ABA Panel Recap: "The PE Effect: Antitrust Scrutiny Abounds"

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The investment strategies of some private equity (PE) firms have recently raised concerns from competition authorities in the United States. So-called "roll-up strategies" (whereby a PE firm makes a series of non-reportable acquisitions[1] within an industry) have caught the attention of the Federal Trade Commission (FTC) and the US Department of Justice (DOJ). The FTC and DOJ claim that such serial acquisitions allow a PE firm to acquire monopoly power in an industry.[2] The FTC has also claimed that PE ownership can have a negative effect on product or service quality.[3]

At the same time, the updated Merger Guidelines and proposed changes to the Hart-Scott-Rodino pre-merger filing requirements include several provisions that could bring increased scrutiny to PE acquisitions.

On April 10, 2024, the ABA Antitrust Section's Insurance & Financial Services Committee hosted the panel "The PE Effect: Antitrust Scrutiny Abounds." The discussion was moderated by John Snyder (Alston & Bird) and featured panelists Norm Armstrong (Kirkland & Ellis), Rebekah Goshorn Jurata (American Investment Council), Leslie Overton (Axinn Veltrop & Harkrider), and Richard Mosier (FTC). The panelists discussed the evolution of PE-related regulations in the United States and their potential implications for PE firms.

I. The PE Business Model

Ms. Jurata explained that PE funds invest capital using a strategy that typically involves acquiring a private company (also called a portfolio company once acquired), managing the private company for a period of three to seven years, and then selling the company. PE firms can provide funding to firms that are not able to access public debt or equity markets. PE firms are incentivized to maximize the value of their portfolio companies, because doing so will increase their return on investment when they eventually sell their portfolio companies.

Mr. Mosier discussed how agencies factor in the PE business model when assessing competition issues. He noted that it is incorrect to assume that acquisitions by financial buyers (such as PE buyers) do not need to be scrutinized to the same extent as acquisitions by strategic buyers (such as other companies in the same or related industry) and that the same rules apply to all buyers. He described some of the public discourse on the PE business model, including criticisms that it focuses too much on short-term profits and/or underinvesting, saddles companies with debt and weakens their balance sheets, and involves layoffs or sale leaseback transactions.

II. PE-Related Statutes

Mr. Mosier highlighted the following statutes relevant to antitrust enforcement and PE:

- Section 7 of the Clayton Act, which prohibits mergers and acquisitions where the effect "may be substantially to lessen competition, or to tend to create a monopoly."[4]
- Section 7A of the Clayton Act, which specifies which acquisitions must be reported to the DOJ and FTC in advance of their execution.[5]
- Section 8 of the Clayton Act, which prohibits directors and officers from serving simultaneously on the boards of competitors.[6]
- Section 1 of the Sherman Act, which prohibits contracts, combinations, or conspiracies in restraint of trade or commerce.[7]
- Section 2 of the Sherman Act, which makes it unlawful for any person "to monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations[.]"[8]

The review of mergers and acquisitions in the United States has undergone some recent revisions, including the updated Merger Guidelines and proposed changes to the pre-merger filing requirements. In addition, the current administration has been taking a "whole of government" approach to competition, including PE deals.[9]

III. Changes to the Hart-Scott-Rodino Act and Pre-Merger Filing Requirements

Ms. Overton discussed the evolution of filing requirements under the Hart-Scott-Rodino Act (HSR Act). 10 In 2011, changes to the HSR Act streamlined the pre-merger notification process for both the filing entities and competition authorities reviewing the pre-merger notifications. Other changes required increased transparency of the acquiring party's "associates" and their overlap with the company being acquired. PE firms fall under the umbrella of "associates," although the definition does not explicitly include the term "private equity."[11]

In 2023, the FTC and DOJ announced a proposal to further change the filing requirements under the HSR Act.[12] The proposed revisions to the HSR filing requirements increase the amount of information that acquiring parties need to disclose as part of the pre-merger notification process.[13] The panelists discussed a proposed change that requires acquiring parties to disclose the history of past acquisitions dating back to at least ten years prior to the filing date. Currently, pre-merger notifications only require a transaction history of five years prior to the filing date.[14]

The FTC and DOJ estimate that the time required to prepare a filing will increase from 37 hours per filing to 144 hours, leading to a total of $350 million dollars in annual labor costs across all filings.[15] Mr. Armstrong, Ms. Jurata, and Ms. Overton also noted that increasing the amount of information required to be disclosed may lead to the disclosure of information that is unnecessary for agencies to assess antitrust issues related to some PE firms' deals, which could delay the review process. For instance, PE firms may invest in portfolio companies that operate in different industries,[16] and information on historical acquisitions in unrelated industries are likely to be unimportant for agencies' assessment of a deal.

IV. Recent Enforcement Efforts

The panelists discussed two recent enforcement efforts by US antitrust authorities: (1) the FTC's actions against JAB Consumer Partners and (2) *Federal Trade Commission v. U.S. Anesthesia Partners, Inc. and Welsh, Carson, Anderson & Stowe XI, L.P., et al.*

Mr. Armstrong discussed the PE firm JAB Consumer Partners' (JAB's) proposed acquisition of SAGE Veterinary Partners (SAGE) in 2021. At the time, JAB was the parent company of Compassion-First Pet Hospitals and National Veterinary Associates. The FTC investigation concluded that the proposed acquisition of SAGE would allow JAB to "establish a dominant position in key markets for specialty and emergency veterinary services in California and Texas."[17] The FTC ordered JAB to divest clinics in California and Texas for it to proceed with the acquisition of SAGE.[18] The FTC also ordered that JAB shall not acquire any veterinary practice, clinic, or facility doing business near National Veterinary Associates without providing written notification to the FTC.[19]

The panelists also reviewed the FTC's complaint against the PE firm Welsh, Carson, Anderson & Stowe (Welsh Carson) and U.S. Anesthesia Partners (USAP), a provider of anesthesia services in Texas that is part of Welsh Carson's portfolio of companies. The FTC alleged that Welsh Carlson and USAP illegally established monopoly power in the market for anesthesiology practices in Texas. The at-issue actions of Welsh Carlson and USAP involved a series of non-reportable acquisitions of large anesthesiology practices in Texas, price-setting agreements with other anesthesiology practices to artificially increase prices, and a deal signed with a competitor preventing it from providing anesthesiology services in the areas served by USAP.[20] The complaint illustrates the FTC's view of serial acquisitions in the same industry as potentially problematic. Smaller, non-HSR reportable acquisitions are subject to investigation by the DOJ and FTC under various antitrust statutes.

V. The PE Business Model and Competition

The PE business model has drawn increased attention from government agencies and legislators. One area of skepticism around PE firms is the possibility that the PE business model may be inherently harmful. Critics claim that the PE business model leads to higher prices or lower product or service quality because of the way that PE deals are financed and because of PE firms' incentives. PE firms use a leveraged buyout strategy in which a company is acquired by borrowing a large amount of debt, and the concern is that increased debt-service costs are passed on to final consumers in the form of higher product or service prices.

The panelists analyzed the results of an academic study that investigated the effect of PE ownership on the quality of the services provide by nursing homes.[21] The study compared the medical outcomes of nursing homes owned by PE firms with other nursing homes. The study concluded that mortality rates were higher, the number of caregivers was smaller, and management fees were larger at the nursing homes owned by PE firms relative to other nursing homes.

Ms. Jurata cautioned against generalizing the results of this study to PE deals in general. She described another study that compared the medical outcomes of nursing homes owned by PE firms with other nursing homes during the COVID-19 pandemic. The study concluded that the nursing homes owned by PE firms experienced a smaller number of COVID-19 cases among patients and staff, as well as a smaller probability of a shortage of N95 masks, surgical masks, and other protective equipment.[22]

VI. Conclusion

The PE business model has gained attention from the FTC, DOJ, media, academic researchers, and the general public, and the proposed changes to the HSR Act indicate that PE deals will undergo more thorough reviews than they have in the past. This increased scrutiny may be intended to detect consolidations that can lead to market power and consumer harm, but it may impose additional costs with unintended consequences. Moreover, the increased monitoring of serial acquisitions made by PE firms may discourage PE firms from specializing in investments within a given industry – a practice which carries both potential benefits and risks, and which will continue to be a subject for debate.[23]

Endnotes

1 In the United States, the Hart-Scott-Rodino Act (HSR Act) establishes the criteria under which firms involved in merger and acquisition deals need to notify the US competition authorities prior to the deals' completion. Deals that are valued above a certain threshold and that involve firms of sufficiently large size are required to be reported under the HSR Act. Sufficiently small deals are not required to be reported under the HSR Act. *See* Federal Trade Commission's [FTC's] Premerger Notification Office, "To File or Not to File: When You Must File a Premerger Notification Report Form," revised September 2008, available at https://www.ftc.gov/sites/default/files/attachments/premerger-introductory-guides/guide2.pdf.

2 *See* Liu, Henry, "Slow the Roll-up: Help Shine a Light on Serial Acquisitions," FTC, May 23, 2024, available at https://www.ftc.gov/enforcement/competition-matters/2024/05/slow-roll-help-shine-light-serial-acquisitions. *See also* US Department of Justice [DOJ], "Justice Department and Federal Trade Commission Seek Information on Serial Acquisitions, Roll-Up Strategies Across U.S. Economy," May 23, 2024, available at https://www.justice.gov/opa/pr/justice-department-and-federal-trade-commission-seek-information-serial-acquisitions-roll.

3 *See* Miller, Jake, "What Happens When Private Equity Takes Over a Hospital," Harvard Medical School, December 26, 2023, available at https://hms.harvard.edu/news/what-happens-when-private-equity-takes-over-hospital. *See also* Abelson, Reed and Margot Sanger-Katz, "Serious Medical Errors Rose After Private Equity Firms Bought Hospitals," *The New York Times*, December 26, 2023, available at https://www.nytimes.com/2023/12/26/upshot/hospitals-medical-errors.html.

4 *See* FTC, "The Antitrust Laws," available at https://www.ftc.gov/advice-guidance/competition-guidance/guide-antitrust-laws/antitrust-laws.

5 *See* FTC, "Revised Jurisdictional Thresholds for Section 7A of the Clayton Act," 2024, available at https://www.ftc.gov/system/files/ftc_gov/pdf/p859910_-_secn_7a_-_new_hsr_thresholds_2024.pdf.

6 *See* DOJ, "Justice Department's Ongoing Section 8 Enforcement Prevents More Potentially Illegal Interlocking Directorates," March 9, 2023, available at https://www.justice.gov/opa/pr/justice-department-s-ongoing-section-8-enforcement-prevents-more-potentially-illegal.

7 *See* Sherman Act, 15 U.S.C. §1 (1890).

8 *See* Sherman Act, 15 U.S.C. §2 (1890).

9 *See* FTC, "Federal Trade Commission, the Department of Justice and the Department of Health and Human Services Launch Cross-Government Inquiry on Impact of Corporate Greed in Health Care," March 5, 2024, available at https://www.ftc.gov/news-events/news/press-releases/2024/03/federal-trade-commission-department-justice-department-health-human-services-launch-cross-government.

10 *See* FTC, "FTC, DOJ Announce Changes to Streamline the Premerger Notification Form," July 7, 2011, available at https://www.ftc.gov/news-events/news/press-releases/2011/07/ftc-doj-announce-changes-streamline-premerger-notification-form.

11 Associates of an acquiring person refer to "an entity that is not an affiliate of such person but: (A) has the right, directly or indirectly, to manage the operations or investment decisions of an acquiring entity (a 'managing entity'); or (B) has its operations or investment decisions, directly or indirectly, managed by the acquiring person; or (C) directly or indirectly controls, is controlled by, or is under common control with a managing entity; or (D) directly or indirectly manages, is managed by, or is under common operational or investment management with a managing entity." *See* 16 C.F.R. § 801.1(d)(2).

12 *See* FTC, "FTC and DOJ Propose Changes to HSR Form for More Effective, Efficient Merger Review," June 27, 2023, available at https://www.ftc.gov/news-events/news/press-releases/2023/06/ftc-doj-propose-changes-hsr-form-more-effective-efficient-merger-review.

13 *See* Id., p. 10.

14 *See* Id., p. 87.

15 *See* Id., pp. 103-104.

16 *See* Lossen, Ulrich, "The Performance of Private Equity Funds: Does Diversification Matter?" in P*ortfolio Strategies of Private Equity Firms: Theory and Evidence* (DUV, 2007).

17 *See* FTC, "Statement of Chair Lina M. Khan," June 13, 2022, available at https://www.ftc.gov/system/files/ftc_gov/pdf/2022.06.13%20-%20Statement%20of%20Chair%20Lina%20M.%20Khan%20Regarding%20NVA-Sage%20-%20new.pdf.

18 *See* FTC, "FTC Approves Final Order Protecting Pet Owners from Private Equity Firm's Anticompetitive Acquisition of Veterinary Services Clinics," August 5, 2022, available at https://www.ftc.gov/news-events/news/press-releases/2022/08/ftc-approves-final-order-protecting-pet-owners-private-equity-firms-anticompetitive-acquisition.

19 *See In the Matter of JAB Consumer Partners SCA SICAR, National Veterinary Associates, Inc., and SAGE Veterinary Partners, LCC*, FTC No. 2110140, "Decision and Order," Docket No. C-4766, p. 21.

20 *See* FTC, "FTC Challenges Private Equity Firm's Scheme to Suppress Competition in Anesthesiology Practices Across Texas," September 21, 2023, available at https://www.ftc.gov/news-events/news/press-releases/2023/09/ftc-challenges-private-equity-firms-scheme-suppress-competition-anesthesiology-practices-across.

21 *See* Gupta, Atul, et al., "Owner Incentives and Performance in Healthcare: Private Equity Investment in Nursing Homes," *The Review of Financial Studies* 37, no. 4 (2024): 1029-1077.

22 *See* Gandhi, Ashvin, YoungJun Song, and Prabhava Upadrashta, "Have Private Equity Owned Nursing Homes Fared Worse Under COVID-19?" *SSRN*, August 28, 2020, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3682892.

23 Some academic research shows that there are potential benefits from PE firms specializing in an industry. *See* Rigamonti, Damiana, et al., "The effects of the specialization of private equity firms on their exit strategy," *Journal of Business Finance & Accounting* 43, no. 9-10 (2016): 1420-1443. *See also* Gejadze, Maia, Pierre Giot, and Armin Schwienbacher, "Private equity fundraising and firm specialization," *The Quarterly Review of Economics and Finance* 64 (2017): 259-274.