or officer of two or more corporations that are engaged in U.S. commerce and that are competitors if certain monetary thresholds, updated annually by the FTC, are met.[31]

In 2022, the threshold that each corporation must meet to fall under the prohibition of Section 8 is capital, surplus, and undivided profits of more than $41,034,000 as described in Section 8(a)(l).[32]

The section's three safe harbors, established in 1990, still stand, with the 2022 threshold for the first — the competitive sales of either corporation are less than $1 million — adjusted to $4,103,400.[33]

Each of the three exceptions "requires an assessment of relative competitive sales levels,"[34] and the FTC cautions that any company with an interlock should monitor its capital position as well as each firm's sales of overlapping products. Even "small increases in competitive sales (or decreases in overall sales) may push a company outside the safe harbors."[35]

The last high-profile government challenge under Section 8 occurred in 2009, when the FTC initiated an antitrust investigation into two major technology companies that shared directors and increasingly competed in the cellphone and operating systems markets.[36] The investigation led the directors to resign. Otherwise, enforcement remained rare.

Now, the government seems poised to begin another cycle of Section 8 enforcement.

At the Spring Enforcers Summit hosted by the DOJ Antitrust Division and the FTC in April, Assistant Attorney General Jonathan Kanter stated:

For too long, our Section 8 [Clayton Act] enforcement has essentially been limited to our merger review process. We are ramping up efforts to identify violations across the broader economy, and we will not hesitate to bring Section 8 cases.[37]

In addition to the DOJ inquiries prompting board of director resignations, the FTC has also been increasing its focus on interlocking directorates. In September 2021, the FTC voted to adopt compulsory process resolutions on a wide range of topics, including common directors and officers.[38]

The FTC has previously stated it could use Section 5 of the FTC Act to enforce the "spirit and policy" of Section 8, even if the behavior in question did not explicitly violate the Section's "letter."[39]

Implications for Companies

The waves of enforcement of Section 8 over the past century demonstrate that companies should be cognizant of the risks associated with directors sitting on multiple boards, even if the relevant companies are not direct competitors.

In practical terms, companies should take care to screen incoming and current directors for any conflicts relating to their membership with other company boards.

Companies should also be aware that periods of increased government enforcement of Section 8 have corresponded to an uptick in private actions to enforce Section 8, a common theme in antitrust law where the plaintiffs' bar often follows closely behind in paths created by regulators.[40]

As antitrust scholar Victor H. Kramer noted in a 1950 Yale Law Journal article:

[T]he program of enforcement may encourage institution of stockholders' [or management] actions attacking the legality of directorships.[41]

If the last hundred years is any indication, most Section 8 disputes do not get to trial — instead they settle or are resolved by a conflicted director stepping down from one or more boards of competitors and disavowing any similar future conduct.

Still, any enforcement action or private litigation can generate unfavorable public attention, slow down company operations, incur serious costs, and have other negative downstream effects.

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[1] Press Release DOJ: Directors Resign from the Boards of Five Companies in Response to Justice Department Concerns about Potentially Illegal Interlocking Directorates (Oct. 19, 2022), https://www.justice.gov/opa/pr/directors-resign-boards-five-companies-response-justice-department-concerns-about-potentially.

[2] Id.

[3] Sherman Antitrust Act, 15 U.S. Code § 1.

[4] Louis D. Brandeis, Chapter III, Other People's Money, 1914, https://louisville.edu/law/library/special-collections/the-louis-d.-brandeis-collection/other-peoples-money-chapter-iii.

[5] Id.

[6] 51 Cong.Rec.1962-1964. Also viewable at Transcript, January 20, 1914: Address to a Joint Session of Congress on Trusts and Monopolies, The Miller Center, https://millercenter.org/the-presidency/presidential-speeches/january-20-1914-address-joint-session-congress-trusts-and.

[7] Id.

[8] Id.

[9] Victor H. Kramer, Interlocking Directorships and the Clayton Act After 35 Years, 59 Yale L.J. 1266 (1950).

[10] Ray S. Baker, 4 Woodrow Wilson: Life and Letters, 369 (1931).

[11] Kramer, supra note 9.

[12] S. Rep. No. 698 16 (1914). See the identical language in H.R. Rep. No. 627 19-20 (1914) ("The idea that there are only a few men in any of our great corporations and industries who are capable of handling the affairs of the same is contrary to the spirit of our institutions.").

[13] S. Rep. No. 698 223-224 (1914).

[14] Act to supplement existing laws against unlawful restraints and monopolies, and for other purposes, Pub. L. No. 63-212 / Chapter 323, 63rd Congress. 38 Stat. 730, 733 (1914).

[15] Id

[16] 1990 U.S.C.C.A.N. 4100, 4102.

[17] United States v. Sears, Roebuck & Co., 111 F. Supp. 614, 616 (S.D.N.Y. 1953).

[18] United States v. W. T. Grant Co., 345 U.S. 629, 634 (1953).

[19] Id. at 633.

[20] Richard E. Day, Developments in Antitrust During the Past Year, 25 A.B.A. Section of Antitrust Law 3, 90 (1964).

[21] Annual Report of the Federal Trade Commission For the Fiscal Year Ended June 30, 1965 at 26, Federal Trade Commission, https://www.ftc.gov/sites/default/files/documents/reports_annual/annual-report-1965/ar1965_0.pdf.

[22] Staff of the Antitrust Subcomm. of the House Comm. On the Judiciary, 89th Cong., 1st Sess., Report on Interlocks in Corporate Management 57, 227 (1965).

[23] Cynthia A. Jorgensen and James J. Clark, Interlocking Directorates and Section 8 of the Clayton Act, 44 Alb. L. Rev 139, 140 (1979).

[24] Id.

[25] TRW, Inc. v. F.T.C., 647 F.2d 942, 948 (9th Cir. 1981).

[26] Id. at 948.

[27] The Interlocking Directorate Act of 1986, Hearing on S. 2063 Before the S. Comm. on the Judiciary, 99th Cong., 2d Sess. (Apr. 28, 1986).

[28] 1990 U.S.C.C.A.N. 4100, 4101.

[29] "Antitrust Amendments Act of 1990," Pub. L. No. 101-588, 101 Congress. 104 Stat. 2879 (November 16, 1990).

[30] Id.

[31] 15 U.S. Code § 19.

[32] See 15 U.S. Code § 19(a)(1); see also Press Release, F.T.C., FTC Announces Annual Update of Size of Transaction Thresholds for Premerger Notification Filings and Interlocking Directorates (Jan. 24, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/01/ftc-announces-annual-update-size-transaction-thresholds-premerger-notification-filings-interlocking.

[33] 15 U.S. Code § 19.

[34] Debbie Feinstein, Have a Plan to Comply With the Bar on Horizontal Interlocks, Federal Trade Commission, January 23, 2017, https://www.ftc.gov/enforcement/competition-matters/2017/01/have-plan-comply-bar-horizontal-interlocks [last visited December 1, 2022].

[35] Id.

[36] Miguel Helft & Brad Stone, Board Ties at Apple and Google are Scrutinized, N.Y. Times, May 4, 2009, https://www.nytimes.com/2009/05/05/technology/companies/05apple.html.

[37] Assistant Attorney General Jonathan Kanter Delivers Opening Remarks at 2022 Spring Enforcers Summit, Department of Justice, April 4, 2022, https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-delivers-opening-remarks-2022-spring-enforcers.

[38] F.T.C. No. 211 0160, Resolution Directing Use of Compulsory Process Regarding Common Directors and Officers and Common Ownership(Sept. 2, 2021), https://www.ftc.gov/system/files/attachments/press-releases/ftc-streamlines-consumer-protection-competition-investigations-eight-key-enforcement-areas-enable/omnibus_resolutions_p859900.pdf.

[39] Kroger Company, 93 F.T.C. 302 (1979), https://www.ftc.gov/sites/default/files/documents/commission_decision_volumes/volume-93/ftc_volume_decision_93_january_-_june_1979pages_302-401.pdf; see also current language on the FTC's website, Debbie Feinstein, Have a Plan to Comply With the Bar on Horizontal Interlocks, Federal Trade Commission, January 23, 2017, https://www.ftc.gov/enforcement/competition-

matters/2017/01/have-plan-comply-bar-horizontal-interlocks [last visited December 1, 2022].

[40] See, for example, the rash of private Section 8 actions that were filed in the 1970's during the third wave of significant government enforcement, Protectoseal Co. v. Barancik, 484 F.2d 585 (7th Cir. 1973), Jicarilla Apache Tribe v. Supron Energy Corp., 479 F. Supp. 536 (D.N.M. 1979), aff'd in part, rev'd in part, 728 F.2d 1555 (10th Cir. 1984); and Kennecott Copper Corp. v. Curtiss-Wright Corp., 449 F. Supp. 951 (S.D.N.Y.), aff'd in part, rev'd in part, 584 F.2d 1195 (2d Cir. 1978) among others.

[41] Kramer, supra note 9, at 1271.