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Private Equity

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LETTER FROM THE EDITOR

Dear Readers,

This edition of the Chronicle focuses on private equity ("PE") markets.

The PE industry has experienced extraordinary growth over the past few years. In parallel, antitrust scrutiny of PE by antitrust enforcers has intensified, with visceral rhetoric from various agencies and legislatures worldwide. The articles in this volume address the implications of these developments.

Giorgio Motta, Kenneth B. Schwartz, David M. Goldblatt & Michael B. Singer focus on developments in the U.S. As noted, over the last several years, private equity firms have faced an increasingly aggressive antitrust enforcement environment. The U.S. Department of Justice, the Federal Trade Commission, and antitrust agencies in Europe are also closely examining private equity acquisition strategies as a whole, general investment incentives, potential filing violations and board interlocks. Antitrust regulators may, however, ultimately have difficulty proving that private equity business models actually result in less competition. The bottom line is that, with the right approach, private equity firms can continue to pursue their investment and acquisition strategies despite greater agency scrutiny.

Vishal Mehta, Megan E. Gerking & David E. Grothouse build on the above, by analyzing how these actions have ranged from strong concessions demanded in PE transactions under review to DOJ letters alleging illegal interlocking directorates and threatening lawsuits. In this article, the authors explore recent antitrust focus on PE in the context of broader enforcement trends, highlight recent enforcement activity, and preview what dealmakers and practitioners may expect on the horizon, and offer practical tips for navigating this new landscape.

Anna Tzanaki ponders the question of where competition, antitrust, and private equity intersect. PE was once antitrust's favored child compared to strategic buyers, but now PE seems to have fallen from competition enforcers' grace. Interestingly, this is part of a broader trend: financial investors in general, have come into the antitrust spotlight. Being a minority financial investor is no longer reason for antitrust immunity. Economic theory and competition policy have been shifting. Common ownership of small stakes in rival firms by institutional investors, even if passive, can create harm. In developments on both sides of the Atlantic, competition law enforcement signals no empty threats, but rather an eagerness to cover blind spots. As the article discusses, what is particularly intriguing is that the US and the EU, for reasons of path dependence and system design, have chosen different legal paths to achieve the same goal.

Taking a specific angle, **Julie Carlson** focuses on one of the unexpected consequences of the pandemic: the dramatic increase in pet ownership. Beginning in 2019, but continuing through the pandemic, private equity firm JAB undertook a series of acquisitions of specialty and emergency veterinary clinics -- each of which was met by an FTC consent order. While the DOJ's recently revised merger remedies guide suggests that private equity buyers may be preferred to strategic buyers of divested assets in consent agreements, recent rhetoric has been increasingly. Aggressive. The recent concerns antitrust enforcers have raised about private equity, i.e. that it creates market power, facilitates unfair methods of competition and undermines the competitive viability of acquired firms, are, in the author's view, largely unfounded.

Finally, **Laura M. Alexander, Ola Abdelhadi, Brent Fulton & Dr. Richard M. Scheffler** also focus on the large and increasing amount of money under PE management and the huge push by PE into healthcare. This raises concerns and challenges for healthcare policy, but also for competition policy. Emerging evidence about the adverse impact of PE investment in healthcare on competition, prices, quality of care, and patient health is a serious concern. These findings raise the question of how, if at all, antitrust law and antitrust enforcers should treat conduct and deals involving PE owners. While one of the virtues of the antitrust laws is their broad applicability, application of those laws to particular markets and companies is only effective when it is rooted in the realities of competition in those markets and the competitive incentives that those companies face. PE's impact on healthcare reveals significant gaps in the tools and methods for using the antitrust laws to protect competition.

As always, many thanks to our great panel of authors.

Sincerely,
CPI Team

SUMMARIES

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ANTITRUST ENFORCERS INTENSIFY SCRUTINY OF PRIVATE EQUITY DEALS

By Giorgio Motta, Kenneth B. Schwartz, David M. Goldblatt & Michael B. Singer

Over the last several years, private equity firms have faced an increasingly aggressive antitrust enforcement environment, both in the U.S. and abroad. This increased scrutiny has involved more than just skepticism regarding private equity's suitability as a divestiture buyer — the U.S. Department of Justice, Federal Trade Commission and antitrust agencies in Europe are also closely examining private equity acquisition strategies as a whole, general investment incentives, potential filing violations and board interlocks. Antitrust regulators may, however, ultimately have difficulty proving that private equity business models actually result in less competition, as the very business models currently under the microscope, in practice, often result in faster growth, greater innovation and enhanced competitiveness. The bottom line is that, with the right approach, private equity firms can continue to pursue their investment and acquisition strategies despite greater agency scrutiny.

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THE VAMPIRE DIARIES: ANTITRUST SCRUTINY INTENSIFIES AROUND PRIVATE EQUITY

By Vishal Mehta, Megan E. Gerking & David E. Grothouse

The private equity ("PE") industry has experienced extraordinary growth over the past few years. In parallel, antitrust scrutiny of PE by the U.S. enforcement authorities has intensified, with visceral rhetoric from the agencies and Capitol Hill transforming into aggressive action. Most recently, these actions have ranged from strong concessions demanded in PE transactions under review to DOJ letters alleging illegal interlocking directorates and threatening lawsuits. In this article, we explore antitrust focus on PE in the context of broader enforcement trends, highlight recent enforcement activity, preview what dealmakers and practitioners may expect on the horizon, and offer practical tips for navigating this new landscape.

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ANTITRUST'S INCREASINGLY LONG ARM: (MINORITY) PRIVATE EQUITY INVESTORS BEWARE

By Anna Tzanaki

Where do competition, antitrust, and private equity intersect? Once antitrust's favored child compared to strategic buyers, private equity seems to have fallen from competition enforcers' grace. Interestingly, this is part of a broader trend: financial investors in general, from BlackRock to Blackstone, have come into the antitrust spotlight. Being a minority financial investor is no longer reason for antitrust immunity. Economic theory and competition policy have been shifting. Common ownership of small stakes in rival firms by institutional investors, even if passive, can create harm. Rollup acquisitions by active private equity investors may also raise concerns under given circumstances. How is the law reacting to economists' and policymakers' nods? With interest on both sides of the Atlantic. Competition law enforcement signals no empty threats, but rather an eagerness to cover blind spots. What is particularly intriguing is that the US and the EU, for reasons of path dependence and system design, have chosen different legal paths to achieve the same goal. What about politics? It is also here (to stay). Antitrust's recent (over)reach into finance suggests a (renewed) balancing act between competition in product markets and in the market for corporate control, with not only legal and economic underpinnings but also political ramifications.

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PANDEMIC PUPPIES AND PRIVATE EQUITY

By Julie Carlson

One of the perhaps unexpected consequences of the pandemic is the dramatic increase in pet ownership. Beginning in 2019, but continuing through the pandemic, private equity firm JAB undertook a series of acquisitions of specialty and emergency veterinary clinics--each of which was met by an FTC consent order. While the DOJ's recently revised merger remedies guide suggests that private equity buyers may be preferred to strategic buyers of divested assets in consent agreements, the enforcement rhetoric at both the DOJ and the FTC around private equity acquisitions has since become considerably negative. Private equity is a business model innovation that can allow firms to achieve productivity improvements that are not attainable through other forms of corporate organization. In addition to increased scrutiny of private equity, the FTC has also reintroduced prior approval provisions into merger consent agreements — a pernicious combination that risks the productivity gains private equity brings to small firms in highly fragmented industries such as veterinary services. The recent concerns antitrust enforcers have raised about private equity, that it creates market power, facilitates unfair methods of competition and undermines the competitive viability of acquired firms, are largely unfounded.

SUMMARIES

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PRIVATE EQUITY'S ENTRY INTO HEALTHCARE REVEALS GAPS IN COMPETITION POLICY

By Laura M. Alexander, Ola Abdelhadi, Brent Fulton & Dr. Richard M. Scheffler

The large and increasing amount of money under private equity ("PE") management and the huge push by PE into healthcare, raises concerns and challenges for healthcare policy, but also for competition policy. Emerging evidence about the adverse impact of PE investment in healthcare on competition, prices, quality of care, and patient health is a serious concern. These troubling findings raise the question of how, if at all, antitrust law and antitrust enforcers should treat conduct and deals involving PE owners. While one of the virtues of the antitrust laws is their broad applicability, application of those laws to particular markets and companies is only effective when it is rooted in the realities of competition in those markets and the competitive incentives that those companies face. PE's impact on healthcare reveals significant gaps in the tools and methods for using the antitrust laws to protect competition. We conclude, however, that competition laws applicable only to PE are not generally needed; rather, when policymakers, regulators, and enforcers are applying competition laws to PE-owned companies, they need to take account of the unique incentives facing PE managers, the competitive implications of the PE ownership structure, and types of competition concerns that tend to arise surrounding PE deals. In markets that already face limited competition, such as healthcare, the incentives and ownership structures of PE may exacerbate existing competition concerns and anticompetitive impacts, potentially necessitating PE-specific policies.

WHAT'S NEXT?

For November 2022, we will feature an Antitrust Chronicle focused on issues related to (1) **CRESSE Insights**; and (2) **Merger Reforms**.

ANNOUNCEMENTS

CPI wants to hear from our subscribers. In 2022, we will be reaching out to members of our community for your feedback and ideas. Let us know what you want (or don't want) to see, at: antitrustchronicle@competitionpolicyinternational.com.

CPI ANTITRUST CHRONICLES December 2022

For December 2022, we will feature an Antitrust Chronicle focused on issues related to (1) **Privacy & Competition**; and (2) **Digital Markets Act**.

Contributions to the Antitrust Chronicle are about 2,500 – 4,000 words long. They should be lightly cited and not be written as long law-review articles with many in-depth footnotes. As with all CPI publications, articles for the CPI Antitrust Chronicle should be written clearly and with the reader always in mind.

Interested authors should send their contributions to Sam Sadden (ssadden@competitionpolicyinternational.com) with the subject line "Antitrust Chronicle," a short bio and picture(s) of the author(s).

The CPI Editorial Team will evaluate all submissions and will publish the best papers. Authors can submit papers on any topic related to competition and regulation, however, priority will be given to articles addressing the abovementioned topics. Co-authors are always welcome.

ANTITRUST ENFORCERS INTENSIFY SCRUTINY OF PRIVATE EQUITY DEALS

BY GIORGIO MOTTA, KENNETH B. SCHWARTZ, DAVID M. GOLDBLATT & MICHAEL B. SINGER[1]

1 Mr. Motta & Mr. Schwartz are partners with Skadden, Arps, Slate, Meagher & Flom LLP's ("Skadden") Antitrust/Competition Group. Mr. Goldblatt & Mr. Singer are associates with Skadden's Antitrust/Competition Group.

I. INTRODUCTION

For the last several years, across two U.S. presidential administrations and amidst increased focus in the European Union and UK, private equity ("PE") firms have faced a rising tide of aggressive antitrust enforcement rhetoric. In the U.S., the wave of increased scrutiny on PE began in earnest with then-FTC Commissioner Rohit Chopra's statements in 2018 on the suitability of PE firms as divestiture buyers. In the years since, both the Federal Trade Commission ("FTC") and the U.S, Department of Justice ("DOJ") have doubled down on their commitment to put PE in the spotlight — not only with respect to PE's role in the divestiture process, but also for PE's acquisition strategy as a whole, general investment incentives and creation of potentially problematic board interlocks.

In the last few months, both agencies have started to make good on this promise. The FTC has reinstituted prior approval and notice requirements in merger-related consent decrees, requiring PE firms to agree to FTC oversight of certain future acquisitions. Additionally, both U.S. antitrust agencies have recently included new provisions in merger-related subpoenas ("Second Requests") to solicit information on PE incentives and potential board interlocks. And recently, the DOJ has begun issuing letters to PE firms informing them that the agency is investigating potential violations of Section 8 of the Clayton Act, which prohibits board interlocks among competitors.

This call for closer scrutiny of PE firms' acquisition strategy and behavior has echoed across the Atlantic. In the UK, former Chief Executive of the Competition and Markets Authority ("CMA"), Andrea Coscelli, has in recent years highlighted the potential need for antitrust regulators to take account for PE acquirers' business models when assessing the anticipated effects of PE transactions. Coscelli has also specifically flagged the alleged impact of PE leveraging on post-closing competitiveness of target companies as an area that merits further investigation.

Regulators may, however, ultimately face an uphill battle to show that PE business models render portfolio companies less competitive — in practice, such investments often spur innovation and accelerate growth. Indeed, PE firms' industry experience, management skills and expertise generally allow for the efficient operation and growth of smaller companies. Thus, despite increasing regulatory scrutiny, it is unlikely that PE firms will be discouraged from pursuing certain acquisitions (nor should they be). With the right approach, PE firms can continue to execute on their acquisition strategies without raising significant antitrust issues.

II. PE ACQUISITION STRATEGY UNDER THE MICROSCOPE

A. Background

One of the most notable ways in which recent U.S. antitrust regulator interest in PE firms has diverged from past PE-related concerns is the call to more closely scrutinize PE acquisition practices and strategy as a whole. While both U.S. agencies have historically relied on Section 7 of the Clayton Act, the U.S. government's primary merger enforcement tool, to prohibit PE acquisitions that substantially lessen competition, management at both the FTC and DOJ have publicly announced an intention to explore new ways to more closely monitor strings of PE acquisitions in the same industry (so-called "roll-ups") and aggressively investigate strategies that, as DOJ Antitrust Division Assistant Attorney General Kanter put it, are "designed to hollow out . . . an industry and essentially cash out."

In Europe, then-Chief Executive Coscelli co-authored a March 2022 working paper on market resilience that reflected on the circumstances in which the effects of highly leveraged acquisitions (including by PE firms) could or should be considered in merger review. Coscelli specifically suggested that such transactions could render target companies more vulnerable to economic uncertainty and, ultimately, failure, resulting in a lessening of competition. This was preceded by a July 2021 letter by Coscelli to the Chair of the UK Parliament's Business, Energy and Industrial Strategy Committee, which raised questions about the scope of the CMA's regulatory powers to review highly leveraged purchases.

Of course, merger control reviews in the UK, as well as in the EU and many other jurisdictions (the rest of the world, or "ROW"), generally are not driven by "public interest" concerns or (at least ostensibly) political considerations. Instead, antitrust regulators scrutinize transactions on their merits — namely, the effects on competition of any horizontal overlaps and vertical or conglomerate links between the merging parties. In other words, regulatory challenges to transactions must be grounded in legal and economic analysis of whether the proposed transaction is expected to result in significant harm to competition within a reasonably short timeline.

B. U.S.

Despite the fact that PE firms may operate their portfolio companies entirely independently of one another (including, e.g. owning the portfolio companies in separate funds with different ownership horizons and performance goals, employing separate management teams, etc.), PE acquisitions are still subject to Section 7 of the Clayton Act, which prohibits mergers and acquisitions where the effect "may be to substantially lessen competition, or to tend to create a monopoly." As part of a Section 7 inquiry, the FTC and DOJ will consider whether the PE firm owns any portfolio companies that compete with the target or have a vertical (i.e. supply) relationship with the target or its competitors. If so, the FTC and DOJ will evaluate a number of factors to determine whether the transaction is likely to present anticompetitive effects, such as closeness of competition, market shares and the existence of any entry and expansion barriers. This is particularly relevant for PE firms that routinely pursue deals in the same industry. For deals that involve the acquisition of a minority interest in a company that competes with a PE firm's portfolio company, it is also critical to account for Section 1 of the Sherman Act, which prohibits contracts, combinations and conspiracies in restraint of trade.

Additionally, PE acquisitions are subject to the Hart-Scott-Rodino Antitrust Improvements Act of 1976 ("HSR Act"), provided the acquisition meets certain requirements. The HSR Act requires the notification of the transaction to the FTC and DOJ, as well as the provision of certain information about the deal and select documents. It is worth noting that PE acquisitions are occasionally exempt from HSR filing requirements due to the application of certain HSR definitions and other rules that determine whether affiliate funds are considered to be commonly controlled and whether affiliate fund holdings should be aggregated (for example, a newly created fund may not meet the required HSR filing threshold because the fund's holdings are not aggregated with an affiliate fund).

During the initial 30-day waiting period mandated by the HSR Act (and any subsequent extensions due to, e.g. a Second Request), the parties are prohibited from closing the acquisition. Additionally, during this period, the buyer may not begin exercising operational control over the target (known as "gun-jumping"). Violations of any of the above — failing to report a transaction that meets the requisite HSR thresholds, observe the waiting period or observe appropriate gun-jumping restrictions — can subject the buyer to significant liability.

So-called industry "roll-ups" or repeated acquisitions in the same industry are top of mind for the U.S. antitrust regulators, even where those acquisitions are not reportable under the HSR Act. In a May *Financial Times* piece, AAG Kanter was critical of certain PE acquisition strategies that are allegedly "at odds with the competition we're trying to protect" and suggested such behavior would necessitate aggressive enforcement that is "top of mind for me." In a June interview with the *Financial Times*, Chair Khan echoed these statements, noting that the FTC needs to "improve our tools to go after [PE firms] in a more muscular way."

The agencies' increased focus on PE has already had an impact on the competitiveness of PE buyers in certain auction settings, as well as on negotiations of antitrust risk-shifting terms in purchase agreements. For example, it is not uncommon for sellers to insist that buyers — even PE buyers that do not present any or minimal antitrust issues — agree to a "hell-or-high-water" efforts standard or strict "clear market" provisions that restrict a PE firm's ability to engage in certain other transactions. PE buyers are increasingly pushing back on these covenants, however, given the mounting uncertainty and risk of potentially prolonged review and the prospects of unpredictable remedies that may materially and adversely impact other investments they hold.

Not only will the U.S. antitrust agencies more closely scrutinize PE acquisitions in the same industry (including those that are not HSR-reportable), but the agencies are also taking a closer look at whether PE firms are being too cavalier in their observation of filing and operational requirements under the HSR Act. In a June speech at the American Bar Association's Antitrust in Healthcare Conference, Antitrust Division Deputy Assistant Attorney General Andrew Forman flagged that the DOJ had recently become aware of "HSR filing deficiencies in the private equity space" and suggested that PE firms were "not taking seriously enough their obligations under the HSR Act." These statements come on the heels of reports that the antitrust agencies are evaluating pre-merger notification forms to enhance disclosure requirements and require merging parties to provide more information to the agencies up-front. Additionally, in September 2020, the U.S. antitrust agencies announced proposed changes to the HSR process that would greatly expand PE reporting obligations, and potentially slow down the ability of PE firms to quickly prepare and file HSR notifications.

C. ROW

This increased scrutiny of PE transactions is also likely to affect merger review processes outside of the U.S. In the UK, if the CMA has concerns about highly leveraged transactions in sensitive markets, it may be less inclined to grant informal regulatory clearance through the use of so-called "briefing papers," short letters to the authority informing them of the transaction and explaining why it does not raise antitrust concerns.

The CMA typically reviews the information provided in the letter for a period of 2-4 weeks and then either confirms that the authority does not have any further questions (i.e. informal clearance) or calls the transaction in for a full review. The CMA may more frequently require that full notifications be submitted, which would significantly lengthen the review timeline from a few weeks to several months (including, at a minimum, pre-notification interactions lasting a few months followed by a minimum of 40 working days for the formal review period).

Similarly, the European Commission ("EC") may find itself less inclined to permit the use of so-called "short" form notifications, which provide significantly less information and are less burdensome for the parties to prepare than the standard "full" versions of the EU merger control filings. This is especially true for bolt-on PE transactions that may create (albeit limited) overlaps or vertical links between certain PE portfolio companies and the target. Permission to notify transactions in the EU using the short-form submission is at the EC's discretion and is largely based on the parties' market shares in the relevant markets and segments. Thus, increasingly concentrated PE investments may mechanically lead to fewer short-form notifications.

III. CONTINUED AGENCY SKEPTICISM OF PE DIVESTITURE BUYERS

A. Background

It is not uncommon for PE firms to find themselves in an auction process for assets that are being sold pursuant to a merger-related divestiture (either in connection with a formal remedy or in a "fix-it-first" scenario). Whether PE firms are a suitable buyer for these divestiture assets, however — due, in large part, to a perception that PE financial incentives may not align with the promotion of competition — has been a hot-button issue for a number of years. The FTC has not been shy in its criticism of PE firms as divestiture buyers, as evidenced by then-Commissioner Chopra's commentary on PE buyers in the Linde/Praxair merger. The DOJ, for its part, has — as recently as 2020 — recognized the potential benefits of PE buyers. That said, the current DOJ administration seems to have picked up the FTC's mantle, questioning PE incentives that may degrade the competitive viability of the purchased business.

B. U.S.

In recent years, both the DOJ and FTC have issued formal guidance on the merger remedies process and the characteristics of a suitable divestiture buyer. The DOJ's Merger Remedies Manual, published in 2020 (though just recently declared inactive and withdrawn by the DOJ), notes that the DOJ's approval of a divestiture buyer is based on three core tests: (1) the divestiture must not create an independent antitrust issue, (2) the divestiture buyer must be incented to use the divestiture assets to compete in the relevant market and (3) the DOJ must be satisfied that the divestiture buyer has the requisite sophistication, industry experience and financial ability to effectively compete with the assets over the long term. Importantly, the DOJ guidance specifically notes that "[t]he Division will use the same criteria to evaluate both strategic purchasers and purchasers that are funded by private equity or investment firms," and specifically references the FTC's 2017 merger remedies retrospective that recognized the reasons why, in certain cases, a PE buyer may be preferable to a strategic purchaser.

The aforementioned FTC merger retrospective, officially entitled The FTC's Merger Remedies 2006-2012, offers insight into how the FTC evaluates potential divestiture buyers. The study notes that, historically, strong divestiture buyers were "familiar with the market, dealt with many of the same customers and suppliers, had developed thoughtful business plans with realistic financial expectations and sufficient backing, and were well received by market participants." The FTC specifically highlighted a proposed buyer's "commitment to the market" (essentially, a buyer's commitment to compete with the asset and likelihood of success), as well as a buyer's financial capabilities, including how it plans to finance the deal and grow the business. As noted above, the FTC retrospective "revealed that there were cases where the buyer's flexibility in investment strategy, commitment to the divestiture, and willingness to invest more when necessary were important to the success of the remedy," whereas "there were cases where a buyer's lack of flexibility in financing contributed significantly to the failure of the divestiture."

In contrast with the above apparent receptiveness to PE buyers, the FTC has, over the last several years, maintained a skepticism when it comes to PE firms' role in the remedy process. In a much-publicized statement on the Linde/Praxair merger in 2018, then-FTC Commissioner Chopra criticized the approved remedy as not going far enough to "safeguard against risks often posed by the private equity buyer interest in the divested assets, as well as the level of debt financing and investment horizons involved." Commissioner Chopra specifically questioned whether the financing or governance structure would hamstring future investments or incentivize a quick flipping of the asset that would ultimately reduce competition. This concern is reflected in the FTC's recommitment (under Chair Khan and Bureau of Competition Director, Holly Vedova, both of whom worked closely with Commissioner Chopra during his tenure) to prior approval and notice requirements (of the type implemented in *Prince/Ferro, ANI/Novitium* and other recent decisions) that are designed to protect against the short-term resale of a divested business.

Current DOJ leadership has also raised doubts recently about PE firms' suitability as divestiture buyers. In a June speech at the American Bar Association's Antitrust in Healthcare Conference, Antitrust Division Deputy Assistant Attorney General Andrew Forman called out PE's "undue focus on short-term profits and aggressive cost-cutting" that influence why the DOJ "often looks more favorably on a market participant as a buyer of assets than a private equity firm." Interestingly, former Antitrust Division Assistant Attorney General Delrahim took to The Wall Street Journal in late July to counter these claims that PE investment has a chilling effect on competition.

C. ROW

PE firms face similar issues in the EU, where the agencies have shown a certain reluctance to accept PE firms as divestiture buyers. On the one hand, European regulators' more interventionist approach presents opportunities for PE firms to acquire divested assets as part of third-party transactions requiring structural remedies. On the other hand, these agencies have consistently raised the bar on what constitutes a suitable divestiture buyer. European competition authorities are increasingly requiring divestiture buyer approval prior to clearing the overall divestiture and, by extension, the main transaction. Such conditions — known as upfront buyer requirements (UFB) — can be burdensome on all parties, including the prospective buyer. This is because UFBs require (i) a detailed antitrust assessment of the divestiture's impact on competition and the buyer's ability to take on and compete with the divested business from day one, and (ii) final form transaction documents, which must be approved by the regulator (and sometimes by multiple regulators across continents with potentially divergent approaches) prior to closing of the main deal.

With respect to point (i), PE firms must show that they would be suitable divestiture buyers. This, in turn, entails demonstrating not only that the divestiture will not generate competition issues of its own (e.g. because the PE firm is already present in the relevant space via another portfolio company), but also that the buyer will have the requisite industry experience and expertise to foster the divested business's growth and competitiveness. For these reasons, European competition authorities have occasionally ruled out PE firms as divestiture buyers by for want of industry experience. Regulators may instead favor strategic investors operating in spaces that are adjacent or vertical to the divested business.

IV. INTERLOCKING DIRECTORATES RECEIVING RENEWED ATTENTION

A. Background

Both the DOJ and FTC have expressed a renewed interest in enforcement under Section 8 of the Clayton Act, the primary antitrust enforcement mechanism limiting directors and officers from simultaneously serving as a director or officer of a competing company. This is particularly relevant to PE firms, which may have a particular industry focus or have employees serving concurrently on multiple portfolio company boards. Though not historically a focus for either agency (indeed, when enforced, Section 8 violations were often remedied retroactively with minimal punishment for the offenders), the DOJ and FTC have recently doubled down on their respective commitments to pursue Section 8 violations, with the DOJ stating in multiple forums that it intends to aggressively investigate board interlocks and the FTC including Section 8-focused provisions in Second Requests.

B. U.S.

Section 8 of the Clayton Act prohibits a person from simultaneously serving as a director or officer of competing companies. The purpose of Section 8 is "to nip in the bud incipient violations of the antitrust laws by removing the opportunity or temptation to such violations through interlocking directorates." Section 8 does not require any actual anticompetitive conduct — rather, service itself on the board of directors of two competing companies is *per se* unlawful. The applicability of Section 8 is, however, subject to a number of requirements, including:

1. the companies must be horizontal competitors (based on traditional market definition criteria) and

2. the companies must each have "capital, surplus, and undivided profits" aggregating more than $41,034,000 (this is the 2022 threshold, which is adjusted annually).

Additionally, in order to remove *de minimis* competitive overlaps from the scope of Section 8, certain interlocks are exempt, including where

1. the competitive sales of either company are less than $4,103,400 (adjusted annually),
2. the competitive sales of either company are less than 2% of that company's total sales, or
3. the competitive sales of each company are less than 4% of that company's total sales.

In the last several months, Section 8 enforcement has taken center stage as an enforcement priority for both U.S. antitrust agencies. In an April speech, AAG Kanter noted that the DOJ would be "ramping up efforts to identify [Section 8] violations across the broader economy and will not hesitate to bring Section 8 cases to break up interlocking directors." The following month, AAG Kanter again flagged Section 8 issues as a key focus area for the DOJ in a *Financial Times* interview. At the American Bar Association's Antitrust in Healthcare conference in June, DOJ Antitrust Division Deputy AAG Andrew Forman stated that "to the extent PE investments in competitors leads to board interlocks in violation of Section 8, the division is committed to taking aggressive action." While the FTC has been less explicit in addressing Section 8 enforcement publicly, both agencies have added new Second Request provisions explicitly targeting information necessary to evaluate potential Section 8 issues.

The DOJ's recommitment to Section 8 enforcement has started to result in significant corporate action. In mid-October, the DOJ announced that seven directors resigned from the boards of five companies—across a variety of industries—as a result of DOJ investigations into Section 8 violations. These violations included both "direct" interlocks (where an individual serves simultaneously on the boards of two competitors) and "indirect" interlocks (where representatives of an entity or person serve on the boards of competing firms). Notably, these resignations were the culmination of DOJ investigations that occurred outside of the merger context (and as a result of Staff's efforts to independently seek out and investigate potential interlocks), signaling that AAG Kanter is making good on his prior statements regarding Section 8 enforcement and dedicating agency resources to look into possible violations. Proactively reviewing potentially problematic interlocks before the DOJ comes calling is a very worthwhile endeavor given the current enforcement environment, particularly for PE firms with a specific industry focus.

C. ROW

Outside of the U.S., many jurisdictions apply the "control" test to determine whether an individual or company is acquiring "decisive influence" over another entity. As such, interlocking directorates tend to be less of an immediate issue in ex-U.S. jurisdictions. That being said, a number of jurisdictions do require notifying parties to provide information on interlocking senior management as part of their standard merger notification forms. Appointing the same individuals as board members of a number of portfolio companies operating in the same space may therefore raise increased scrutiny in the relevant jurisdictions.

V. KEY TAKEAWAYS

The next several months will be particularly telling in terms of how U.S., UK and European antitrust enforcers translate rhetoric into action. It is critical, however, that PE firms plan ahead to mitigate against increased scrutiny and consider the following:

- Take a close look at any industry-specific acquisition plans, including initial investments. Antitrust agencies will aggressively scrutinize perceived "roll-ups" and may seek to impose prior approval and notice requirements as conditions for transaction approval.
- Be prepared to proactively address potential agency concerns if vying to be a divestiture buyer, including regarding investment incentives, business plans, industry experience, corporate infrastructure, and appropriate financial support.
- Think carefully when negotiating risk-shifting language in acquisition agreements given increasing agency aggressiveness and unpredictability, including the various obligations the agreement places on the merging parties in light of any substantive antitrust risk the deal poses.
- Observe extra caution when pursuing a transaction in "hot button" industries, including, e.g. tech and healthcare.
- Assess currently held board positions at competing portfolio companies to ensure compliance with Clayton Act Section 8 and other antitrust laws, and proactively remedy any issues.

By planning accordingly, PE firms can continue to pursue their acquisition strategies even in a challenging antitrust environment.

THE VAMPIRE DIARIES: ANTITRUST SCRUTINY INTENSIFIES AROUND PRIVATE EQUITY

BY VISHAL MEHTA, MEGAN E. GERKING & DAVID E. GROTHOUSE[1]

1 Vishal Mehta and Megan Gerking are partners in the Global Antitrust Law Practice of Morrison & Foerster LLP in Washington, D.C. Omar Pringle is a partner in the Mergers & Acquisitions and Private Equity Investments & Buyouts Practices of Morrison & Foerster in New York. David Grothouse is an associate in in the Global Antitrust Law Practice of Morrison & Foerster in San Francisco.

It is no secret that the private equity ("PE") industry has reached extraordinary heights in recent years. The past 18 months have been particularly explosive: buyout values and exit multiples have skyrocketed, fundraising has surged, and PE strategies such as buy-and-build and growth investing have experienced dynamic growth.[2] In spite of recent economic headwinds stemming from factors such as rising inflation, high interest rates, and the war in Ukraine, the industry has remained strong. Its allure has even penetrated the rare air of pop culture royalty, with reality star Kim Kardashian recently announcing the launch of SKKY Partners, a private equity firm focusing on consumer products, hospitality, luxury, digital commerce, and media.[3]

Against this backdrop, antitrust scrutiny of PE by the Federal Trade Commission ("FTC") and the U.S. Department of Justice Antitrust Division ("DOJ") has intensified, as political rallying cries and sharp rhetoric have transformed into enforcement action with real economic consequences. In this article, we explore this transition in the context of broader enforcement trends, highlight recent enforcement activity, and preview what dealmakers and practitioners may expect on the horizon.

I. VISCERAL ANTITRUST ENFORCEMENT RHETORIC

Over the last several years, the chorus of voices calling for greater antitrust scrutiny of PE has grown louder. In July 2019, Senator Elizabeth Warren famously described PE firms as "vampires [that bleed companies] dry and walk away enriched" and "suck value out of the economy."[4] Former FTC Commissioner and current head of the Consumer Financial Protection Bureau, Rohit Chopra (another outspoken critic of PE) previously remarked that "many [PE] funds load companies up with debt and sell off the best assets," which "can kill off competition."[5] In July 2020, Chopra released a statement criticizing roll-ups involving successive, non-HSR-reportable transactions. Focusing on the impact of roll-ups in the healthcare sector, Chopra called out nefarious practices resulting from consolidation, including excessive billing by out-of-network physicians and "body brokering" by opioid treatment centers.[6] More recently, FTC Chair Lina Khan has vowed to take a "muscular" approach to PE enforcement to forestall the "life and death consequences" of PE firms controlling too much of the economy.[7] And, DOJ Antitrust Division head Jonathan Kanter recently declared, "the era of lax enforcement is over, and the new era of vigorous and effective antitrust law enforcement has begun."[8]

The visceral rhetoric calling for heightened scrutiny of PE – seemingly lifted from the pages of a David Cronenberg script – has now coalesced with a major escalation in antitrust enforcement across the board. This is occurring at a time when many PE firms are opting for sector-specific investment strategies, whether through the more recent trend of industry-focused funds, or through longstanding roll-up/add-on strategies at the individual portfolio company level.

II. BROADER ANTITRUST ENFORCEMENT CHANGES IMPACTING PRIVATE EQUITY

The Biden administration, Congress, and the agencies have undertaken significant reforms to merger review that have had a real-time impact on PE. These changes – recently characterized by FTC Commissioner Christine Wilson as "death by a thousand cuts" to the HSR regime – include (1) President Biden's Executive Order calling for a whole-of-government approach to antitrust enforcement;[9] (2) indefinite suspension of early

2 The Private Equity Market in 2021: The Allure of Growth, Bain & Company (March 7, 2022).

3 Kim Kardashian's Newest Business Venture: Private Equity, The Wall Street Journal (Sep. 7, 2022).

4 Elizabeth Warren, *End Wall Steet's Stranglehold on Our Economy*, Medium (Jul. 18. 2019), https://medium.com/@teamwarren/end-wall-streets-stranglehold-on-our-economy-70cf038bac76.

5 Rohit Chopra, Twitter (Jan. 28, 2019).

6 Rohit Chopra, Statement of Commissioner Rohit Chopra Regarding Private Equity Roll-ups and the Hart-Scott-Rodino Annual Report to Congress (July 8, 2020), https://www.ftc.gov/legal-library/browse/cases-proceedings/public-statements/statement-commissioner-rohit-chopra-regarding-private-equity-roll-ups-hart-scott-rodino-annual.

7 Stefania Palma, Mark Vandevelde, and James Fontanella-Khan, *Lina Khan vows 'muscular' US antitrust approach on private equity deals*, Financial Times, https://www.ft.com/content/ef9e4ce8-ab9a-45b3-ad91-7877f0e1c797.

8 Jonathan Kanter, Assistant Attorney General, Antitrust Division, United States Department of Justice, Keyn Address at the University of Chicago Stigler Center: Antitrust Enforcement: The Road to Recovery (April 21, 2022).

9 Exec. Order No. 14036, 86 FR 36987 (2021).

termination for deals that are competitively benign;[10] (3) legislation that will increase HSR filing fees for large transactions;[11] (4) expansion of the scope of Second Requests to cover areas such as impact on labor markets; (5) issuance of "warning letters" cautioning merging parties that agency investigations remain open indefinitely, and they close at their own risk;[12] (5) adoption of a "prior approval" policy requiring parties that enter into settlements to resolve competition concerns to give the FTC veto power over future deals;[13] and (6) a comprehensive reassessment of the Merger Guidelines.[14]

Many of these changes have already impacted dealmaking, particularly transactions involving existing portfolio companies, or where sponsors have multiple investments in the same or adjacent sectors. These impacts include longer deal timetables, the agencies discrediting deal efficiencies, skepticism around the labor market impact of anticipated headcount reductions, and complications in purchasing divestiture assets (not particularly easy for PE in the first place).

III. ENFORCEMENT FOCUS ON HEALTHCARE TRANSACTIONS

While these impacts are seemingly broad-ranging and sector-agnostic, the healthcare sector has been a particular focus of the agencies, foreshadowing how antitrust enforcement in the PE context may unfold in other areas.

On June 3, 2022, in prepared remarks presented at the ABA Antitrust Healthcare Conference in Washington, DC, DOJ Deputy Assistant Attorney (AAG) General Andrew Forman publicly stated that the DOJ is considering "enhancing antitrust enforcement around a variety of issues surrounding private equity."[15] Forman set the stage by pointing to the volume of PE dealmaking in 2021, citing "a record 14,730 deals globally worth $1.2 trillion… that is trillion with a T," adding that healthcare was the second leading sector for PE investments. While acknowledging that "[p]rivate equity can play an important role in our economy," he suggested that "certain private equity transactions and conduct suggest an undue focus on short-term profits and aggressive cost-cutting" that in the healthcare space "can lead to disastrous patient outcomes and, depending on the facts, may create competition concerns."[16]

In addition, Forman referred to testimony from industry stakeholders at healthcare "listening forums" hosted by the Federal Trade Commission and DOJ, describing "firsthand experiences about the effect of consolidation and acquisitions by private equity groups … [such as] fewer caregivers, degradation of care, commoditization of health care services, and increased prices."[17] He also remarked that the DOJ

10 Press Release, Fed. Trade Comm'n, FTC, DOJ Temporarily Suspend Discretionary Practice of Early Termination (February 4, 2021), https://www.ftc.gov/news-events/news/press-releases/2021/02/ftc-doj-temporarily-suspend-discretionary-practice-early-termination.

11 On September 29, 2022, the U.S. House of Representatives passed the Merger Filing Fee Modernization Act of 2022 (H.R. 3843, 117th Cong. § 2 (2022)). The Senate passed a similar bill in 2021, and the Biden Administration expressed its support for the bill. Executive Office of the President, Statement of Administrative Policy: H.R. 3843 – Merger Filing Fee Modernization Act of 2022 (September 27, 2022).

12 See Holly Vedova, Acting Director of the Fed Trade Comm'n's Bureau of Competition, Adjusting merger review to deal with the surge in merger filings (August 3, 2021), https://www.ftc.gov/enforcement/competition-matters/2021/08/adjusting-merger-review-deal-surge-merger-filings.

13 See Press Release, Fed Trade Comm'n, FTC Rescinds 1995 Policy Statement that Limited the Agency's Ability to Deter Problematic Mergers (July 21, 2021), https://www.ftc.gov/news-events/press-releases/2021/07/ftc-rescinds 1995-policy-statement-limited-agencys-ability-deter.

14 Press Release, Fed. Trade Comm'n and Dep't of Justice, Federal Trade Commission and Justice Department Seek to Strengthen Enforcement Against Illegal Mergers (Jan. 18, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/01/federal-trade-commission-justice-department-seek-strengthen-enforcement-against-illegal-mergers.

15 Andrew Forman, *The Importance of Vigorous Antitrust Enforcement in Health Care*, Remarks as Prepared for Delivery, https://www.justice.gov/opa/speech/deputy-assistant-attorney-general-andrew-forman-delivers-keynote-abas-antitrust.

16 *Id.*

17 *Id.*

is analyzing recent competition studies, which he said illustrate the negative impact of certain PE acquisitions in healthcare products and services, including home health care, inpatient services, outpatient services, and pharmaceuticals.[18]

Against this backdrop, Forman highlighted four specific areas of enforcement focus:

1. Roll-Ups: Increased scrutiny of PE "roll-ups" consisting of smaller, often sub-HSR-reportable transactions that may cumulatively reduce competition or create a monopoly over time. Along similar lines, the DOJ is analyzing whether reportable PE acquisitions may violate the antitrust laws by creating or enhancing market power across a stack of technology or other products or services.

2. Incentives: The DOJ is focused on whether PE transactions may chill competition by dampening firms' incentives to act as disruptors or mavericks, and/or causing them to focus on short-term financial gain, rather than innovation or quality.

3. Interlocking Directorates: The DOJ is committed to taking "aggressive action" to enforce Section 8 of the Clayton Act, which prohibits interlocking directorates. Subject to certain exceptions, a prohibited interlock can occur where the same person – or different individuals appointed by the same firm – serve(s) as an officer or director of one or more competing portfolio companies.[19]

4. HSR Deficiencies: Forman also indicated that the DOJ has recently become aware of unspecified "HSR filing deficiencies" relating to PE transactions causing them to "ask themselves whether private equity companies may not be taking seriously enough their obligations under the HSR Act." The agency is considering next steps in these areas.

IV. RECENT ENFORCEMENT – JAB CONSUMER PARTNERS

Less than two weeks after Forman's remarks, on June 13, 2022, the FTC announced it had entered into a consent agreement with JAB Consumer Partners SCA SICA (JAB), a PE owner of two portfolio companies operating veterinary clinics, in connection with its proposed acquisition of veterinary clinic operator SAGE Veterinary Partners, LLC (Sage) for $1.1 billion. The FTC's complaint alleged that the combination would substantially lessen competition in the market for internal medicine, neurology, medical oncology, critical care, surgery, and emergency veterinary services in Austin, Texas; San Francisco, California; and between Oakland, Berkeley, and Concord, California.[20] The settlement requires JAB to divest competing veterinary clinics in Texas and California.[21] In addition, JAB must obtain the FTC's prior approval for any acquisition of a veterinary clinic within 25 miles of its existing clinics in California and Texas for 10 years,[22] and provide 30-day written notice to the FTC of any acquisition of a veterinary clinic within 25 miles of an existing JAB clinic anywhere in the U.S.[23]

18 See, e.g. Laura Alexander and Richard Scheffler, *Soaring Private Equity Investment in the Healthcare Sector: Consolidation Accelerated, Competition Undermined, and Patients at Risk* (May 18, 2021), available at https://publichealth.berkeley.edu/wp-content/uploads/2021/06/AAI-Petris-Private-Equity-Healthcare-Report.pdf; Liu, Tong, Bargaining with Private Equity: Implications for Hospital Prices and Patient Welfare (July 30, 2021) https://ssrn.com/abstract=3896410 (finding that PE buyouts led to "an 11% increase in total healthcare spending for the privately insured in affected markets"). More generally, there is a growing body of scholarship finding that common ownership of minority interests in competing companies can lead to anticompetitive effects. See Fiona Scott Morton and Herbert Hovenkamp, *Horizontal Shareholding and Antitrust Policy*, 127 Yale L.J. 2026 (2018); Jose Azar, Martin C. Schmalz, and Isabel Tecu, Anticompetitive Effects of Common Ownership, 73(4) Journal of Finance 1513 (2018). Other scholars have found "ample empirical evidence that PE funds raise the productivity of the businesses they acquire," with a tendency to decrease marginal costs and increase product quality, and that "blocking acquisitions [by PE funds] may come at the cost of forgoing the reorganization of inefficient firms." Pehr-Johan Norbäck, Lars Persson & Jooacim Tåg, *Private Equity Buyouts: Anti- or Pro-Competitive?*, SSRN Electronic Journal at 2-3 (January 2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3128858. Along similar lines, former DOJ Antitrust Division head Makan Delrahim has warned that aggressive enforcement against private equity firms is "at odds with the economic evidence," as "[a]cademic studies have found that private equity is good for competition…" Makan Delrahim, *Antitrust Attacks on Private Equity Hurt Consumers*, Wall Street Journal, Jul. 31, 2022.

19 Michael E. Blaisdell, *Interlocking Mindfulness*, Competition Matters (FTC Blog) (June 26, 2019), available at https://www.ftc.gov/enforcement/competition-matters/2019/06/interlocking-mindfulness.

20 Complaint at 3-5, *In the Matter of JAB Consumer Partners SCA Sicar et al.*, File No. 211 0140, Docket No. C-4766 (June 13, 2022).

21 Decision and Order, *In the Matter of JAB Consumer Partners SCA Sicar et al.*, File No. 211 0140, Docket No. C-4766 (June 13, 2022).

22 *Id.* at 21.

23 *Id.*

In a statement supporting the action, FTC Chair Lina Khan, joined by Commissioners Rebecca Slaughter and Alvaro Bedoya, opined that such provisions would enable the agency to "better address stealth roll-ups by private equity firms."[24] In addition, Chair Khan issued a scathing rebuke of the private equity business model, which could be read as a policy position on PE M&A moving forward:

> Antitrust enforcers must be attentive to how private equity firms' business models may in some instances distort incentives in ways that *strip productive capacity, degrade the quality of goods and services*, and *hinder competition*. Private equity firms' playbook for purchasing or investing in companies can include tactics such as leveraged buyouts, which saddle businesses with debt and shift the burden of financial risk in ways that can *undermine long-term health and competitive viability*. While private equity firms can support capacity expansion and upgrades, firms that seek to strip and flip assets over a relatively short period of time are focused on increasing margins over the short-term, which can *incentivize unfair or deceptive practices and the hollowing out of productive capacity*. Meanwhile, serial acquisitions or "buy-and-buy" tactics can be used by private equity firms and other corporations to roll up sectors, enabling them to accrue market power and reduce incentives to compete, potentially leading to *increased prices and degraded quality*.[25]

Two weeks later, the FTC announced another settlement with JAB in connection with its acquisition of VIPW, LLC and Ethos Veterinary Health LLC. That settlement also contained a prior approval provision and required JAB to divest veterinary clinics in various metropolitan areas.[26] In the FTC's press release announcing the consent agreement, Holly Vedova, Director of the Bureau of Competition, explained that the agency took action to "prevent private equity firm JAB from gobbling up competitors in regional markets that are already concentrated."[27]

V. AGGRESSIVE ENFORCEMENT AROUND INTERLOCKING DIRECTORATES

Following AAG Andrew Forman's public warning, U.S. antitrust enforcers have been taking aggressive action to discover and eliminate unlawful interlocks under Section 8 of the Clayton Act, with potentially serious consequences for private equity funds.

Section 8 prohibits a "person" from serving simultaneously as an officer or director of competing corporations engaged in commerce in the U.S., where each corporation has capital, surplus, and undivided profits of more than $41,034,000 (adjusted annually).[28] Section 8 has historically been a prophylactic statute intended to prevent antitrust violations by reducing the opportunity for competitors to coordinate decision-making or exchange competitively sensitive information. While the agencies or private plaintiffs may seek injunctive relief or civil damages, the most common remedy has been elimination of the interlock through removal of a conflicted officer or director. Historically, agency enforcement actions and litigated cases have been uncommon, with Section 8 enforcement relying instead on a mix of proactive self-policing and naming-and-shaming. However, this may change in light of the agencies' recent aggressive posture

In September 2021, the FTC adopted a resolution giving staff greater authority to issue compulsory process to investigate "common directors and officers and common ownership."[29] In April 2022, DOJ's Kanter vowed to "ramp[] up efforts to identify [Section 8] violations" and bring enforcement actions.[30] In late September 2022, DOJ began issuing letters to public companies, investors, and individuals, alleging unlawful

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24 Statement of Chair Lina M. Khan Joined by Commissioner Rebecca Kelly Slaughter and Commissioner Alvaro M. Bedoya In the Matter of JAB Consumer Fund/SAGE Veterinary Partners Commission File No. 2110140 (June 13, 20220, 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 citing Eileen Appelbaum & Rosemary Batt, Private Equity at Work: When Wall Street Manages Main Street (2014); Statement of Commissioner Rohit Chopra Regarding Private Equity Roll-ups and the Hart-Scott Rodino Annual Report to Congress (July 8, 2020).

25 *Id*. (emphasis added).

26 Decision and Order, *In the Matter of JAB Consumer Partners SCA Sicar et al*., File No. 2110174, FTC Docket No. C-4770 (June 29, 2022).

27 Press Release, Fed Trade Comm'n, FTC Takes Second Action Against JAB Consumer Partners to Protect Pet Owners from Private Equity Firm's Rollup of Veterinary Services Clinics (June 29, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/06/ftc-takes-second-action-against-jab-consumer-partners-protect-pet-owners-private-equity-firms-rollup-of-veterinary-services-clinics.

28 Section 8 provides a safe harbor where (1) the competitive sales of either corporation are less than $4,103,400 (adjusted annually); the competitive sales of either corporation are less than two percent of that corporation's total sales; or (3) the competitive sales of each corporation are less than four percent of that corporation's total sales. There is also a one-year grace period for resignation if there is change (e.g., corporations becoming competitors) that creates an interlock in violation of Section 8.

29 Press Release, Fed Trade Comm'n, FTC Streamlines Consumer Protection and Competition Investigations in Eight Key Enforcement Areas to Enable Higher Caseload (September 14, 2021), https://www.ftc.gov/news-events/news/press-releases/2021/09/ftc-streamlines-consumer-protection-competition-investigations-eight-key-enforcement-areas-enable.

30 Jonathan Kanter, Opening Remarks at 2022 Spring Enforcers Summit (April 4, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-delivers-opening-remarks-2022-spring-enforcers.

interlocking directorates, citing public filings in support of their claims, and threating legal action if the recipients did not respond within 24–48 hours. The DOJ has sent similar notice to PE private firms, presumably stemming from information provided in HSR filings.

On October 19, 2022, the DOJ announcement that seven board members of five separate companies had resigned in response to DOJ's concerns around potential Section 8 violations.[31] The resignations spanned several industries, including healthcare, aerospace infrastructure, transportation, online educational services, and alternative energy software.[32] In the DOJ's press release, Antitrust Division head Kanter signaled that this was just the beginning, saying "[t]he Antitrust Division is undertaking an extensive review of interlocking directorates across the entire economy and will enforce the law."[33]

VI. KEY TAKEAWAYS

In light of these developments, practitioners and PE dealmakers should note the following:

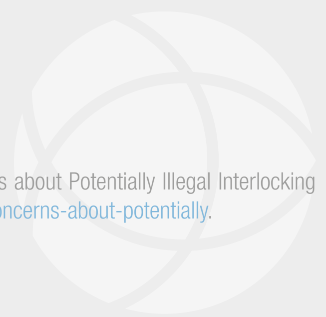
- Private equity dealmaking is increasingly a focus of the U.S. antitrust enforcers. The agencies' recent statements and decisions illustrate that their escalating rhetoric and skepticism towards private equity is culminating in action, with real consequences for M&A in this space, with more headwinds likely on the horizon.

- Private equity firms considering M&A in any segment of the healthcare sector should anticipate greater scrutiny, particularly for deals that may create portfolio overlaps, entail vertical relationships with portfolio companies, target market disruptors, or involve companies that operate in areas that are adjacent to existing holdings. They should also pay close attention to antitrust-related regulatory provisions upfront, including with respect to efforts, cooperation, hell-or-high-water obligations, outside date, reverse termination fees, and responsibilities in the event of receipt of a warning letter from the agencies.

- Private equity teams should pay close attention to the language they use in their deal analyses and investment memoranda and assume they will be examined by antitrust enforcers. Even sparing use of seemingly innocuous terminology that is common in the transaction context can be taken out of context by the agencies, leading to protracted review. Moreover, deal elements such as SG&A headcount synergies, which previously may have been considered procompetitive, may be closely scrutinized for their potential impact on labor.

- Private equity firms should work with antitrust counsel to conduct thorough HSR filing analyses, ensure that HSR filings are complete and accurate, and assess the risk of any potential interlocks stemming from transactions. They should also understand that agencies may utilize filings to gain greater transparency into fund and portfolio structure and M&A pipelines.

- Finally, private equity firms should (1) undertake detailed, proactive review of governance frameworks across portfolios to identify potential Section 8 issues; (2) work with counsel to closely analyze the applicability of Section 8, including possible exemptions and relevant case law; and (3) and implement appropriate compliance safeguards to address existing issues and prevent future violations.



31 Press Release, Dep't of Justice, Directors Resign from the Boards of Five Companies in Response to Justice Department Concerns about Potentially Illegal Interlocking Directorates (October 19. 2022), https://www.justice.gov/opa/pr/directors-resign-boards-five-companies-response-justice-department-concerns-about-potentially.

32 *Id.*

33 *Id.*

ANTITRUST'S INCREASINGLY LONG ARM: (MINORITY) PRIVATE EQUITY INVESTORS BEWARE

BY ANNA TZANAKI[1]

1 Senior Lecturer & Researcher, Lund University Faculty of Law, Sweden; Senior Research Fellow, UCL Centre for Law, Economics & Society, London, UK; Affiliate Fellow, Stigler Center, University of Chicago Booth School of Business, USA anna.tzanaki@jur.lu.se

I. INTRODUCTION

Who's afraid of antitrust enforcers? Big Tech firms active in digital markets have for one tasted their bite. Yet, zooming out of center stage action, less likely suspects are more recently targeted by antitrusters' guns: Big Finance. First, it was diversified passive institutional investors and index funds with small but significant equity holdings in several publicly listed firms competing in the same product market. The "common ownership" story has sent shockwaves across the asset management industry. While the ink on that debate is yet to dry, one thing is becoming increasingly clear: the antitrust floodgates have opened for financial investors.

Where to now? This time antitrust agencies have stretched out their vision aiming at private equity. But when and how come this happened? Is this the sign of antitrust "hybris" reaching beyond its traditional turf, or an epiphenomenon of our times and the rampant "financialization" of the real economy? Where did competition advocates lost, or found, their "raison d'être" by going after active private equity financiers? From BlackRock to Blackstone, is there in the antitrust enforcer's eyes not that much of a difference?

This short article explores the intersections of competition, antitrust and private equity taking the form of minority investments. Section II tracks recent trends in markets and enforcer's tone that brought private equity to the antitrust spotlight. Section III dissects the economic imprint of private equity on financial and product markets. Section III documents the law's recent aggressive stance towards private equity investors in the U.S. and the EU, with increasing merger control scrutiny and parental liability for cartel activity of portfolio companies. Section IV discusses the politics of private equity, given antitrust's double down on finance, as a renewed balancing act between competition in product markets and in the market for corporate control.

II. MARKET TRENDS AND ENFORCERS' RHETORIC – REAL GAME NOW?

Analysts' buoyant glance is fixed on private equity as the industry is booming and reaching record heights for yet another year. According to McKinsey's annual review, private equity has been "once again the highest-performing private markets asset class" in terms of returns on investment while its assets under management (AUM) "reached an all-time high of $6.3 trillion."[2] A Bain report completes this picture noting that "private equity deal value set a new record in 2021 [with] $1.1 trillion in buyouts doubl[ing] 2020's total of $577 billion and shatter[ing] the old record of $804 billion set back in 2006."[3] The favorable economic environment with low interest rates and government stimulus measures to mitigate the impact of the pandemic have only increased the appetite for private equity and alternative investment opportunities, which have consistently outperformed sluggish public markets. At the same time, 2021 has been an exceptional year for global M&A soaring to their highest levels on record with deal value totaling more than $5.8 trillion, 64 percent higher than the year before and the fastest growth rate since the mid-1990s according to Refinitiv. Private equity groups along SPACS have been considered the major force behind this M&A boom.[4]

Could this conspicuous success be at fault for bringing private equity into the antitrust limelight? In part at least, probably so. The size and frequency of M&A transactions involving private equity firms as a parent entity, minority investor or divestiture buyer as well as the significance of the industry itself within the corporate finance and restructuring ecosystem have raised the stakes and as a corollary antitrust enforcers' awareness of new potential concerns and targets. U.S. public officials made this explicit: "competitive overlaps at the investor level" are a relevant factor for the substantive assessment of mergers and acquisitions of partial ownership interests.[5] While expressing reservations about the general "common ownership" theory targeting large, diversified asset managers, FTC's Acting Director Bruce Hoffman noted examples of competition investigations involving private equity firms as "common owners." Indeed, competitive issues arising from holding minority interests in rivals are recognized in practice when such shareholdings are "substantial" (usually above 10 percent) and coupled with "positions of either influence or access to information" (e.g. right to nominate directors).[6]

So, is this a jaw-dropping moment in antitrust history? Well, not really. Control or influence has always been part of an anticompetitive theory of harm. Active investors have always enjoyed their fair share of antitrust glory. But this is not the full story. What makes antitrusters' interest in private equity intriguing is use of a new language. In a recent memo discussing agency priorities, FTC Chairwoman Lina Khan suggested

2 https://www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/mckinseys-private-markets-annual-review.

3 https://www.bain.com/insights/private-equity-market-in-2021-global-private-equity-report-2022/.

4 Wiggins Kaye et al, "Dealmaking Surges Past $5.8tn to Highest Levels on Record" Financial Times (30 December 2021).

5 U.S. Federal Trade Commission, "Antitrust in the Financial Sector - Remarks of Acting Director D. Bruce Hoffman at Concurrences Conference" (2 May 2018).

6 *Ibid.*

"targeting root causes rather than looking at one-off effects," in effect "focusing on structural incentives that enable unlawful conduct" such as those originating from "dominant intermediaries and extractive business models."[7] Yet, surprisingly perhaps, reference to gatekeepers did not single out Big Tech companies but instead private equity whose growing role and "business models may distort ordinary incentives in ways that strip productive capacity" warranting closer antitrust scrutiny.[8]

Cheap talk or too much fuss about nothing? The record shows this language and the zeroing in on private equity is no singular occasion. In an interview, DOJ's Assistant Attorney General Jonathan Kanter became more specific aiming at "roll up acquisitions" by private equity buyout groups whose motive might sometimes be "to hollow out or roll up an industry and essentially cash out," highlighting that "[t]hat business model is often very much at odds with the law and very much at odds with the competition [the agencies are] trying to protect."[9] Speaking with particular reference to the health care sector, where private equity investment is extensive, DOJ's Deputy Assistant Attorney General Andrew Forman further clarified that "certain private equity transactions and conduct suggest an undue focus on short-term profits and aggressive cost-cutting… It is also for these reasons that the division often looks more favorably on a market participant as a buyer of assets than a private equity firm."[10]

No more a place to hide in antitrust land, even for temporary or time-limited financial investors? Apparently not. Are strategic buyers to regain ground in the antitrust battleground and the market for M&A over non-industrial financial investors? If enforcers' threat is credible, for instance as said soon to be reflected in guidelines,[11] then this is indeed a remarkable milestone in the evolution of modern competition policy. Is that all new there is? Almost. FTC's Lina Khan warns against missing the big picture: while "[e]very individual transaction might not raise problems, [concerns may arise] as in the aggregate you've got a huge private equity firm controlling [rivals]."[12] This aggregate approach to serial acquisitions echoes a proposal for amending the HSR merger reporting rules to expand the interpretation of the acquiring "person" to include all entities ("associates") within the same family of funds.[13] Among the reasons for the proposed reforms is concern that potential harm stemming from "common ownership" may go unnoticed.[14]

Is this sensible? Very much so. Enforcement follows reality. Nonetheless, the hidden change that this latter development entails is that antitrust scrutiny will not be limited solely to a "single transaction" subject to merger review but may look at an interrelated group of them. Equally, HSR merger filing will not be judged on the basis of a "single controlling entity," say a parent private equity fund with stakes in rivals, but in aggregate for the whole group of separate funds managed by a private equity firm. The new "person" test for M&A reportability is essentially set to capture all entities under "common investment management," although not "common control" in the HSR sense.[15] The practical difference is rather significant.

What does this mean for antitrust's integrity as a discipline then? Let's turn to economics first and then law for some answers.

III. ECONOMICS TO THE RESCUE – LET'S COMPETE BUT FOR WHAT?

Can economics justify the haunting of private equity and more broadly, the recent unorthodox trajectory of competition policy? Maybe. Or said differently, the answer to this question depends on the context and the framing of the issue at hand. Notably, this question is even more pertinent to the U.S. since: (i) it is perceived as "the home" of financial markets – "Wall Street" is a term of art to describe the finance and investment industry; and (ii) U.S. antitrust law has historically taken a back seat in regulating finance.

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7 U.S. Federal Trade Commission, "Memo from Chair Lina M. Khan to Commission Staff and Commissioners Regarding the Vision and Priorities for the FTC" (22 September 2021).

8 *Ibid.*

9 Stefania Palma & James Fontanella-Khan, "Crackdown on Buyout Deals Coming, Warns Top U.S. Antitrust Enforcer" *Financial Times* (19 May 2022).

10 U.S. Department of Justice, "Deputy Assistant Attorney General Andrew Forman Delivers Keynote at the ABA's Antitrust in Healthcare Conference, 'The Importance of Vigorous Antitrust Enforcement in Health Care'" (Washington, DC, 3 June 2022).

11 Palma and Fontanella-Khan (n 9); Stefania Palma, Mark Vandevelde and James Fontanella-Khan, "Lina Khan Vows "Muscular" U.S. Antitrust Approach on Private Equity Deals" *Financial Times* (9 June 2022).

12 Palma, Vandevelde and Fontanella-Khan (n 11).

13 U.S. Federal Trade Commission, Notice of Proposed Rulemaking, Federal Register Vol. 85, No. 231 (Tuesday, December 1, 2020): Proposed Rules, 77053-77093. See newly proposed definition of "associate" under section 801.1(d)(2).

14 Anna Tzanaki, "Varieties and Mechanisms of Common Ownership: A Calibration Exercise for Competition Policy" (2022) 18 Journal of Competition Law & Economics 168, 194–195.

15 See n 13 above; cf Malika Levarlet, Leo Caseria and Ariel Yehezkel, 'HSR and Antitrust Considerations for Private Equity Firms in M&A Transactions' [2018] CPI Antitrust Chronicle July 2018.

In principle, antitrust law applies to financial services firms – as *firms*, not as *investors*. But in case of conflict, federal sector regulation (e.g. securities laws) displaces antitrust in protecting competition in financial markets due to the "implied antitrust immunity" doctrine.[16] This carveout is premised on a marginal cost-benefit analysis: when antitrust enforcement provides little "added value" to competition and consumers.[17] In addition, the key premises underlying this balance – an important one of which is that the sector regulation serves as an "effective steward of the antitrust function"[18] – are empirical in nature. Thus, potentially subject to change over time and context.

So, is there enough market competition? This is a critical consideration not only for the above regulatory balancing and antitrust enforcement in general, but also for assessing the economic import and impact of financial investors' conduct, in our setting private equity firms. Here, there two levels to consider: i) competition between private equity firms themselves as rivals in the provision of financial investment services, ii) competition between industrial firms in the relevant product market, in which private equity firms acquire shareholdings as part of their portfolio of investments. Competition, or concentration, on both levels matters for how efficiently *markets* will operate. Yet, there is a third level that affects how efficiently *firms* will operate: competition in the market for corporate control.[19]

What is the practical relevance of this distinction? Antitrust has traditionally focused on competitive overlaps *at the market level.* Changing economic conditions such as the increasingly prominent role of institutional investors and private equity have forced competition policy and enforcement to shift its look to financial intermediaries as common investors in rival firms and thus start looking at competitive overlaps *at the investor level*. Accordingly, antitrust is now concerned and estimates not only concentration in the relevant market but also due to common shareholding.[20] As regards the third level, i.e. competition among (financial or strategic) bidders for the control of companies through M&A transactions aiming at improving managerial efficiency, this has been left out of antitrust's purview.[21]

The logic being that this latter competition may produce substantial benefits but primarily in the corporate governance of firms. In other words, the "consumers" that are protected by the competitiveness of this market, providing a solution to the problem of "separation of ownership and control," are the company's shareholders.[22] Given the focus on the *internal* affairs and constituencies of firms, it is understandable then why the market for corporate control is subject to regulation by corporate and securities laws rather than antitrust, which is interested in *external* market effects.[23]

Are private equity and common ownership changing this equilibrium? Probably but quietly so. The private equity market is said to have helped reinvent the "market for corporate control," redefining it as competition between "financial" and "strategic" buyers.[24] This is competition whose players are not active within one and the same industry. It is competition between different organizational forms – a territory more familiar to organizational law rather than antitrust. Product market competition (market power) may influence the choice of organization form,[25] but so may a desire to increase efficiency by reducing governance costs (transaction cost economizing) even absent technological synergies.[26] One such organizational efficiency rationale would be enhancing the efficiency of management in an effort to minimize agency costs and improve firm performance. From this perspective, it is no accident that private equity has been warmly embraced by economists who perceived it as a new model of "organizational innovation driven by the rebirth of 'active investors'" solving the perennial principal-agency problem plaguing large public corporations.[27]

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16 Samuel N. Weinstein, "Financial Regulations In The (Receding) Shadow Of Antitrust" (2019) 91 Temple Law Review 447.

17 Abbott B. Lipsky and others, "The U.S DoJ Antitrust Division Public Roundtable Series on Competition and Deregulation, First Roundtable on State Action, Statutory Exemptions and Implied Immunities - Comment of the Global Antitrust Institute, Antonin Scalia Law School" (2018) George Mason Law & Economics Research Paper No. 18-03; Jacob A Kling, "Securities Regulation in the Shadow of the Antitrust Laws: The Case for a Broad Implied Immunity Doctrine" (2011) 120 The Yale Law Journal 910.

18 Barak Orbach, "The Implied Antitrust Immunity" (2014) Arizona Legal Studies Discussion Paper No. 14-16.

19 Henry G. Manne, "Mergers and the Market for Corporate Control" (1965) 73 Journal of Political Economy 110.

20 José Azar, Martin C Schmalz & Isabel Tecu, "Anticompetitive Effects of Common Ownership" (2018) 73 The Journal of Finance 1513.

21 Edward B Rock, "Antitrust and the Market for Corporate Control" (1989) 77 California Law Review 1365.

22 Fred S. McChesney, "Manne, Mergers, and the Market for Corporate Control" (1999) 50 Case Western Reserve Law Review 245.

23 Anna Tzanaki, "Common Ownership and Minority Shareholding at the Intersection of Competition and Corporate Law: Looking Through the Past to Return to the Future?" in Marco Claudio Corradi and Julian Nowag (eds), *The Intersections between Competition Law and Corporate Law and Finance* (Cambridge University Press forthcoming).

24 Karen H Wruck, "Private Equity, Corporate Governance, and the Reinvention of the Market for Corporate Control" (2008) 20 Journal of Applied Corporate Finance 8.

25 Benjamin E Hermalin, "Heterogeneity in Organizational Form: Why Otherwise Identical Firms Choose Different Incentives for Their Managers" (1994) 25 The RAND Journal of Economics 518.

26 Oliver E Williamson, *The Economic Institutions of Capitalism* (The Free Press 1985); Oliver E Williamson, "Strategizing, Economizing, and Economic Organization" (1991) 12 Strategic Management Journal 75.

27 Michael C Jensen, "Eclipse of the Public Corporation" (1989) *Harvard Business Review*.

Nonetheless, antitrust is already "sneak peeking" into the market for corporate control at the stage of considering remedies in M&A transactions and specifically when deciding suitable divestiture buyers. Often competition agencies prefer private equity buyers of divested assets to resolve concerns related to a proposed acquisition: taking into account the likely long-term viability of the divested business as an independent competitive force following the financial investor's exit and the short-term organizational improvements in productivity and performance without adding to existing product market concentration. Further, having "an active PE market can trigger mergers between incumbents in a merger-stable industry" as incumbents are triggered to engage in M&A that would be privately unprofitable but socially beneficial in attempt to prevent private equity firms outbidding them and reorganizing their rivals.[28] Indeed, private equity being a relatively temporary owner and non-strategic buyer has been seen a win-win solution to promote competition and enable beneficial restructuring of firms and markets.

The language used by U.S. antitrust officials signals a striking policy reversal, with merger control review now said to favor strategic buyers (industry rivals) and treat skeptically private equity investors. Is the antitrust world turning upside down, and importantly is it for good reasons? Yes and no. *Common* ownership even of minority shareholding investments in rivals by *active* investors such as private equity firms may lead to counterintuitive insights with profound implications. On the one hand, in an environment of common ownership productive efficiencies or synergies for the merging firms cannot be presumed to be the driver for M&A transactions – thus far a solid principle built in the Horizontal Merger Guidelines of the U.S. and the EU.[29] The motive to merge may instead reflect the potential net gains from common shareholdings in the target and non-merging firms in which the common investors have parallel stakes and which may compensate for any losses incurred by the acquiring firm.[30] In this light, it may be justified that strategic acquirers under common ownership (although favored from an industrial organization point of view in its absence) fall from antitrust's grace when reviewing merger transactions.

On the other hand, common minority ownership of rivals by diversified financial investors, in private or public markets in the absence of larger dominant shareholders in their corporate governance, may make "selective intervention" (that Williamson thought impossible in a standard merger context from an organizational point of view) attainable but in a novel way: due to "effective" partial integration based on "across-firm" *diversification* rather than "within-firm" *integration*.[31] Assuming common investors have some form of partial control even if factual in their commonly held firms, they could intervene only when the net expected gains exceed the costs. As a result, "common ownership could act as a (partial) merger substitute with the additional advantage that "selective intervention" is possible."[32] Seen from this perspective, common ownership by private equity investors may have an organizational efficiency rationale that would suggest a favorable treatment by antitrust and merger control enforcers. At least as a potential credible alternative to a market power motive.

Therefore, in comparative terms financial acquirers may deserve a more friendly attitude vis-à-vis strategic acquirers given a common ownership setting: the former may demonstrate an (organizational) efficiency rationale for the acquisition whereas for the latter a beneficial motivation (productive synergies) may be more doubtful. Anticompetitive effects arising from either additional concentration due to common institutional ownership or due to industrial market consolidation respectively will also need to be compared, in magnitude and likelihood, to draw more concrete conclusions on the overall effects. In short, common ownership complicates significantly not only the substantive effects analysis of mergers and acquisitions but also the assessment of structural remedies and efficiencies. For instance, "out of market" remedies and efficiencies (e.g. corporate governance or capital markets benefits) are not typically credited by antitrust enforcers, however in the presence of common ownership either by private equity or otherwise, these become significant and commonplace.[33]

How to apply this analytical framework to private equity? An economic assessment essentially will need to consider all three levels of competition outlined above – competition in the private equity industry, competition in the relevant product market, and competition in the market for corporate control – rather than just the first two. This means that given the extent and increasing importance of common institutional ownership, antitrust enforcement may not reasonably disregard the market for corporate control as it has consistently done in the past. The integrity of the discipline is threatened more by failing to update its approach rather than by not adhering to the traditional paradigm. Such competition policy updating would reflect changes in the actual ownership and organizational ecosystem and the overall economy.

As regards the specific effects of private equity buyouts and investments in rivals, the empirical evidence is mixed. These will hinge on the particular market and other factual conditions. Indeed, to assess the impact of private equity acquisitions on consumers, competition au-

28 Pehr-Johan Norbäck, Lars Persson & Joacim Tåg, "Private Equity Buyouts: Anti- or Pro-Competitive?" (23 February 2018) https://papers.ssrn.com/abstract=3128858.

29 José Azar & Anna Tzanaki, "Common Ownership and Merger Control Enforcement" in Ioannis Kokkoris & Claudia Lemus (eds), *Research Handbook on the Law and Economics of Competition Enforcement* (Edward Elgar Publishing 2022).

30 Miguel Antón et al, "Beyond the Target: M&A Decisions and Rival Ownership" (2022) 144 Journal of Financial Economics 44.

31 Tzanaki, "Varieties and Mechanisms of Common Ownership" (n 14) 221.

32 *Ibid.*

33 Azar & Tzanaki (n 29).

thorities need to consider, "in addition to the concentration of markets where acquisitions occur," the "competitive sensitivity" of acquirers: given that "PE-owned facilities exhibit greater competitive sensitivity, [they] compet[e] more aggressively when competitive incentives are strong and exploit market power more aggressively when competitive incentives are weak."[34] Yet such high powered incentives may prove counterproductive in industries such as healthcare where quality is not only an important competitive parameter but also of special public policy relevance.[35] At the same time, some studies find that private equity may have beneficial effects, especially for smaller and capital constrained firms, under tough economic conditions (e.g. credit, pandemic or crisis).[36] Further, the effectiveness and efficiency of antitrust enforcement will also matter for determining whether private equity may be of pro- or anticompetitive nature.[37] Closer scrutiny of private equity may thus be justified depending on the specifics, but a case-by-case analysis will need to be conducted.[38]

IV. LAW FIXED ON DIFFERENT MEANS – WITH GREATER POWER COMES MORE SCRUTINY?

To what extent does the law follow along these economic insights or the public officials' warning statements? Antitrust enforcers seem to walk the talk as experience shows. Heightened scrutiny and liability of private equity is a fact of antitrust enforcement practice both in the U.S. and the EU. Notably, such enforcement action is observed not only for full acquisitions or wholly owned subsidiaries but also regarding minority investment interests. What is particularly interesting, however, is that the two jurisdictions pursue this task by using different antitrust tools and legal pathways. More specifically, in their pursuit of common *minority* ownership of rivals, U.S. agencies rely on their broad and flexible merger control jurisdiction (under Section 7 Clayton Act)[39] whereas European authorities have chosen as of late to extend the parental liability doctrine (under Article 101 TFEU) to private equity firms.[40]

Really? Oh yeah. How come? There is a long and quirky history of antitrust enforcement against minority shareholdings across the Atlantic. The very term minority shareholdings implies that the equity positions held are "non-controlling": typically, when the ownership stake in the firm is less than 50 percent of its equity capital, absent special circumstances, this entails having less than 50 percent of the voting rights.[41] So no "legal control" or the ability to exercise "decisive influence" over the company, using the legal jargon applying in U.S. antitrust and EU competition law respectively. In the U.S., legal control is key to determine the scope of the "Copperweld immunity" doctrine pursuant to which a parent and a subsidiary company, or other affiliate sister companies controlled by the parent, cannot be found to conspire with each other in violation of Section 1 of the Sherman Act. Such group of companies is considered a "single economic unit" in the eyes of U.S. antitrust law. In the EU, we have a similar "single economic entity" doctrine to determine the number of economic actors liable for the application of EU competition law. Furthermore, we use the "decisive influence" criterion to capture and scrutinize mergers under the EU Merger Regulation (Article 3 EUMR) but also to assign intra-group liability in case of violation of Article 101 TFEU (the equivalent of Section 1 of the Sherman Act). As a rule, both the test of legal control and decisive influence translate in plain terms as having majority ownership and control rights. Hence, when companies come under *common majority* ownership and common control, we scrutinize them as *ex ante* under merger rules and we immunize them from

34 Ashvin Gandhi, YoungJun Song & Prabhava Upadrashta, "Private Equity, Consumers, and Competition" (12 June 2020) https://papers.ssrn.com/abstract=3626558.

35 Atul Gupta et al, "Does Private Equity Investment in Healthcare Benefit Patients? Evidence from Nursing Homes" (NBER Working Paper No 28474, February 2021); Rohit Pradhan and others, "Private Equity Ownership of Nursing Homes: Implications for Quality" (2014) 42(2) Journal of Health Care Finance; Richard M Scheffler, Laura M Alexander & James R Godwin, "Soaring Private Equity Investment in the Healthcare Sector: Consolidation Accelerated, Competition Undermined, and Patients at Risk" (18 May 2021) https://petris.org/soaring-private-equity-investment-in-the-healthcare-sector-consolidation-accelerated-competition-undermined-and-patients-at-risk/.

36 Steven J Davis et al, "The (Heterogenous) Economic Effects of Private Equity Buyouts" (2019) NBER Working Paper 26371; Shai Bernstein, Josh Lerner & Filippo Mezzanotti, "Private Equity and Portfolio Companies: Lessons from the Global Financial Crisis" (2020) 32 Journal of Applied Corporate Finance 21; John Gilligan & Timothy Galpin, "Rethinking the M&A Process: Learning Private Equity's Secret to Outperforming Corporate Strategic Acquirers" (2022) 50 Strategy & Leadership 21.

37 Norbäck, Persson & Tåg (n 28).

38 Cf U.S. Department of Justice (n 10).

39 James A. Keyte & Kenneth B. Schwartz, "Private Equity and Antitrust: A New Landscape" (2016) 31 Antitrust 21; Kara Kuritz & Matthew Wheatley, "An Antitrust Roadmap for Private Equity Investment" (2020) 34(3) Antitrust 70. Seminal recent cases include In the Matter of *Red Ventures* Holdco and Bankrate (2018): https://www.ftc.gov/legal-library/browse/cases-proceedings/1710196-red-ventures-holdco-bankrate-matter; In the Matter of *ValueAct* (2016): https://www.justice.gov/atr/case/us-v-va-partners-i-llc-et-al; In the Matter of *Third Point* (2015): https://www.ftc.gov/news-events/news/press-releases/2015/08/third-point-funds-agree-settle-ftc-charges-they-violated-us-premerger-notification-requirements; In the Matter of TC Group, LLC., Riverstone Holdings LLC, Carlyle/Riverstone Global Energy and Power Fund II, LP, and Carlyle/Riverstone Global Energy and Power Fund III, LP ("*Kinder Morgan*") (2007): https://www.ftc.gov/legal-library/browse/cases-proceedings/0610197-tc-group-llc-riverstone-holdings-llc-carlyleriverstone-global-energy-power-fund-ii-lp.

40 Vasiliki Fasoula, "Extending the Presumption of Decisive Influence to Impute Parental Liability to Private Equity Firms for the Anticompetitive Conduct of Portfolio Companies" (2021) 4 Nordic Journal of European Law 101.

41 Annex I "Economic Literature on Non-Controlling Minority Shareholdings ('Structural links')" to European Commission, Staff Working Document, "Towards More Effective EU Merger Control," SWD(2013) 239 final, para 19.

ex post antitrust liability for anticompetitive agreements among several actors as they are (to become) one entity – one unified *economic* entity under common management regardless of whether consisting of more separate *legal* entities.

Antitrust law counts "economic units" so to say. This is the basic principle. At this high level, it is all simple and clear, and U.S. and EU competition rules are congruent and consistent. But there are a few complications. One relates to the "intra-group" liability of affiliates for violations of other companies within the same business group, the second relates to "non-controlling" minority shareholdings. Under the so called "parental liability" doctrine, the EU competition law regime can impose vicarious (strict) liability on parent companies for violations of their subsidiaries, simply because they are part of the same economic entity, and the former are in a formal position to control the latter. In the EU, there is in fact a rebuttable presumption for such parental liability in case of wholly owned or wholly controlled subsidiaries. The latter legal principle was in fact recently established in a case involving a private equity firm as a parent, which held the majority (but not all) of the share capital but the totality of voting rights in the subsidiary.[42] Despite the technicalities and its practical significance, no major surprise lurks in this extension of the presumption.

What is most striking is that in *Goldman Sachs* the European Commission and Courts went one step further: parental liability may be also be established as a matter of fact even when the parent is a private equity firm that only holds a *minority ownership* interest in the subsidiary but actually exercises decisive influence over it *as a general matter*. A finding of actual control automatically implicates parental liability as the parent and the subsidiary are considered to form a single economic unit. Direct involvement in the subsidiary's commercial management relating to, or awareness of, the subsidiary's antitrust infringement is not necessary. What is required is only that overall the parent is found to exercise decisive influence over that company's business decisions.[43] For a finding of *actual* (and not presumptive) decisive influence, therefore, rather than merely relying on the (full) level of ownership or voting rights, EU authorities need to take into consideration "*all* the relevant factors relating to the economic, organizational and legal links which tie the subsidiary to the parent company" including both formal and informal relationships such as personal links.[44] Importantly, the EU Courts confirmed that the Commission's conclusion also applied in the post-IPO period in that same case, when the private equity parent had reduced its previously majority ownership-control position to a minority equity stake. [45]

Breaking news in other words for private equity whose business as usual is having minority shareholdings in industrial firms whose governance and operations seek to influence. The Rubicon has been crossed? Hell yeah! The circumstances of the Goldman Sachs case,[46] where this principle was set, were indeed particular, among others because the parent private equity firm, albeit a minority financial investor, in practice had adopted a business strategy and conduct that approximated that of a strategic acquirer-owner. According to the Court, its governance rights and levels of influence went beyond those normally enjoyed by minority shareholders to protect their financial interests.[47] The particularities of the case notwithstanding, this now stands as active EU law, and the precise limits of the principle are to be tested. Private equity firms cannot hide behind their formalistic labelling as financial investors. They may well be exposed to parental antitrust liability as long as they exercise actual control over subsidiaries. This ultimately remains a factual question. "Substance over form" is the take-home message signaled by EU authorities.

In the U.S., by contrast, this is plainly unthinkable given the current structure of antitrust law as influenced by corporate or organizational law. Under U.S. antitrust law if anything there is a presumption against parental liability for violations of its subsidiaries, even if wholly owned: a separate legal entity or "person" cannot be held vicariously liable for actions of another, even a parent company may only be found to be personally and directly liable when it has active participation in the infringement but not based on the mechanistic application of the "legal fiction" of control. The strong principle of separate "legal personhood" in corporate law, which prevents piercing the corporate veil in all but exceptional cases, carries over in antitrust law. In fact, U.S. antitrust law is addressed to "persons," both physical and legal, whereas EU competition law is targeting "undertakings," i.e. only business economic actors but not actual persons. These fundamental structural and contextual differences in the antitrust laws of the two jurisdictions may partially explain the different emphasis and application of the rules on parental liability. The latter requires more than legal control in the U.S. while in the EU *de facto* control based on minority shareholding may suffice. Having said that, a notable development observed during private antitrust enforcement litigation involving a parent private equity firm whose subsidiary has been accused of antitrust violations is that U.S. courts may not be so formalistic either anymore: in *Packaged Seafood*,[48] the court did not immediately dismiss a private claim against the private equity owner which may indicate some flexibility in interpretation as to whether the private equity parent went

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42 Case T-419/14 The Goldman Sachs Group, Inc. v European Commission [2018] ECLI:EU:T:2018:445; confirmed on appeal by the European Court of Justice, Case C-595/18 P The Goldman Sachs Group Inc. v European Commission [2021] ECLI:EU:C:2021:73.

43 Case T-419/14 The Goldman Sachs Group, Inc. v European Commission [2018] ECLI:EU:T:2018:445, para 152.

44 *Ibid*, para 82.

45 *Ibid*, para 137.

46 See n 42 above.

47 Case T-419/14 The Goldman Sachs Group, Inc. v European Commission [2018] ECLI:EU:T:2018:445, para 132.

48 In re Packaged Seafood Products Antitrust Litigation, 338 F. Supp. 3d 1118 (S.D. Cal. 2018).

beyond "activities that […] are consistent with the parent's [financial] investor status.[49] Again, the factual details of the case here may matter but arguably signs of approximation between the EU and the U.S. may be seen.

What about the second complication? The EU and the U.S. have historically approached differently cases of potentially anticompetitive "non-controlling" minority shareholdings. Although the two regimes have evolved, they continue to do so. The reason has been distinct structural limitations in the law of each jurisdiction that in practice favored certain antitrust tools and provisions over others. Given the above doctrinal limits and generally more demanding legal requirements in applying Section 1 of the Sherman Act, U.S. antitrust enforcement has pursued minority ownership interests that raised antitrust concerns under its merger control laws. Compared to the EU and other jurisdictions, the U.S. merger control regime is the most far reaching as it relies on a flexible "effects-based" test to capture and challenge M&A transactions.[50] The Horizontal Merger Guidelines have a separate section devoted to "partial acquisitions" which explicate that minority shareholdings may be subject to enforcement depending on their effects in each case if they: i) enable the acquirer to *influence* the target's conduct, ii) alter the acquirer's *incentives* to compete, or iii) provide access to the target's competitive sensitive *information*.[51] While there is a "solely for investment" exemption from substantive liability and merger filing for shareholdings up to 10 percent, this requires absolute passivity and any *ex post* action aiming to influence the target (e.g. board seats, nominating directors, soliciting proxies) will be construed as contrary to the alleged *ex ante* passive intent. This is so even for financial investors, which are not excused from exposure to liability unless completely passive.[52] Hence, the exemption may have little practical relevance for private equity investors that seek to follow active investment strategies.

In short, any form of *de facto* control (sole or joint) or even pure financial interests that may be found likely to change the parties' structural incentives and conduct post-merger may be liable under Section 7 of the Clayton Act. As long as there is a credible theory of harm and sufficient evidence to show effects, U.S. merger law is malleable in its application. Arguably, even "diffuse" common minority shareholdings in rivals held by passive institutional investors may be subject to merger control enforcement based on their aggregate anticompetitive effects assuming those common investors-shareholders have joint de facto control in their commonly held portfolio firms.[53] In this light, threats by U.S. antitrust enforcers that they may go after "serial" or "roll up" acquisitions of competitors in concentrated markets by private equity firms, as a potentially problematic business strategy in case of cumulative anticompetitive effects, should not be read as an empty threat or necessarily be taken lightly. One interpretation of this policy pronouncement could be that the law is adapted to catch up with new emerging finance and industry realities.

In the EU, on the other hand, a similar pronouncement would be a dead letter or simply unrealistic. EU merger control is strongly rooted around the concept of "decisive influence," a legal criterion that is inherently more formalistic compared to an economics-based "effects" test such as the one under U.S. merger law. While M&A transactions including minority shareholdings that give rise to sole de facto control may be captured under the EUMR, joint *de facto* control in particular by common financial investors is all but unlikely to be found to amount to decisive influence according to the implementing guidelines explaining the scope of the EU merger rules.[54] Thus, unlike the U.S. and other merger control regimes, there is a formalistic control jurisdictional threshold embedded in the EUMR constraining its application to "non-controlling" minority shareholdings of strategic or financial acquirers. But the EU story has a twist. When one looks to history before the adoption of the pan-European merger control system, EU authorities had actually made aggressive use of Article 101 TFEU to scrutinize minority shareholdings that although formally not *controlling* could serve as an instrument for *influencing* the target's conduct.[55]

In the pre-EUMR time, controlling majority acquisitions could be liable under Article 102 TFEU whereas non-controlling minority acquisitions could be scrutinized under Article 101 TFEU. That meant that minority shareholdings that gave rise to *de facto* control (influence) but were not completely passive need not go unchecked. That flexible and creative EU competition law enforcement era belongs though to the history books, as the Commission had to commit to give up its jurisdiction under Articles 101 and 102 TFEU that operated as a *de facto* merger statute in order to convince Member States to agree to adopt an EU-wide merger control regime.[56] One thing to note from the limited case law from the pre-EUMR era, however, is the remedies that the Commission requested to eliminate concerns while "settling" a case: in *Philip Morris*,[57] EU

49 Colin R. Kass & David Munkittrick, "Private Equity in the Antitrust Crosshairs" *Financier Worldwide* (September 2022) https://www.financierworldwide.com/private-equity-in-the-antitrust-crosshairs.

50 Tzanaki, "Varieties and Mechanisms of Common Ownership" (n 14) 193.

51 U.S. HMG 2010 §13.

52 Kuritz & Wheatley (n 39); Levarlet, Caseria & Yehezkel (n 15).

53 Tzanaki, "Varieties and Mechanisms of Common Ownership" (n 14).

54 Commission Consolidated Jurisdictional Notice under Council Regulation 139/2004 on the control of concentrations between undertakings [2008] OJ C 95/1.

55 Alec J. Burnside, "Minority Shareholdings: An Overview of EU and National Case Law" (2013) e-Competitions Bulletin N° 56676.

56 Anna Tzanaki, "The Regulation of Minority Shareholdings and Other Structural Links between Competing Undertakings: A Law & Economics Analysis" (Doctoral Thesis, UCL (University College London) 2017).

57 Joined Cases 142 and 156/84, BAT and Reynolds v. Commission [1987] ECR 4487 ("*Philip Morris*").

antitrust enforcers had the parties agree not only to restructure their shareholdings (so that they are not symmetric) and abandon some related governance rights (board representation, limited voting rights), but also to "prophylactic" commitments enabling future administrative control and constraining their future conduct (notification to and prior approval by the Commission in case of any increase of Philip Morris' shareholding in a competitor or its voting rights above 25%).[58] Such are exactly the "novel conditions" or "strict limits" on future acquisitions of competing firms that U.S. antitrust agencies very recently imposed on private equity acquirers in order to approve their proposed transactions.[59] Thus, going back to the time before the EU even had a proper merger control regime, we can find relevant precedent under EU competition law and some similarities to current U.S. merger control enforcement practice. At least as regards the type of remedies imposed, their proportionality is another (case specific) question.

To wrap up, if one abstracts from the technical details and legalese, the substance of the formula employed and its elements to enable antitrust enforcement against minority shareholdings is one and the same: minority ownership plus at minimum *de facto* control, while the possibility of future *ex ante* approval commitments (for further acquisitions) as a prophylactic remedy is not excluded. This latent and perhaps surprising convergence across the Atlantic may allude to and be explained by the same root concerns: a fear of circumventing the law by having present *actual* rather than legal control based on minority shareholdings and a fear of acquiring future *legal* control in or across rivals in an industry in a way that goes unnoticed and unchecked. Another counterintuitive insight follows from the preceding legal analysis set in historical perspective: when it comes to antitrust enforcement against minority shareholdings, control still matters – in fact, it matters quite a lot albeit in different forms, and the law has expanded and adapted to capture and assess that reality accordingly.

Same aims, different ways? Yes. In a sense, both in the U.S. and the EU, with greater power attached to minority shareholdings, even if factual and held by financial investors, greater antitrust scrutiny follows. What is truly fascinating is the different legal rules and doctrines applied to capture any such harmful cases, also when specifically applying to private equity: merger liability for partial acquisitions in the U.S. whereas parental liability of a private equity firm for antitrust violations of any portfolio company over which it actually exercises control even if as a minority shareholder. This very generalized broad picture of juxtaposition between U.S. antitrust and EU competition laws is depicted in the table below.

Jurisdiction / *Scrutiny*	**U.S.**	**EU**
Partial acquisitions (Merger liability)	Minority ownership (*de facto* control-)	Majority ownership (legal control-)
Single economic entity (Parental liability)	Majority ownership (legal control+)	Minority ownership (*de facto* control+)

In that sense, U.S. policymakers are quite on point then when they suggest that it is "common management" rather than formal "common control" one needs to look out for when motivating their proposed reforms of the merger reporting rules, especially given the growing presence of common ownership of rival firms by financial investors. As antitrust enforcement seems to "go global" and break tradition in an effort to close legal gaps, the next big act of the antitrust play is to take place in the U.S. Private equity and common ownership are included as specific topics in the recent request for public comments relating to the ongoing process about potential revision of the U.S. merger guidelines.[60] Any upcoming changes in line with the preceding analysis would not be wholly without ground.

What about the repeatedly professed relative preference of strategic over financial acquirers by U.S. public officials lately? One the one hand, the economic analysis drawn above suggests thinking twice before embarking on such categorical policy revision. On the other hand, a look at the corporate law origins of antitrust points to a practice of treating more favorably mergers between horizontal competitors, which were thought to have a more justifiable corporate "purpose."[61] Perhaps this early U.S. corporate law permissive view on horizontal strategic acquirers reflects what economists describe as the potential of creating "synergies" due to the merger. Yet, industrial organization today universally accepts that horizontal mergers are also the most likely to cause competition harm in concentrated markets; hence, efficiencies and pro-competitive rationales may be more prominent in non-horizontal merger cases. Based on this economic learning, modern antitrust law provides a more

58 Tzanaki, "The Regulation of Minority Shareholdings and Other Structural Links between Competing Undertakings" (n 56) 105-109.

59 U.S. Federal Trade Commission, "Statement of Chair Lina M. Khan, Joined by Commissioner Rebecca Kelly Slaughter & Commissioner Alvaro M. Bedoya Regarding JAB Consumer Fund/SAGE Veterinary Partners" (13 June 2022); In the Matter of *JAB Consumer Partners/National Veterinary Associates/SAGE Veterinary Partners:* https://www.ftc.gov/legal-library/browse/cases-proceedings/2110140-jab-consumer-partnersnational-veterinary-associatessage-veterinary-partners-matter.

60 U.S. Department of Justice and U.S. Federal Trade Commission, 'Request for Information on Merger Enforcement' (18 January 2022) https://www.ftc.gov/policy/studies/submit-comment-merger-enforcement-request-information.

61 Tzanaki, 'Common Ownership and Minority Shareholding at the Intersection of Competition and Corporate Law' (n 23).

favorable treatment of non-horizontal compared to horizontal mergers, essentially reversing the earlier corporate law-based principle for merger scrutiny. To add to these considerations, while a shift in the law may have some theoretical grounding in pre-existing law and modern economics abstracting from everything else, the presence of common ownership as discussed earlier significantly complicates and potentially subverts a simplistic conclusion on this theme.[62] A deeper analysis is required that goes well beyond private equity.

V. CONTROL AND THE POLITICS OF PRIVATE EQUITY – ANTITRUST'S COMING OF AGE OR PROMETHEUS UNCHAINED?

Where are we left and where to go? Adding a dose of politics to the mix, one may think of three narratives of how we reached this moment in antitrust's history and what it may mean for the future. First, the "pragmatist" scenario would suggest that the recent verbal and enforcement attacks on private equity and other institutional investors is no antitrust revolution. It is simply a realigning of the law to ensure it addresses current surrounding reality. It signals antitrust's maturity, updating it to focus on substance over form. Second, the "populist" scenario would ascribe less naïve motives to regulators who may seek to appeal to rhetoric more than science by targeting prominent in size or activism financial investors. The ethos and logos of antitrust could be compromised in order to nurture the pathos of its wide consumer audience. Third, the "anarchist" scenario would foreshadow antitrust's self-directed inflation as a countermovement to the financialization of product markets and take the populistic account to the next level. Disregarding their historical boundaries or its limiting principles, antitrust could be seen to cross into corporate law and governance territory. By intervening in the "market for corporate control" (e.g. in an attempt to prevent private equity investors from influencing corporate management and hence market outcomes),[63] antitrust could take a "pro-manager" flavor as its enforcement could in practice shield executives while targeting (potential) controlling shareholders. Such turn would expose antitrust's and corporate law's radically antithetical aims and policy directions on common themes of interest. To avoid any unprincipled use or misuse of antitrust in this area, a more thorough analysis and rebalancing of policies would be required by going back to first principles.

And now? We can choose which way we may want to go. Modernizing antitrust law and policy to keep abreast of contemporary developments in the changing financial and ownership landscape is imperative to keep it alive. Overdoing it, however, may be a hazardous or life-threatening exercise. Where to start then? A sensible first step would be by antitrust policymakers and enforcers talking to corporate and financial law regulators. Rather than artificial silos and sweeping broad-brush reforms, we need targeted antitrust strategies when real issues of harm may exist in congruence or dialogue with corporate law experts. The aim should be safeguarding competitive markets without endangering competitive companies. It is instructive how old debates come back in vogue with a different glossing. Antitrust started as a (populist) public interest enterprise to tackle an unprecedented wave of mergers and acquisitions and holding structures ("trusts") between competing companies leading to detrimental market outcomes.[64] Common ownership and minority shareholding return us back to that history and the corporate law origins of antitrust.[65] As such, this momentum should not be seen as a threat but be seized as an opportunity for rapprochement of antitrust laws across the Atlantic, in tune with new economic learning, while aiming at increasing cooperation with corporate laws. Politics may be part of that bargain but not all at that.

Let the dice be cast!

62 See n 33 above and surrounding text.

63 Michael C Jensen, 'Corporate Control and the Politics of Finance' (1991) 4 Journal of Applied Corporate Finance 13; Wruck (n 24).

64 *Ibid.*

65 *Ibid.*

PANDEMIC PUPPIES AND PRIVATE EQUITY

BY JULIE CARLSON[1]

1 Associate Director, Schumpeter Project on Competition Policy, Information Technology and Innovation Foundation.

I. INTRODUCTION

One of the perhaps unexpected consequences of the pandemic is the dramatic increase in pet ownership. Nearly 20 percent of U.S. households adopted a pet during the pandemic.[2] Pet ownership increased more in 2020 than over the prior twelve years.[3] The increase in pet ownership has led to a sharp increase in demand for appointments at veterinary clinics and long waits for emergency veterinary services.[4] Over the past ten years or so, private equity firms have increasingly taken an interest in veterinary clinics — bringing needed scale and professionalization of management to a highly fragmented industry.[5] Given the pandemic-induced increase in demand for veterinary services, the increase in private equity acquisitions could not come at a more opportune time.

The Federal Trade Commission ("FTC") has taken note of private equity's interest in veterinary clinics — bringing three enforcement actions in the space of three years, beginning in 2020, against JAB Consumer Partners ("JAB") relating to their acquisitions of specialty and emergency veterinary clinics. Since 2020, the antitrust rhetoric surrounding private equity acquisitions has become increasingly negative with leadership at both the FTC and the Antitrust Division of the Department of Justice ("DOJ") calling for more stringent review of PE acquisitions. Assistant Attorney General Jonathan Kanter has said that the private equity "business model is often very much at odds with the law, and very much at odds with the competition we're trying to protect" while FTC Chair Lina Khan notes that regulators need to "improve our tools to go after [private equity acquisitions] in a more muscular way."[6]

The heightened antitrust scrutiny of private equity acquisitions, as evidenced by the enforcement actions against JAB, appears to be pretextual, furthering an antitrust populist agenda, and is not supported by facts or evidence about private equity. The private equity "roll-up" model, which has borne the brunt of enforcers' ire, can increase productivity at small firms largely through increased scale and synergies between the acquired firms. Targeted enforcement against private equity risks the benefits the roll-up model brings to highly fragmented industries. In addition to increased scrutiny of private equity, the FTC has also reintroduced prior approval provisions into merger consent agreements. On their own, prior approval provisions are problematic but, to make matters worse, these provisions are most burdensome to the small firms that would see the largest productivity gains from the PE roll-up model. The unwarranted attack on private equity combined with the reinstitution of prior approval is particularly pernicious and harms business model innovation and economic growth.

II. FTC ACTIONS AGAINST JAB

Beginning in 2019, JAB undertook a series of acquisitions of specialty and emergency veterinary clinics — each of which was met by an FTC consent order. JAB first sought to acquire National Veterinary Associates ("NVA").[7] NVA was owned by a private equity firm at the time of the proposed acquisition by JAB.[8] In order to resolve competitive concerns with the transaction, the FTC required the divestiture of three clinics to

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2 American Society for the Prevention of Cruelty to Animals, *New ASPCA Survey: Vast Majority of Dogs and Cats Acquired During Pandemic Still in Their Homes* (2021), https://www.aspcapro.org/resource/new-aspca-survey-vast-majority-dogs-and-cats-acquired-during-pandemic-still-their-homes.

3 Debbie Phillips-Donaldson, *Insights on Pet Ownership Changes, Impact on Pet Food*, PETFOODINDUSTRY.com (Apr. 16, 2021), https://www.petfoodindustry.com/blogs/7-adventures-in-pet-food/post/10204-insights-on-pet-ownership-changes-impact-on-pet-food.

4 Jacob Bogage, *Americans Adopted Millions of Dogs During the Pandemic. Now What Do We Do with Them?* Washington Post, Jan. 7, 2022, https://www.washingtonpost.com/business/2022/01/07/covid-dogs-return-to-work/.

5 Deborah Balshem, *PE Firms Still Drooling Over Veterinary Practice Management Space*, FORBES, May 7, 2018, https://www.forbes.com/sites/mergermarket/2018/05/07/pe-firms-still-drooling-over-veterinary-practice-management-space/?sh=2648348078af.

6 James Fontanella-Khan, *Private Equity Moves into the Antitrust Spotlight*, FIN TIMES, May 23, 2022, https://www.ft.com/content/f222e618-dc96-4204-8a27-00e0a9316236; Stefania Palma et al., *Lina Khan Vows 'Muscular' U.S. Antitrust Approach on Private Equity Deals*, FIN TIMES, June 9, 2022, https://www.ft.com/content/ef9e4ce8-ab9a-45b3-ad91-7877f0e1c797.

7 *Compassion-First Owner to Acquire National Veterinary Associates*, TODAY'S VETERINARY BUS. (June 17, 2019), https://todaysveterinarybusiness.com/compassion-first-owner-to-acquire-nva/.

8 Press Release, Ares Mgmt. and JAB Investors, Ares Management Agrees to Sell NVA, the Leading Independent Veterinary Platform, to JAB Investors (June 17, 2019), https://www.businesswire.com/news/home/20190617005249/en/Ares-Management-Agrees-to-Sell-NVA-the-Leading-Independent-Veterinary-Platform-to-JAB-Investors.

MedVet.[9] MedVet is another private equity-backed operator of specialty and emergency veterinary clinics.[10] The consent order, which became final in 2020, contained a prior notice provision requiring JAB's parent, Agnaten, to notify the commission in advance of any future veterinary clinic acquisitions in certain geographic areas.[11]

In 2021, JAB agreed to acquire SAGE Veterinary Partners ("SAGE") — a private equity-backed operator of specialty and emergency veterinary clinics.[12] As with the prior acquisition, the FTC required divestitures to resolve competitive concerns with the transaction. In this case, JAB was required to divest six clinics to United Veterinary Care ("UVC").[13] UVC is a private equity-backed operator of veterinary clinics.[14] In addition to these divestitures, the FTC's order, which became final on August 2, 2022, imposed extensive prior notice and prior approval conditions on both JAB and UVC. The order requires JAB to obtain "prior approval before acquiring a specialty or emergency veterinary clinic within 25 miles of any then-owned JAB-owned clinic *anywhere in California or Texas* [emphasis in original]" despite the relevant geographic areas of concern being limited to the San Francisco Bay area and Austin. In addition to this prior approval requirement, the order also requires JAB to provide prior notice for any acquisition of a "specialty or emergency veterinary clinic within 25 miles of a clinic owned by JAB *anywhere in the United States* [emphasis in original]." The order also requires UVC to obtain prior approval prior to selling any of the assets acquired under the order.[15]

Finally, just weeks after reaching an agreement to acquire SAGE, JAB agreed to acquire Ethos Veterinary Health — a private equity-backed operator of specialty and emergency veterinary clinics.[16] To resolve competitive concerns with this acquisition, the FTC required relief similar to that which was required with the SAGE acquisition. JAB was required to divest three clinics to UVC and two clinics to Veritas Veterinary Partners ("Veritas").[17] Veritas is a private-backed operator of specialty and emergency veterinary clinics.[18] The FTC's order, which is not yet final, imposed similar statewide prior approval requirements for JAB acquisitions in California, Colorado, the District of Columbia, Maryland, and Virginia despite the relevant geographic areas of concern being limited to San Francisco, Denver, the D.C. metro area, and Richmond, VA. The order also imposed a nationwide prior notice requirement on JAB and prior approval requirements on UVC and Veritas.[19]

III. ENFORCERS' CONCERNS ABOUT PRIVATE EQUITY ACQUISITIONS

While the DOJ's recently revised merger remedies guide suggests that private equity buyers may be preferred to strategic buyers of divested assets in consent agreements, the enforcement rhetoric around private equity acquisitions has since become considerably negative.[20] Former FTC Commissioner, now Consumer Financial Protection Bureau Director, Rohit Chopra began raising concerns about private equity acquisitions as early as 2018. He noted in a public statement accompanying the FTC's and DOJ's annual report to Congress on the Hart-Scott-Rodino Act

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9 FTC, *Analysis of Agreement Containing Consent Orders to Aid Public Comment* In the Matter of Agnaten SE, Veterinary Specialists of North America, LLC, and NVA Parent Inc. File No. 191-0160, C-4707 (Feb. 14, 2020), https://www.ftc.gov/system/files/documents/cases/cf-nva_analysis_to_aid_public_comment_-_final.pdf.

10 Press Releases, MedVet, MedVet Secures Investment Supporting Continued Growth in Specialty Healthcare for Pets (July 15, 2019), https://www.medvetforpets.com/news/medvet-secures-investment-supporting-continued-growth/.

11 FTC, *Decision and Order* In the Matter of Agnaten SE, Veterinary Specialists of North America, LLC, and NVA Parent Inc. File No. 191-0160, C-4707 (Apr. 9, 2020), https://www.ftc.gov/system/files/documents/cases/1910160c4707agnatennvaorder.pdf. The specific geographic areas are not listed in the public version of the order.

12 Sarah Pringle, *Chicago Pacific Founders' SAGE Veterinary Goes to NVA for $1.25bn*, PE HUB, June 23, 2021, https://www.pehub.com/chicago-pacific-founders-sage-veterinary-goes-to-nva-for-1-25bn/.

13 Press Release, FTC, FTC Acts to Protect Pet Owners from Private Equity Firm's Anticompetitive Acquisition of Veterinary Services Clinics (June 13, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/06/ftc-acts-protect-pet-owners-private-equity-firms-anticompetitive-acquisition-veterinary-services.

14 Press Release, Nordic Capital, Nordic Capital Partners with United Veterinary Care, Acquiring Atlantic Street Capital's Shareholding in the Fast-Growing U.S. National Group of Primary, Specialty and Emergency Veterinary Practices (Apr. 23, 2021), https://www.nordiccapital.com/news/nordic-capital-partners-with-united-veterinary-care/.

15 FTC, *supra* note 13.

16 Sarah Pringle, *JAB Investors' NVA Buys Ethos Veterinary Health in $1.65bn Deal*, PE HUB, Aug. 16, 2021, https://www.pehub.com/jab-investors-nva-buys-ethos-veterinary-health-in-1-65bn-deal/.

17 Press Release, FTC, FTC Takes Second Action Against JAB Consumer Partners to Protect Pet Owners from Private Equity Firm's Rollup of Veterinary Services Clinics (June 29, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/06/ftc-takes-second-action-against-jab-consumer-partners-protect-pet-owners-private-equity-firms-rollup-of-veterinary-services-clinics.

18 Press Release, Percheron Capital, Veritas Veterinary Partners Launches National Network of Specialty and Emergency Veterinary Hospitals (Mar. 29, 2022), https://percheroncapital.com/news/veritas-veterinary-partners-launches-national-network-of-specialty-and-emergency-veterinary-hospitals/.

19 FTC, *supra* note 17.

20 DOJ, 2020 Merger Remedies Manual (Sept. 2020), 24, https://www.justice.gov/atr/merger-enforcement.

that "many private equity firms commonly employ "buy-and-build" approaches [and] … [t]hrough these strategies, private equity sponsors can quietly increase market power and reduce competition."[21] Outside of health care, where quality is also a concern, antitrust enforcers have identified three main concerns with private equity acquisitions: (1) stealth private equity roll-ups create market power; (2) private equity firms strip productive capacity making it harder to compete and, consequently, may facilitate unfair methods of competition; and (3) private equity saddles businesses with debt and thereby undermines their competitive viability.[22]

Given the competitive concerns raised about private equity , Chair Khan has said that "[r]egulators should be 'sceptical', when private equity funds seek to absorb businesses divested by companies that are merging" noting that this is "a concession often demanded by government agencies in exchange for consenting to a deal that could otherwise stunt competition."[23] However, the skepticism Chair Khan prescribes appears to be largely absent with respect to the recent consent orders against JAB. Neither the proposed complaint nor the analysis to aid public comment in the JAB matters raise concerns about competitive harm due to JAB's status as a private equity firm.[24] Furthermore, in each of the 2022 orders, Khan's Commission required JAB to divest clinics to *another private equity firm*. The FTC's willingness to require divestitures to private equity buyers suggests that concerns raised by enforcers about private equity are pretextual.

The real objection appears not to be to the private equity business model per se but to any business model that increases firm size through mergers or acquisitions. Antitrust populists, including the current leadership of the U.S. antitrust enforcement agencies, decry the political influence of large firms. But instead of advocating for policies that tackle this political influence directly, they seek reforms to antitrust enforcement that aim to limit the economic advantages of these firms, believing that this will translate into political enfeeblement.[25] The current enforcement focus on private equity is no different. As discussed further below, the private equity "buy and build" or "roll-up" model, which involves achieving scale through acquisition, is anathema to the populist worldview which would have the economy populated largely by small independent firms.[26] And as with other proposed antitrust reforms, the skepticism aimed at private equity risks the real benefits associated with the private equity model.

IV. BENEFITS OF THE PRIVATE EQUITY MODEL

At its heart, private equity model is a business model innovation that can allow firms to achieve productivity improvements that are not attainable through other forms of corporate organization. The private equity model addresses two sources of inefficiencies in business operations: (1) separation of ownership and control; and (2) lack of scale.

Inefficiency arising from the separation of ownership and control typically arises in large, public firms. It has been long understood that "[d]ue to weaknesses in the market for corporate control, difficulties in monitoring by dispersed shareholders, problematic incentives of corporate directors, compensation schemes that reward empire building and myriad other reasons, publicly traded firms can be especially prone to

21 Rohit Chopra, *Statement of Commissioner Rohit Chopra Regarding Private Equity Roll-ups and the Hart-Scott Rodino Annual Report to Congress Commission File No. P110014* (July 8, 2020), https://www.ftc.gov/system/files/documents/public_statements/1577783/p110014hsrannualreportchoprastatement.pdf.

22 FTC, *supra* note 13; Lina Khan, *Statement of Chair Lina M. Khan Joined by Commissioner Rebecca Kelly Slaughter and Commissioner Alvaro M. Bedoya In the Matter of JAB Consumer Fund/SAGE Veterinary Partners Commission File No. 2110140* (June 13, 2022), 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.

23 Stefania Palma et al., *supra* note 6.

24 Noah Phillips & Christine Wilson, *Concurring Statement of Commissioners Noah Joshua Phillips and Christine S. Wilson*, JAB Consumer Partners SCA SICAR/SAGE Veterinary Partners, LLC, *File No. 2110140* (June 13, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/2110140C4766NVASAGEPhillipsWilsonConcurringStatement.pdf.

25 Sarah Miller, *End Monopoly Power*, DEMOCRACY J., July 14, 2020, https://democracyjournal.org/magazine/end-monopoly-power/.

26 Sandeep Vaheesan, *Merger Policy for a Fair Economy*, LPE PROJECT, April 5, 2022, *https://lpeproject.org/blog/merger-policy-for-a-fair-economy/*.

value-destroying activities."[27] By taking a public firm private, agency problems associated with the separation of ownership and control may be reduced as the private equity owners take an active role in the management of the firm. To the extent these public-to-private buyouts are focused on long-run profitability and eliminate wasteful spending, they can increase productivity through better management of the firm's assets.

Inefficiency due to lack of scale typically arises in small, private firms. These small firms are less likely to face the agency problems of public firms as the owners are often actively managing the firm, however, their small size may make it more difficult to access capital markets in order to grow the business. An acquisition by a private equity firm, a private-to-private buyout, allows the firm to make investments that increase scale and thereby lower costs and improve productivity. Davis et al. (2021) estimated that productivity at the target firms in private-to-private buyouts increases by nearly 15 percent relative to similar firms that are not backed by private equity.[28]

Private equity firms have continued to innovate and further develop their business model. A recent innovation is the "roll-up" or "buy and build" model. In the roll-up model, the private equity firm makes an initial, typically private-to-private, buyout which serves as a platform to make additional acquisitions in the same or an adjacent industry. The roll-up model has become increasingly popular over the last 20 years. In recent years, about of third of add-on acquisitions (i.e. acquisitions of firms in the same industry as another firm in the private equity firm's portfolio) are part of a roll-up strategy.[29] In addition to the benefits from stand-alone private equity acquisitions, the roll-up model allows for synergies between the acquired firms, additional scale economies, and increased productivity from larger firm size.[30]

The benefits of the private equity roll-up model are readily apparent in the recent roll-ups of veterinary clinics. As noted by the FTC, staffing and obtaining the relevant equipment for veterinary clinics, particularly emergency and specialty clinics, is expensive.[31] Veterinary clinic roll-ups "create efficiencies by offering a standardized package of management, training, and administrative support. Individual clinics … keep their local identities, and resident veterinarians … remain in control of medical decisions."[32] Improved operating efficiency is particularly important at a time "when supply chain bottlenecks are pushing up operating costs" for veterinary clinics. In addition to the supply chain crisis, veterinary clinics are also experiencing a human capital crisis. Acquiring multiple veterinary clinics ensures there are enough veterinarians to cover slack shifts.[33]

V. TARGETED ENFORCEMENT AGAINST PRIVATE EQUITY IS UNWARRANTED

The concerns antitrust enforcers have raised about private equity are largely unfounded. The assertion that private equity firms are engaged in stealth acquisitions that allow them to gain market power neglects that defining a relevant market, a precursor to identifying market power, requires identifying both the relevant product market *and the relevant geographic market*. To the extent that the acquired firms compete in local geographic markets, as do veterinary clinics, as opposed to national geographic markets, the roll-up acquisitions, irrespective of whether they

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27 Steven Davis et al., The (Heterogenous) Economic Effects of Private Equity Buyouts (National Bureau of Economic Research, Working Paper No. 26371, Oct. 2019) 4, https://doi.org/10.3386/w26371.productivity, and job reallocation vary tremendously with macroeconomic and credit conditions, across private equity groups, and by type of buyout. We reach this conclusion by examining the most extensive database of U.S. buyouts ever compiled, encompassing thousands of buyout targets from 1980 to 2013 and millions of control firms. Employment shrinks 13% over two years after buyouts of publicly listed firms – on average, and relative to control firms – but expands 13% after buyouts of privately held firms. Post-buyout productivity gains at target firms are large on average and much larger yet for deals executed amidst tight credit conditions. A post-buyout tightening of credit conditions or slowing of GDP growth curtails employment growth and intra-firm job reallocation at target firms. We also show that buyout effects differ across the private equity groups that sponsor buyouts, and these differences persist over time at the group level. Rapid upscaling in deal flow at the group level brings lower employment growth at target firms.","event-place":"Cambridge, MA","language":"en","note":"DOI: 10.3386/w26371","number":"w26371","page":"w26371","publisher":"National Bureau of Economic Research","publisher-place":"Cambridge, MA","source":"DOI.org (Crossref

28 *Id.* at 20.productivity, and job reallocation vary tremendously with macroeconomic and credit conditions, across private equity groups, and by type of buyout. We reach this conclusion by examining the most extensive database of U.S. buyouts ever compiled, encompassing thousands of buyout targets from 1980 to 2013 and millions of control firms. Employment shrinks 13% over two years after buyouts of publicly listed firms – on average, and relative to control firms – but expands 13% after buyouts of privately held firms. Post-buyout productivity gains at target firms are large on average and much larger yet for deals executed amidst tight credit conditions. A post-buyout tightening of credit conditions or slowing of GDP growth curtails employment growth and intra-firm job reallocation at target firms. We also show that buyout effects differ across the private equity groups that sponsor buyouts, and these differences persist over time at the group level. Rapid upscaling in deal flow at the group level brings lower employment growth at target firms.","event-place":"Cambridge, MA","language":"en","note":"DOI: 10.3386/w26371","number":"w26371","page":"w26371","publisher":"National Bureau of Economic Research","publisher-place":"Cambridge, MA","source":"DOI.org (Crossref

29 Bain & Company, Global Private Equity Report 2019 (Feb. 25, 2019) 37, https://www.bain.com/insights/buy-and-build-global-private-equity-report-2019/.

30 Danny Leung et al., *Firm Size and Productivity* (Bank of Canada, Working Paper No. 2008-45, Nov. 2008), https://www.bankofcanada.ca/wp-content/uploads/2010/02/wp08-45.pdf.

31 FTC, *supra* note 9.

32 Bain & Company, *supra* note 29, at 41.

33 Ross Kelly, *Pandemic Hastens Ongoing Trend in Veterinary Consolidation*, VIN NEWS SERVICE, Dec. 30, 2021, https://news.vin.com/default.aspx?pid=210&Id=10652228.

are financed by private equity, are unlikely to create market power except in very limited cases. The JAB matters demonstrate that these roll-ups create few overlaps.

The FTC's consent orders in the JAB matters required the divestiture of less than 10 percent of the total number of post-merger clinics. Furthermore, even if veterinary clinics compete in a national geographic market, which they clearly do not, that market is unconcentrated. In 2017, the market share of the four largest firms providing veterinary services was 13 percent while the market share of the 50 largest firms was only 22 percent.[34] Consequently, there is no basis for the assertion that "[p]rivate equity firms increasingly engage in roll up strategies that allow them to accrue market power off the Commission's radar" — particularly in the context of veterinary clinic acquisitions.[35]

The assertion that private strips productive capacity and saddles a firm with debt making it harder for the firm to compete and threatening the firm's viability is also unfounded and irrelevant to the antitrust analysis. First, this contradicts the goals of the private equity model. Private equity only earns a return when it sells a firm that is more valuable than when it was acquired. A firm that is not competitively viable is not more valuable. Second, this contradicts the evidence on the viability of firms backed by private equity. Bernstein et al. (2020) studied the performance of private equity-backed firms during the 2008-2009 financial crisis and found that, during the crisis, private equity-back firms invested five to six percent more than similar firms that were not backed by private equity. Private equity-backed firms also experienced a greater increase in their stock of assets in the years following the financial crisis and "were not more likely to go out of business or enter into distress in the post-crisis period."[36]

That these assertions are unfounded further demonstrates that the targeted enforcement to which private equity is now subject is pretextual and is only intended to achieve the political ends of antitrust populists. Unfortunately, slowing the growth of the private equity roll-up model also means slowing the growth of small businesses — many of which benefit from the improved access to credit markets and the professionalization of management practices provided by private equity. When these small businesses are more productive, consumers face lower prices. This is something we should cheer, not discourage, in the current high inflation environment.

VI. PRIVATE EQUITY AND PRIOR APPROVAL

Since rescinding the 1995 Policy Statement on Prior Approval and Prior Notice Provisions in July 2021, the FTC now routinely includes prior notice and prior approval requirements in its consent orders — the 2022 JAB orders are no exception.[37] Holly Vedova, Director of the FTC's Bureau of Competition, stated that "[t]he prior notice and approval provisions [in the JAB/SAGE order] will ensure the Commission has full visibility into future consolidation and the ability to address it."[38] The prior notice requirements, while extensive, may be reasonable in an industry where, due the local nature of markets, small transactions that escape Hart-Scott-Rodino notification thresholds can produce large increases in market concentration. The 2020 JAB order reasonably included such a provision. The prior approval requirements, however, evade the statutory limitations placed on the FTC by Congress and unnecessarily burden both merging parties and divestiture buyers.

Given the extensive prior approval requirements in the JAB orders, future acquisitions in relevant geographic markets completely unrelated to the markets in which the FTC alleged harm are now subject to review by the FTC even if they are not competitively problematic. Furthermore, the burden falls on the parties to demonstrate that their deal is not anticompetitive. This is especially burdensome for small firms as they are least likely to be able to bear the costs associated with heightened review. This has the perhaps not unintended consequence of not just deterring anticompetitive acquisitions but deterring procompetitive acquisitions as well. And as the prior approval provisions also apply to divestiture buyers, it will be harder to find qualified buyers to remedy limited overlaps in otherwise competitively unproblematic transactions.

While the unwarranted attack on private equity and the reinstitution of prior approval each on their own are harmful, the combination of the two is particularly pernicious. The private equity roll-up business model brings scale to inefficient, small firms while prior approval require-

34 U.S. Census Bureau, Economic Census (2017), https://data.census.gov/cedsci/table?q=concentration&n=N0600.00&tid=ECNSIZE2017.EC1700SIZECONCEN. This is the most recent year for which data on concentration are available.

35 FTC, *supra* note 13.

36 Shai Bernstein et al., *Private Equity and Portfolio Companies: Lessons from the Global Financial Crisis*, 32, no. 3 J. APPLIED CORPORATE FIN 21-42 (September 2020), https://doi.org/10.1111/jacf.12416.

37 FTC, *Statement of the Commission on Use of Prior Approval Provisions in Merger Orders* (Oct. 25, 2021), https://www.ftc.gov/system/files/documents/public_statements/1597894/p859900priorapprovalstatement.pdf.

38 FTC, *supra* note 13.

ments are most onerous for the small firms that would benefit most from private equity investment. The combination of these two policies puts the largest productivity gains from the private equity roll-up model at risk and thereby limits business model innovation and economic growth.

VII. CONCLUSION

Two wrongs don't make a right. Heightened antitrust scrutiny of private acquisitions combined with the reinstitution of prior approval requirements risks the productivity gains private equity can bring to small firms in highly fragmented industries. We have seen these productivity benefits over the last century, in industry after industry. This includes hotels, restaurants, hair salons, hardware stores, and others. In short, this happens when firms with a national presence bring scale to previously highly fragmented industries. The potential for productivity gains is readily apparent in the veterinary services industry where most veterinary clinics are still independently operated. Bringing cost-reducing innovation to veterinary clinics is particularly important in the current environment where inflation is high and demand for veterinary services is surging. Antitrust enforcers should throw pandemic pet owners a bone and end this unwarranted attack on private equity.

PRIVATE EQUITY'S ENTRY INTO HEALTHCARE REVEALS GAPS IN COMPETITION POLICY

BY LAURA M. ALEXANDER, OLA ABDELHADI, BRENT FULTON & DR. RICHARD M. SCHEFFLER[1]

1 Respectively, Director of Markets and Competition Policy at the Washington Center for Equitable Growth, Researcher at the Nicholas C. Petris Center of Healthcare Markets and Consumer Welfare, Associate Research Professor of Health Economics and Policy at UC Berkeley and Associate Director of the Nicholas C. Petris Center on Healthcare Markets and Consumer Welfare (petris.org) at UC Berkeley & Distinguished Professor of Health Economics and Public Policy in Graduate Schools of Public Health and Goldman School of Public Policy at UC Berkeley and Director of the Nicholas C. Petris Center on Healthcare Markets and Consumer Welfare (petris.org) at UC Berkeley. Ms. Alexander worked on this piece while serving as the Vice President of Policy at the American Antitrust Institute.

The large and increasing amount of money being managed by private equity ("PE") firms, and the huge push by PE into healthcare, raises concerns and challenges for healthcare policy, but also for competition policy. The PE business model and the business practices of PE firms threaten already limited competition in healthcare. By consolidating healthcare providers, offloading assets, cutting services, and loading acquired companies with debt, PE firms' move into healthcare is associated with increasingly concentrated markets providing higher cost and lower quality healthcare to patients.[2]

PE investment in healthcare has exploded over the last decade, and is projected to grow even more rapidly as we emerge from the pandemic.[3] The number of PE deals in healthcare as gone from 325 in 2010 to 1,085 in 2021.[4] Annual PE healthcare deal values have gone from at $41.5B in 2010 to $119.9B in 2019.[5] A multitude of PE funds have been raised to focus on healthcare and healthcare markets. PE funds have expanded to all areas of healthcare, with a primary focus on physician practices. Currently we are seeing expansive growth of PE in specialties such as dermatology, ophthalmology, and gastroenterology.

Lawmakers and regulators have expressed concern about the effects on patients and markets from this surge of PE investment. Jonathan Kanter, Assistant Attorney General for Antitrust, said that the PE business model is "often very much at odds with the law and very much at odds with the competition we're trying to protect."[6] FTC Chair Lina Kahn, joined by Commissioners Slaughter and Bedoya, likewise expressed skepticism about PE generally and in healthcare in particular.[7] President Biden highlighted PE ownership of nursing homes as a policy concern in his 2022 State of the Union address.[8]

These words from policymakers are beginning to translate into action. A recent FTC consent decree involving an acquisition of a veterinary practice by a PE fund imposed additional reporting requirements on future mergers involving the PE-owned entity.[9] The White House directed CMS to enact rules to implement ownership reporting requirements from the ACA that will shine light on PE ownership.[10] Rep. Jayapal introduced legislation in the House to require disclosure of PE ownership of nursing homes,[11] and several states have enacted legislation expressly or implicitly directed at increasing supervision of PE deals in healthcare.[12]

All of this attention from policymakers and regulators begs the question of whether PE funds should be treated differently than other owners under the antitrust laws and competition policy. Put differently, do PE firms present such extreme or unique competition concerns that

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2 See Martin Gaynor, Kate Ho & Robert J. Town. *The industrial organization of health-care markets*. 53 J. of Econ. Lit. 2 (2015) and references therein; see also Martin Gaynor, *Antitrust Applied: Hospital Consolidation Concerns and Solutions*, U.S. Senate Subcommittee on Competition Policy, Antitrust, and Consumer Rights (Washington, DC May 19, 2021), https://www.judiciary.senate.gov/imo/media/doc/Gaynor_Senate_Judiciary_Hospital_Consolidation_May_19_2021.pdf; Brent D. Fulton, *Healthcare Market Concentration Trends in the United States: Evidence and Policy Responses*, 9 Health Affairs 36, 1530-1538 (2017).

3 Nirad Jain, Kara Murphy, Franz-Robert Klingan, Dmitry Podpolny & Vikram Kapur, *Healthcare Private Equity Outlook: 2022 and Beyond*, Report, Bain & Co. (Mar. 15, 2022).

4 Petris Center at University of California, Berkeley, analysis of Pitchbook Data, prepared by Ola Abdelhadi. Data has not been reviewed by PitchBook analysts.

5 Richard M. Scheffler, Laura M. Alexander & James R. Godwin, *Soaring PE Investment in the Healthcare Sector: Consolidation Accelerated, Competition Undermined, and Patients at Risk*, The American Antitrust Institute & The Petris Center at the School of Public Health, University of California, Berkeley (May 18, 2021), https://www.antitrustinstitute.org/work-product/study-finds-private-equity-investment-accelerates-concentration-and-undermines-a-stable-competitive-healthcare-industry/. Deal values fell in 2020, presumably due to the COVID-19 pandemic, but are expected to rebound to above pre-pandemic levels. Preliminary results from our forthcoming study funded by the Laura & John Arnold Foundation supports the hypothesis of continued strong growth in PE spending in healthcare.

6 Stefania Palma & James Fontanella-Khan, *Crackdown on Buyout Deals Coming, Warns Top US Antitrust Enforcer*, Financial Times, May 19, 2022.

7 Statement of Chair Lina M. Khan Joined by Comm'r Rebecca Kelly Slaughter and Comm'r Alvaro M. Bedoya In the Matter of JAB Consumer Fund/SAGE Veterinary Partners, Comm'n File No. 2110140, Federal Trade Commission (June 13, 2022);

8 President Joseph R. Biden, Jr., Remarks by President Biden in State of the Union Address to the United States Congress (Mar. 1, 2022) ("[A]s Wall Street firms take over more nursing homes, quality in those homes has gone down and costs have gone up. That ends on my watch."), https://www.whitehouse.gov/briefing-room/speeches-remarks/2022/03/02/remarks-by-president-biden-in-state-of-the-union-address/. See also FACT SHEET: Protecting Seniors by Improving Safety and Quality of Care in the Nation's Nursing Homes, The White House (Feb. 28, 2022), https://www.whitehouse.gov/briefing-room/statements-releases/2022/02/28/fact-sheet-protecting-seniors-and-people-with-disabilities-by-improving-safety-and-quality-of-care-in-the-nations-nursing-homes/.

9 *In the Matter of JAB Consumer Partners SCA SICAR, National Veterinary Assocs., Inc., and SAGE Veterinary Partners, LLC*, Docket No. C-4766 (Aug. 2, 2022); see also Statement of Chair Lina M. Khan, supra n.2 ("Private equity firms have been particularly active in healthcare…. A focus on short-term profits in the healthcare context can incentivize practices that may reduce quality of care, increase costs for patients and payors, and generate appalling patient outcomes.").

10 FACT SHEET, *supra* n.3. See also Patient Protection & Affordable Care Act, Pub. L. No. 111-148 § 6101 (Mar. 23, 2010) (requiring disclosure of each member of the governing body of a nursing facility, all of its officers, directors, and managers, as well as their organizational structures and their relationships to one another), https://bit.ly/3vXClGk.

11 Healthcare Ownership Transparency Act, H.R. 6885, 117th Cong. (2022).

12 See, e.g. Wash. Rev. Code § 19.390 (2019) (establishing reporting requirements for mergers and acquisitions of hospitals, hospital systems, and provider organizations).

they merit special or different treatment under the law? The answer to this question is complicated, and depends on understanding how PE funds are structured, the incentives their managers face, and their strategies for profitability. We conclude that, for the most part, competition laws applicable *only to* PE are not needed; rather, when policymakers, regulators, and enforcers are applying competition laws to PE-owned companies, they need to take account of the unique incentives facing PE managers, the competitive implications of the PE ownership structure, and the types of competition concerns that tend to arise surrounding PE deals. In the particular case of mergers, such informed assessment of deals involving PE also requires updating the HSR reporting requirements.

I. THE STRUCTURE OF PE FIRMS

PE firms are structured as partnerships of fund managers.[13] Fund managers raise money for individual PE funds from institutional and other wealthy investors, which the fund managers then invest and oversee. Most of the money that PE funds use to acquire companies, however, comes not from the managers or the investors, but from large investment banks in the form of debt. A typical PE fund manager contributes only 2 percent of the fund's total assets. Institutional and other investors contribute about 20 percent, and the remaining 70-80 percent of the fund's "equity" is debt financing from banks.

A typical PE fund has a ten-year lifespan from the point at which it begins taking on investors until it returns the investment, adjusted for gains or losses, to the investors. During those 10 years, the fund will buy and sell companies, typically aiming to hold each company for 3-5 years. PE funds generally seek to use those 3-5 years to improve these companies by restructuring struggling firms, investing capital so they can expand, and providing needed management expertise, with the goal of selling them at a profit. These profits generate returns for the fund investors and for the PE managers. But this is not the only (or even the primary) way that PE managers make money.

PE funds typically operate on a "2-and-20" fee model, whereby the PE managers take an annual management fee of 2% of the money invested in the fund each year, plus 20 percent of the profits at the end of the fund. On top of these fund-level fees, however, PE funds also impose management and consulting fees on the businesses they acquire. In addition, as managers of the acquired businesses, PE managers often put in place business deals between the companies acquired by the fund and the fund, its investors, or the fund manager's affiliates. These deals can include supply agreements, licensing deals, or the sale of assets of the acquired companies to real estate investment trusts or other investors.

PE funds measure sales prices for companies in terms of multiples of EBITDA (earnings before interest, taxes, depreciation, and amortization). To profitably divest an acquired company, the PE fund must find a way to increase the company's multiple, its EBITDA, or both. To increase EBITDA, the PE fund will look for quick ways to cut costs and increase revenue. In the healthcare setting, cutting costs often involves cutting workers or replacing highly paid (and highly qualified) workers with lower paid (and less qualified) workers. It might also involve switching to cheaper supplies, such as sutures and tubing, or reducing hours or closing entire facilities. These cuts may adversely affect quality, which is often not transparent to patients or payers in healthcare. To raise healthcare revenues, PE managers have been known to put pressure on healthcare workers to perform more profitable procedures or to shift the business focus from a less profitable practice to a more profitable practice.[14] PE managers might also engage in aggressive billing and collection practices to increase revenues.[15]

To increase the EBITDA multiple, future growth in EBITDA is necessary, often through acquisitions. There are at least two reasons for this strategy. First, PE firms engage in what they call "consolidation plays." As the name implies, a fund will seek to consolidate a fragmented industry or market with a goal of becoming a dominant player in that market. Achieving such dominance gives the firm pricing power and allows the PE fund to demand a higher multiple in a subsequent sale. Second, larger companies have access to more and cheaper debt.[16] By growing an acquired company, the PE fund positions it to take on more debt, which makes it a desirable acquisition target for a second PE fund that wants to further leverage the company. The goal of the PE fund in most cases is to grow by acquisition to both consolidate competitors and leverage the company as much as possible.

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13 For an in-depth examination of the legal framework, business models, and compensation structures of PE funds, see generally Eileen Appelbaum & Rosemary Batt, PE at Work: When Wall Street Manages Main Street (Russell Sage Foundation 2014).

14 J.S. Resneck Jr., *Dermatology Practice Consolidation Fueled by Private Equity Investment: Potential Consequences for the Specialty and Patients*, 154 Jama Dermatology 1, at 13-14 (2018), https://doi.org/10.1001/jamadermatol.2017.5558.

15 See e.g. *UnitedHealthCare Services, Inc. v. Team Health Holdings, Inc.*, Memorandum & Order , 3:21-00364-DCLC-JEM 3 (May 10, 2022).

16 J. Bailey, *Why It May Pay to Buy Before Selling the Firm*, Wall St. J. (Feb. 25, 2003).

The structure of PE firms and the way they structure their mergers allows much of this growth and consolidation to take place without any (or any effective) review. Under the typical financial structure of PE funds, whereby the various partners at a single PE firm oversee a multitude of individual funds, the reporting requirements often fail to provide antitrust authorities with sufficient information to accurately evaluate the competitive risk from fund acquisitions. For example, a newly formed PE fund's first acquisition is generally not reportable, because the fund does not meet the "size of the person" test due to how rules about ultimate parent entities are determined.[17] But PE firms typically have multiple funds covering the same market areas and the manager of a newly-formed fund often oversees other funds that do hold assets in related areas. So, even though the newly-formed fund is exempt from HSR reporting on its first acquisition of a target company, the PE manager and the PE firm may well have significant holdings that compete with that target company.

Even without this "first-one-free" gap in HSR reporting, the buy-and-build model deployed by PE funds allows the funds to accumulate significant market power, particularly in products that compete in localized geographic markets, without any oversight from federal competition authorities. As we detailed in our recent report, PE funds deal amounts, particularly in healthcare, often fall just below the threshold for HSR reporting and pre-approval.[18] Through a "buy-and-build" approach, PE funds will buy a medium or large company in an industry and then use a series of small acquisitions of competitors and companies in adjacent markets, each falling below the HSR reporting thresholds, to build the original acquisition target into a powerful market player. As a result, many PE acquisitions are never reviewed by antitrust regulators and are not assessed by the FTC and DOJ for their impact on competition.

In discussing PE, though, it is critical to appreciate how hard it is to conduct effective research on PE investment and its effects. The vast majority of PE firms are not publicly traded or subject to any significant SEC reporting. As just discussed, many of the acquisitions made by PE funds using buy-and-build or roll-up models are not subject to HSR reporting. Even when acquisitions are subject to HSR reporting, outdated reporting requirements fail to capture the full scope of the PE fund's ownership interests.[19] Pitchbook, the gold standard for PE deal data, is forced to estimate up to 90 percent of its deal values due to lack of publicly available data.[20] Before President Biden's direction earlier this year, the ACA's provisions calling for increased reporting on ownership of nursing homes had not been implemented and no such data was available.[21] We—the authors of this piece—are currently working under a grant from Arnold Ventures[22] to conduct empirical research on the competition impacts of PE investment in healthcare provider markets. Such research is sorely needed to better understand the scope and extent of competition impacts from PE, but is currently significantly hampered by a lack of disclosure and centralized datasets on PE ownership.

II. THE PE BUSINESS MODEL IN HEALTHCARE

While the PE model can be problematic in all sectors, it is particular so in healthcare where lives are on the line, quality is often not transparent, and competition is far from robust. First, the high-risk, high-reward PE investment strategy leaves healthcare facilities and providers burdened with debt and without a cushion of assets, making them vulnerable in the face of a systemic shock, like a pandemic or a market downturn.

Second, while consolidation can lead to efficiencies, consolidation can also lead to increased market power, which can in turn lead to reduced choice, reduced quality, and increased prices. This issue is particularly acute in the healthcare setting, where PE firms regularly deploy a "buy-and-build" or "roll up" strategy. Most physician practice acquisitions are too small[23] to require HSR reporting to antitrust authorities and, as a result, most go unreviewed.[24] Using this method, PE funds have been able to accumulate some remarkable and concerning market shares,

17 16 C.F.R. § 801.11(e) (allowing an entity that is its own ultimate parent entity and without a regularly prepared balance sheet to exclude funds used for the purpose of acquisitions).

18 Richard M. Scheffler, Laura M. Alexander, & James R. Godwin, *Soaring PE Investment in the Healthcare Sector: Consolidation Accelerated, Competition Undermined, and Patients at Risk*, The American Antitrust Institute & The Petris Center at the School of Public Health, University of California, Berkeley (May 18, 2021), https://www.antitrustinstitute.org/work-product/study-finds-private-equity-investment-accelerates-concentration-and-undermines-a-stable-competitive-healthcare-industry/.

19 See Premerger Notification; Reporting and Waiting Period Requirements, 85 Fed. Reg. 77053 (proposed Dec. 1, 2020) (proposal to expand definition of "person" to better capture relevant information about PE holdings).

20 The low percentage of reported deal values raises concerns about the precision of Pitchbook's estimated total deal values. Those concerns are partially mitigated by recognizing that few if any large deals are unreported, because deals above a certain dollar threshold trigger SEC and FTC reporting requirements. Nevertheless, the PitchBook numbers must be taken for what they are: the best available estimate.

21 Taylor Lincoln, *Is it Private Equity? We Can't See*, Public Citizen (Sept. 1, 2022), https://www.citizen.org/article/nursing-home-transparency/.

22 Grant No. 21-06178 to the American Antitrust Institute.

23 For 2022, the HSR reporting threshold is $101M. *Revised Jurisdictional Thresholds for Section 7A of the Clayton Act*, 87 Fed. Reg. 3541 (Jan. 24, 2022).

24 https://www.healthaffairs.org/doi/full/10.1377/hlthaff.2017.0054.

for example in multiple healthcare specialties in local and regional markets. PE controls 69 percent of the market for dermatologists in Salem, OR; 78 percent of the market for dermatologists in Lansing-East Lansing, MI; 80 percent of the market for anesthesiology physician groups in Wilmington, NC; and 91 percent of the market for radiology physician groups in Idaho Falls, ID.[25]

Take the case of Team Health. Team Health, the country's largest physician staffing company, has twice been taken private by PE firm Blackstone, for the second time in early 2017. In just the first year after Blackstone's 2017 takeover, Team Health's presence in emergency medical staffing, already large, exploded. The number of metropolitan statistical areas ("MSAs") in which Team Health owned emergency medicine practices went from 34 in 2016 to 47 in 2017. The number of MSAs where Team Health owned more than 50 percent market share of emergency medicine went from 3 to 6 in that same time period. In Knoxville, where Team Health is headquartered, its market share in emergency medicine went from 38.5 percent in 2016 to 82.5 percent in 2020.[26] Nearly all of this growth was fueled by acquisitions and none of those acquisitions were challenged by antitrust authorities.

Third, research suggests that PE investors are more responsive than non-PE investors to market incentives.[27] In markets with robust competition, then, PE funds are by-and-large particularly adept competitors. The corollary of this finding, though, is that PE companies are also particularly adept at exploiting market power and market and regulatory failures in markets where they exist. Healthcare is a poster child for such markets.

Healthcare markets have a number of characteristics that make them exceptionally vulnerable to exploitation by PE.[28] Healthcare markets are highly concentrated and lacking in competition. To the extent PE is driving further consolidation in healthcare, PE is making this existing concentration problem worse. But, even if PE is not the only driver of the consolidation, it may be particular adept at exploiting it.

Beyond high levels of concentration, healthcare markets are further characterized by opaque product quality, heavy government subsidies, and a disconnect between demand and payments driven by third-party payer models, all of which serve to hamper effective competition. Studies have shown that in such markets, PE ownership can be associated with higher prices, lower quality, and worse health outcomes.[29]

Anecdotally, there are reasons to worry that PE strategies may serve to exacerbate the very issues that impair health competition in these markets. For example, overbilling hampers competition by disconnecting services demanded from prices charged for those services (in addition to directly inflicting financial harm on payers). Overbilling is not just a civil issue impacting patients and markets; when the payer is the government, overbilling can also amount to criminal fraud. The False Claims Act, which imposes criminal liability on medical professionals who engage in overbilling, however, requires that the medical profession knows about the overbilling. Because of way PE funds separate the billing function from the providers, the providers generally lack the required knowledge for False Claims Act liability.

This separation between physicians and patient billing also means that physicians have little oversight over whether their patients are being fairly billed in their name for the services provided. Yet, when a group of physicians opposed to the corporate practice of medicine recently proposed a rule that would require ER staffing companies (like those being acquired by PE funds) to periodically furnish their physicians with data on what is being billed under their license numbers, the American College of Emergency Physicians (ACEP) had a troubling response: it engaged outside lawyers to evaluate whether such disclosure could expose physicians to liability under the False Claims Act because the provision of the information would leave them "knowing" of inflated billings.[30]

Overbilling is not a problem limited to PE ownership,[31] and not all aggressive billing amounts to criminal fraud, but one of the established PE strategies for generating the short-term improvements in revenues needed to make their business model work is to stretch the boundaries of ethical and accurate billing practices to their limits (and sometimes beyond their limits). The same characteristics that make PE exceptionally

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25 Petris Center at University of California, Berkeley, analysis of Pitchbook Data, prepared by Ola Abdelhadi. Data has not been reviewed by PitchBook analysts.

26 Petris Center at University of California, Berkeley, analysis of Pitchbook Data, prepared by Ola Abdelhadi. Data has not been reviewed by PitchBook analysts.

27 Atul Gupta, Sabrina T. Howell, Constantine Yannelis, & Abhinav Gupta, *Does PE Investment in Healthcare Benefit Patients? Evidence from Nursing Homes*, Working Paper (March 9, 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3537612.

28 See Scheffler, et al., *supra* n.21 at 5-6.

29 *Id.*

30 Maureen Tkacik, *Wall Street in Pressing ER Docs to Fleece Patients*, The Lever (Oct. 27, 2021).

31 See, e.g. Michael Geruso & Timothy Layton. *Upcoding: Evidence from Medicare on Squishy Risk Adjustment.* 128 J. of Pol. Econ. 3 (2020); Elaine Silverman & Jonathan Skinner. *Medicare upcoding and hospital ownership.* 23 J. of Health Econ. 2 (2004).

responsive to competitive pressures also make PE exceptionally responsive to opportunities to exploit market power and market failures like those seen in healthcare. This is a competition problem.

III. IMPLICATIONS FOR COMPETITION LAW & POLICY

Recognition that PE raises competition concerns does not necessarily imply that private-equity-specific competition rules and policies are necessary. While PE funds may have incentives to engage in certain strategies that are anticompetitive, it is those strategies that should be prohibited, regardless of whether they are perpetrated by PE funds or other owners.[32] The ultimate issue in the antitrust inquiry—does the merger or conduct reduce or prevent competition—does not change based on whether the merger involves PE-ownership. Because many of the most concerning practices from PE funds are not exclusive to PE funds, it is important the laws are able to reach others engaged in those practices as well, even if not as often or to the same degree as PE funds. The Sherman and Clayton Acts speak in broad principles and do not try to imagine or legislate against the myriad ways that companies might try to accrete market power, collude, or monopolize markets; they instead express a legislative choice for competition over monopolization and collusion. Although PE funds have invented new ways (or perfected old ways) of undermining competition, this should not impact the ability of the antitrust laws to push back against those methods, provided that the competition dynamics underpinning them are properly understood.

What the competition concerns surrounding PE do suggest, however, is that PE firms and their strategies reveal gaps and holes in current competition rules and policy — in reporting requirements, in the treatment of small and seriatim mergers — that should be filled with regard to all parties, not PE firms only. Antitrust law and policy should be hardened generally against certain anticompetitive mergers and conduct, regardless of whether perpetrated by PE firms, tech firms, or traditional corporations, including non-profits. Research has suggested that PE funds are particularly adept at exploiting gaps in existing enforcement policy, laws, and regulations. They function, essentially, as divining rod for regulatory cracks. Finally, the structures and business models of PE firms imply that they face different competitive incentives and models of profitability than more traditional ownership structures. It is critical that in applying the antitrust laws to PE firms, courts and enforcers understand and take account of those differing incentives and their implications for the competitive effects of mergers and conduct involving PE-owned firms.

The HSR requirements, for example, were enacted in 1976, and have undergone only limited updates. While several attempts have been made since the early 80s to adapt HSR reporting to account for new ownership structures like PE,[33] they have been only partially successful.[34] It is critical that HSR filing requirements are updated to better capture the relationships between funds, fund managers, investors, and target companies, so that the antitrust agencies will have the information they need to evaluate the likely competitive impact of PE acquisitions. The "first-one-free" gap, which immunizes a new PE fund's first purchase from HSR filing, should also be closed.

Another area where observation of PE suggests attention is needed is serial acquisitions and small mergers involving localized markets.[35] Part of the solution is surely to increase scrutiny and enforcement by states, who are in many ways better positioned to police local markets and who have always played a significant role in healthcare. But many PE funds are implementing acquisition strategies that cover multiple states and regions, suggesting that federal enforcement and attention is also needed. Moreover, enforcement challenges posed by serial acquisitions and acquisitions of small companies (such as nascent competitors) are a problem that extends well beyond healthcare and beyond private equity.

Finally, in healthcare in particular, interventions that are more specific to PE and other complex business models may be needed. If research continues to show that PE ownership in healthcare can be associated with increased prices, decreased quality, and increased mortality and morbidity, broadly applicable antitrust laws may be insufficient to address PE's negative effects on healthcare competition and health outcomes. Instead, a coordinated response from the Secretary of Health and Human Services, the Centers for Medicare and Medicaid Services, and Congress with the support of the President will be needed to ensure higher mortality and morbidity from poorly functioning healthcare markets and low quality of care are not the price paid for PE profits.

32 The No Surprise Act, signed into law on Dec. 27, 2020, and which outlaws surprise billing by ER doctors and other providers, is a good example of legislation that targets undesirable and anticompetitive business practices pioneered and exploited by PE-owned companies but that is broadly applicable without regard for PE ownership status; by its terms, the law outlaws surprise billing by all providers, regardless of their PE ownership status. No Surprises Act, H.R. 3630, 116th Cong. (2020).

33 See Premerger Notification; Reporting and Waiting Period Requirements, 76 Fed. Reg. 42,471 (July 19, 2011) (adding the "associate" definition targeted at PE funds and master limited partnerships

34 See e.g. Premerger Notification; Reporting and Waiting Period Requirements, 85 Fed. Reg. 77053 (proposed Dec. 1, 2020) (proposal to expand definition of "person" to better capture relevant information about PE holdings), on which the FTC has taken no action since the comment period closed.

35 See T.G. Wollmann, *How to Get Away with Merger: Stealth Consolidation and its Real Effects on US Healthcare* (No. w27274), National Bureau of Economic Research, Inc., https://doi.org/10.3386/w27274.

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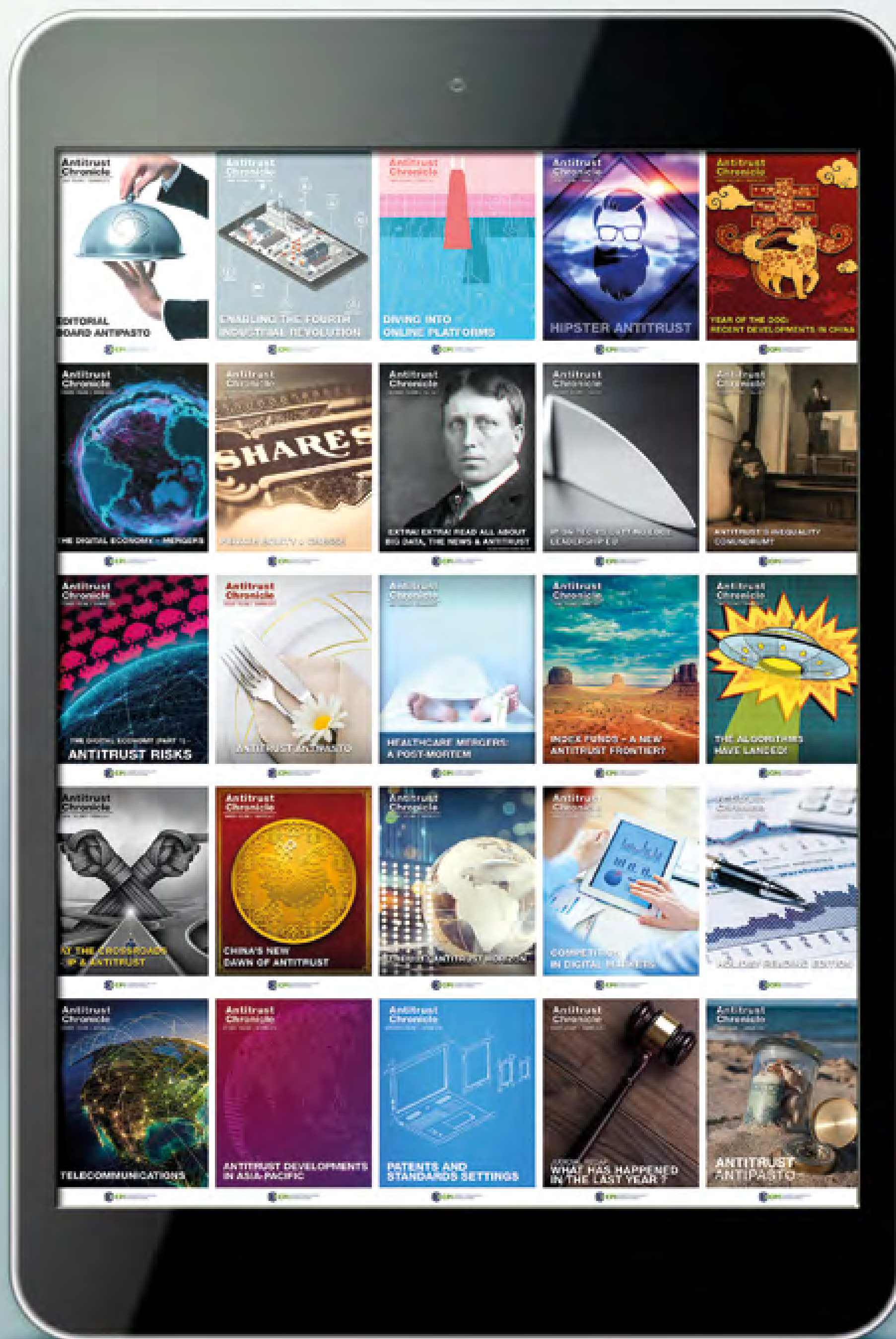

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