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Management Alert

Private Equity & Antitrust Law: Primer in the Face of the DOJ's Investigation of Possible Anticompetitive Behavior

The U.S. Department of Justice (DOJ) is monitoring the private equity industry. According to recent reports in the Wall Street Journal and other publications, the DOJ has contacted some of the leading private equity firms in the U.S. to ask them to provide information concerning their practice of cooperating with competitors in connection with the acquisition of target companies. The DOJ is interested in learning whether private equity firms are tacitly reaching understandings not to compete for the same targets in order to reduce the price they have to pay. According to the financial press, the DOJ is also scrutinizing "club" arrangements pursuant to which multiple PE firms agree to bid for a target together in order to attain the necessary funding and to diversify risk. Although the DOJ inquiries are preliminary and the information requests were not compulsory, the DOJ's action has raised concerns within the industry. This alert provides a brief primer on applicable antitrust law and identifies safeguards that a private equity firm can adopt to reduce the risk of liability.

The principal applicable antitrust law is the Sherman Act. Section 1 of the Sherman Act makes illegal contracts, combinations and conspiracies that unreasonably restrain trade. Specifically, Section 1 targets anticompetitive agreements or understandings among competitors. Certain restraints are considered so pernicious that they are considered *per se* illegal and no explanation of the reasonableness of the conduct will excuse the conduct. Conversely, the DOJ will not have to prove that such conduct is unreasonable. Price fixing agreements among competitors, bid-rigging schemes, and allocation of opportunities by industry or territory are all considered to be *per se* offenses. Other activity such as non-price restraints that an influential investor could impose on a financial intermediary will be judged under a "rule of reason" analysis and, hence, be illegal only when the restraint is found to be unreasonable.

On the one hand, agreements among private equity firms not to compete with each other at auction could constitute a *per se* violation of Section 1. On the other

hand, a decision by a private equity firm not to submit a bid after another firm has entered a letter of intent, might be reasonable if the purpose is to avoid accusations of interference with contract or prospective advantage. Both situations would require factual analysis. For instance, if the bid for a target was made jointly by two or more private equity firms, such conduct would not likely be deemed as unreasonable if the purpose was to spread the risk. However, if the purpose of a joint bid (or subsequent future joint participation) is to avoid competition in the bidding process, a *per se* antitrust violation might arguably exist.

Price fixing and bid rigging violations must be taken seriously as they can result in significant jail sentences, substantial fines, and treble damages from any subsequent private antitrust litigation brought by any injured party. An effective antitrust compliance program will help detect any potential areas of antitrust concern and deter any future anticompetitive activity. Further, having an effective compliance program in place can help reduce any penalties that may be imposed should a violation of law occur despite the compliance efforts.

Compliance with the law concerning unfair competition has not been a pressing issue for the PE industry. The DOJ's inquiry has changed that. Given the difficulty in prosecuting violations of the antitrust laws and the informal nature of the inquiry, it is not expected that the DOJ's overture will lead to any enforcement actions. Nonetheless, it is advisable that PE firms take steps to ensure that their principals are educated on the applicability of unfair competition to their business. By adopting the safeguards described above, PE firms can reduce the risk of liability associated with broader DOJ investigations.

The attorneys in Seyfarth Shaw's Antitrust Group regularly present to executives on antitrust compliance matters and collaborate with their colleagues in the Private Equity Group. For more information or to schedule a compliance training, please be in touch with your primary Seyfarth contact or either of the following attorneys:

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