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PRIVATE EQUITY FIRM RELINQUISHES BOARD RIGHTS, DISSOLVES JOINT VENTURE AFTER FTC RAISES ANTITRUST CONCERNS

To Our Clients and Friends:

On August 16, 2023, the Federal Trade Commission announced the resolution of an antitrust investigation into the proposed acquisition by EQT Corporation of THQ Appalachia I, LLC and THQ-XcL Holdings I, LLC, two companies backed by equity commitments from funds managed by Quantum Energy Partners. As part of the resolution, Quantum is required to relinquish any rights to a seat on EQT's board, forgo the acquisition of a board seat on seven other natural gas producers active in the Appalachian Basin, and dissolve a separate, pre-existing joint venture between EQT and Quantum, among other commitments. The announcement is a reminder that companies must continue to be mindful of potential Clayton Act Section 8 concerns when considering mergers and other combinations.

Background

An interlocking directorate—where competing firms share common officers or directors—raises potential antitrust concerns because of the perceived risk that the officer or director may serve as the conduit for an anticompetitive agreement or an exchange of competitively sensitive information.

The agencies have dramatically ratcheted up the frequency and tenor of their warnings on Section 8 compliance. As discussed in a prior Client Alert,[1] DOJ Antitrust Division head Jonathan Kanter promised in an April 2022 speech to bring litigation to break up alleged interlocks. In 2019, the FTC published a blog post, *Interlocking Mindfulness*, on the need to avoid director interlocks, particularly where mergers or spin-offs are involved.[2]

Clayton Act, Section 8

Section 8 of the Clayton Act (15 U.S.C. § 19) is the primary vehicle by which the U.S. antitrust agencies police interlocking directorates. In general, the statute prohibits one person from being an officer (defined as an "officer elected or chosen by the Board of Directors") or director at two companies that are "by virtue of their business and location of operation, competitors." The agencies have asserted that "person" has a broader meaning than a natural person, and includes a single firm or other entity that "deputizes" an agent or agents to sit on boards of competing corporations.[3] Under this very broad construction, which remains untested in court and unclear in application, a single firm could be at risk of a Section 8 violation by appointing directors or officers of two competing corporations, even if different individuals are appointed.

Section 8 broadly defines "competitors" to include any two corporations where "the elimination of competition by agreement between them would constitute a violation of any of the antitrust laws." Section 8 is broad and potentially applies where two competitors have an officer or director in common, subject to certain exceptions.

There are three potential safe harbors from Section 8 liability:

- The competitive sales of ***either*** company are less than 2% of that company's total sales;
- The competitive sales of ***each*** company are less than 4% of that company's total sales; or
- The competitive sales of ***either*** company are less than $4,525,700 as of 2023.

While there are no penalties or fines imposed due to a Section 8 violation, the statute requires that the parties eliminate the interlock if a violation is found to have occurred. There is a one-year grace period to cure violations that develop after the interlock has occurred (e.g., competitive sales surpassing *de minimis* thresholds), provided the interlock did not violate Section 8 when it first occurred.

An antitrust investigation into a potential interlock may force the resignation of key officers or directors, lead to a consent settlement relating to Section 8 compliance, delay the closing of a proposed transaction, or trigger a broader examination of information sharing or possible collusion between the firms involved.

The Quantum-EQT Enforcement Action

Under the terms of the proposed transaction, which was announced in September 2022, EQT (the largest producer of natural gas in the Appalachian Basin) would acquire: 1) Quantum Energy's Tug Hill, alleged to be the eleventh largest producer of natural gas in the Appalachian Basin, and 2) Quantum Energy's XcL Midstream, which holds gas processing and transportation assets for production from Tug Hill's assets. In exchange, Quantum would acquire up to 55 million EQT shares and the right to a seat on EQT's board of directors. The parties contemplated that Quantum's CEO, Wil VanLoh, would sit on EQT's board.

After an extended investigation lasting almost twelve months, the FTC announced a proposed consent order clearing the transaction subject to the following commitments:

- A prohibition on any Quantum-affiliated person serving on EQT's board for 10 years (and vice versa);
- A prohibition on any Quantum-affiliated person serving on the board of any of the seven largest producers of natural gas in the Appalachian Basin without FTC approval;
- Divestiture of Quantum's EQT shares, and a prohibition on acquisition of any additional shares without FTC approval;

- Dissolution of EQT and Quantum's The Mineral Company joint venture, which was a cooperative arrangement to acquire mineral rights in the Appalachian Basin that pre-dated the proposed transaction; and

- Implementation by Quantum and EQT of an antitrust compliance program.

The action is notable in several respects.

First, despite Section 8's textual limitation to corporations, the FTC's analysis of the proposed consent order indicates that "Quantum is subject to the prohibition on interlocking directors and officers under Section 8 of the Clayton Act, despite Quantum's limited liability and limited partnership corporate structure."[4] If approved, this may mark the first instance (albeit in an uncontested settlement) in which Section 8 was applied to a non-corporate business structure and could have important ramifications for private equity firms such as Quantum.

Second, the case would mark the FTC's first Section 8 enforcement action in 40 years. Section 8 has traditionally been enforced by DOJ, and the Quantum-EQT action suggests that both DOJ and FTC will act to enforce alleged Section 8 violations going forward.

Third, the complaint alleges that The Mineral Company joint venture and board seat arrangement are each an "unfair method of competition" in violation of Section 5 of the FTC Act. As discussed in a prior Client Alert,[5] the FTC issued a Policy Statement in November 2022 announcing its intent to expand enforcement of Section 5 of the FTC Act to a wide range of alleged anticompetitive conduct, including alleged interlocking directorates and anticompetitive joint ventures. The Quantum-EQT action may mark the first such instance of Section 5 being applied in this way following the November 2022 Policy Statement.

Section 8 Compliance in the Current Regulatory Environment

Companies should take reasonable steps to detect interlocks before they occur and monitor existing ones to ensure they comply with current Section 8 safe harbors.

Companies whose directors or officers are being considered for an outside position should first evaluate the position for potential Section 8 concerns. Where a company's director or officer holds an outside position at another firm subject to a safe harbor 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. This can occur because of growing sales in existing overlaps or entry into new lines of business. These checks can be incorporated as part of existing director/officer independence analyses.

Companies engaged in financial transactions, such as 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.

Private equity firms holding board seats or appointing leadership in multiple portfolio companies should evaluate whether any could be considered "competitors" for Section 8 purposes.

Expect DOJ and FTC to continue to push expanded interpretations of Section 8 that strain precedent and look beyond the individuals themselves who sit on a board of directors and look instead to the companies appointing them and/or whether those directors have affiliations that might trigger antitrust scrutiny.

Other antitrust statutes, particularly Section 1 of the Sherman Act (which prohibits agreements that unreasonably restrain trade), but possibly now Section 5 of the FTC Act, continue to apply even if the interlock is within Section 8 safe harbors. A sound antitrust compliance plan will therefore also establish reasonable procedures to prevent sharing of competitively sensitive information, among other things.

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[1] https://www.gibsondunn.com/doj-antitrust-division-head-promises-litigation-to-break-up-director-interlocks/.

[2] Michael E. Blaisdell, *Interlocking Mindfulness*, June 26, 2019, available at: https://www.ftc.gov/enforcement/competition-matters/2019/06/interlocking-mindfulness.

[3] *Interlocking Mindfulness* (Section 8 "prohibits not only a person from acting as officer or director of two competitors, but also any one **firm** from appointing two different people to sit as its agents as officers or directors of competing companies").

[4] Analysis of Agreement Containing Consent Order to Aid Public Comment, *In the Matter of EQT Corp.*, File No. 221-0212, available at: https://www.ftc.gov/system/files/ftc_gov/pdf/2210212eqtquantumaapc.pdf.

[5] https://www.gibsondunn.com/ftc-announces-broader-vision-of-its-section-5-authority-to-address-unfair-methods-of-competition/.

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