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FTC and DOJ Provide Critical Clarity on Passive Investment Rules Under Antitrust Law

Alert
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In a significant development for institutional investors, the Federal Trade Commission (FTC) and Department of Justice (DOJ) have provided their first explicit statement confirming that engagement with companies on corporate governance matters is consistent with passive investment status under antitrust laws. This clarification came through a Statement of Interest (SoI) filed in Texas' antitrust lawsuit against major asset managers BlackRock, State Street, and Vanguard.

THE "SOLELY FOR INVESTMENT" EXEMPTION

Under Section 7 of the Clayton Act and the Hart-Scott-Rodino (HSR) Act, investors can claim a "solely for investment" exemption when acquiring stock holdings. This exemption allows institutional investors to bypass certain antitrust reporting requirements for acquisitions under 10% (or 15% for institutional investors) of a company's shares, provided they have "no intention of participating in the formulation, determination, or direction of the basic business decisions of the issuer."

Historically, antitrust agencies have characterized this as a "narrow exemption" limited to "passive investors," warning that it becomes unavailable if investors "attempt to influence" management decisions. This created uncertainty about what types of engagement activities might jeopardize passive investor status.

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PROVIDING NEW CLARITY WITH CRITICAL BOUNDARIES AND LIMITATIONS

The FTC/DOJ SoI represents the first time federal antitrust agencies have explicitly confirmed that certain corporate governance activities are permissible under the passive investment framework. The agencies identified several permissible activities where passive investors are allowed to provide input or even to advocate:

- Board Structure Discussions: Conferring with officers and directors on board size and composition.
- Compensation Policy Engagement: Working with management on executive compensation frameworks.
- Reporting Standards: Advocating for improved public reporting practices and disclosure standards.

The agencies characterized these activities as "ordinary course conduct" of asset managers and noted that improving corporate governance is often "competitively neutral or procompetitive." This statement supports the common understanding that efforts to enhance oversight and reporting practices generally benefit consumers and don't implicate antitrust concerns.

While providing welcome clarity, the SoI lays out important boundaries. The DOJ and FTC view the passive investment exemption as a test that must be satisfied continually throughout ownership of the company, not just at the time of acquisition. The agencies stressed that the exemption can be forfeited "depending on how investors use those investments" after acquisition.

The agencies also emphasized that the *subject matter of engagement with the company is crucial* to the analysis. Investors must avoid "pushing for specific operational or strategic decisions" under the guise of corporate governance, as such actions would likely be deemed inconsistent with passive investing. For example, efforts to coordinate "output reduction targets" or influence production decisions across competing companies would risk antitrust enforcement.

The FTC and DOJ specifically declined to support the "common ownership" theory of antitrust harm — an academic theory whereby passive investors' minority interests in competing firms could automatically lessen competition without evidence of anticompetitive behavior. The agencies reaffirmed their 2017 position cautioning against across-the-board limitations on common ownership, citing concerns about "unintended real-world costs on businesses and consumers by making it more difficult to diversify risk."

At the same time, the agencies rejected expansive interpretations of "solely for investment," emphasizing that any additional motive beyond financial returns can jeopardize the passive investment exemption. Investments made to leverage holdings across competitors to shape market-wide behavior fail the passive investment test.

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IMPLICATIONS FOR THE INVESTMENT COMMUNITY

The agencies' commentary that antitrust laws shouldn't chill "typical asset management behavior" provides reassurance to institutional investors who have been uncertain about the boundaries of permissible engagement. This development represents a significant step toward providing the clarity that institutional investors have long sought regarding their role in corporate governance while maintaining compliance with antitrust laws. Even so, investors must remain vigilant about staying within the defined boundaries, particularly avoiding operational or strategic decision-making that could compromise their passive status and avoid coordination across competing investments that could invite antitrust scrutiny.

For more information on passive investment exemptions under antitrust law, please contact Jeetander Dulani, Bill Greene, Nicci Warr, Vicki Smith, John Bessler, Emily Asp, or the Stinson LLP contact with whom you regularly work.

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