FTC-DOJ Inquiry on Serial Acquisitions: Cracking Down on PE Roll-Ups?

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May 30, 2024

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On May 23, 2024, the Federal Trade Commission (FTC) and Antitrust Division of the Department of Justice (DOJ) jointly announced a request for members of the public to provide information that the agencies can use "to identify serial acquisitions and roll-up strategies throughout the economy that have led to consolidation that has harmed competition" (the RFI).

This is the latest step in the Biden Administration's years-long efforts to more aggressively police what the RFI defines as "corporate consolidation strategies that occur when a company becomes larger — and potentially dominant — by buying several smaller firms in the same or related business sectors or industries." The agencies believe that roll-up strategies, often employed by private equity firms, are particularly pernicious, because individual transactions may fall below the Hart-Scott-Rodino (HSR) reporting thresholds and thus escape agency scrutiny.

The focus on roll-ups is not new. Both the agencies' new Merger Guidelines and the proposed changes to the HSR filing process reflect the agencies' concerns. But the timing of the RFI inadvertently highlights some of the challenges the agencies face in trying to ramp up enforcement in this area. Specifically, the RFI was released only days after a court dismissed a PE firm defendant from the FTC's first true challenge to an alleged roll-up strategy (discussed below). This harkens back to the prediction we made after the new Merger Guidelines were finalized that courts may be reluctant to apply the novel theories of harm reflected in the new Guidelines. See our December 21, 2023, client alert "DOJ and FTC Release Final 2023 Merger Guidelines Formalizing Aggressive Merger Enforcement Playbook."

Despite this setback, the agencies are still undoubtedly in search of more test cases with favorable facts, which likely include a relatively small set of transactions involving high combined market shares and direct evidence of anticompetitive effects (*e.g.*, price increases).

We do not anticipate the RFI will materially amplify the agencies' enforcement efforts. However, the exercise does serve as a reminder of the agencies' keen interest in roll-ups, and companies making multiple acquisitions in the same industry should be mindful of the greater risk of antitrust scrutiny and should consider ways to mitigate the risk.

Content of the Request for Information

The RFI and requests members of the public to provide the agencies with examples of so-called serial acquisitions and roll-up strategies that they believe have proved to be anticompetitive. While seeking information across all sectors of the U.S. economy, the RFI specifically calls out the housing, agriculture, defense, cybersecurity, distribution, construction, aftermarket/repair, and professional services sectors.

The categories of information sought in the RFI include examples of serial acquisitions and their effects on competitors, customers, workers, and suppliers; specific business practices the buyer has engaged in; the claimed business objectives of the acquisition; and information about ownership and control of the PE firm post-acquisition.

The agencies seek input from a wide range of stakeholders including consumers, workers, businesses, advocacy organizations, professional and trade associations, local, state and federal elected officials, and academics. The comment period closes on July 22, 2024, and the comments received will be publicly posted.

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More Tough Talk About Serial Acquisitions

The RFI is the latest in a string of agency enforcement measures aimed at serial acquisitions.

- In November 2022, the FTC issued a policy statement articulating a broad interpretation of its enforcement authority under Section 5 of the FTC Act, which explicitly called out "a series of mergers, acquisitions, or joint ventures that tend to bring about the harms that the antitrust laws were designed to prevent" as a potential unfair method of competition that could violate Section 5. Here, as in the FTC's most recent rule banning worker noncompetes, the commission is seeking to stretch the application of Section 5 beyond the bounds of how the agencies have enforced the antitrust laws for the last several decades. See our April 24, 2024, client alert "FTC's Final Rule Banning Worker Noncompete Clauses: What It Means for Employers."
- In June 2023, the agencies proposed amendments to the HSR premerger notification forms that include disclosures about each party's prior acquisition history — a clear effort by the agencies to more easily identify serial acquirers. See our July 6, 2023, client alert "FTC and DOJ Propose Dramatic Expansion of HSR Filings' Scope."
- When the agencies issued their final revised Merger Guidelines in December 2023, they expressly asserted that "[a] firm that engages in anticompetitive pattern or strategy of multiple acquisitions in the same or related business lines" may violate not only Section 7 of the Clayton Act, but also potentially Section 2 of the Sherman Act and Section 5 of the FTC Act.
- Earlier this year the agencies, together with the Department of Health and Human Services, commenced a separate joint public inquiry that specifically seeks information about the impact of PE investment in the health care market.

Setback in a Test Case

These policies were put to an initial test in federal court in Texas, where the FTC filed a complaint against U.S. Anesthesia Partners (USAP) in September 2023, alleging that USAP had engaged in illegal consolidation of the anesthesia market in Texas in violation of the FTC Act via a roll-up scheme, as well as other conduct including price-setting arrangements with independent anesthesia groups and a market allocation agreement with another large anesthesia services provider. The FTC also named as a defendant the PE firm Welsh Carson, a minority owner of USAP with a 23% share and two of 14 board seats.

In a May 13, 2024, decision, the court granted Welsh Carson's motion to dismiss, holding that the FTC had not adequately alleged that Welsh Carson "'is violating' Antitrust Law," because the mere "act of receiving profits from USAP is not an ongoing antitrust violation."

The court also held that the FTC failed to establish that "a minority, noncontrolling investor — however hands-on — [should be] liable under Section 13(b) because the company it partially owned made anticompetitive acquisitions." The court decided that "[s]uch a construal of Section 7 and 13(b) would expand the FTC's reach further than any court has yet seen fit."

In addition, the court held that the FTC "ha[d] not adequately alleged that Welsh Carson is 'about to violate' Antitrust Law." Here, the court held that "the mere capacity to do something does not meet the requirement that the thing is likely to recur."

While the court dismissed the PE firm on the basis of its minority ownership and lack of control over the operating company, it allowed the FTC's claims against USAP to proceed, finding that the complaint adequately alleged that "USAP continues to own the anesthesia groups it unlawfully acquired and continues to charge high prices; USAP currently maintains two price-setting arrangements that result in higher prices; and USAP's overall monopolization scheme remains intact," which sufficed to plead that USAP "is currently or about to violate antitrust laws." The court cited USAP's business records, including statements by a business executive, as evidence that the acquisitions could plausibly have anticompetitive effects.

Takeaways

The FTC and DOJ inquiry on serial acquisitions and roll-ups evidences once again the agencies' attention to these types of acquisition strategies and the acquisition practices of PE firms more generally. Some public comments could lead to new investigations of past acquisitions. However, despite the tough talk, the agencies are likely to focus their enforcement efforts on deals presenting the traditional evidence of high combined shares or price increases and other anticompetitive effects. And, as seen in the FTC's anesthesia case, business records touting explicit roll-up strategies and post-acquisition price increases will also attract close attention.

But, if the agencies challenge serial acquisitions without traditional evidence (such as high shares or anticompetitive effects), they likely will face skeptical courts. The government also must contend with the fact that roll-ups can have a number of pro-competitive benefits, such as providing management, industry, and operational expertise to target firms, thereby improving their overall performance; injecting needed capital into operating companies (for example to rescue neglected assets); and lowering costs, increasing output and generating employment opportunities.

Companies engaged in or contemplating a series of acquisitions should be aware of the agencies' ongoing interest in this space and be mindful of how the relevant operating companies are being run to avoid landing in the agencies' crosshairs.

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