

ALERT

Walking the Walk: FTC Lawsuit Targets Private Equity Roll-Up Strategy

October 2, 2023



**SCHULTE
ROTH +
ZABEL**



ALERT

Walking the Walk: FTC Lawsuit Targets Private Equity Roll-Up Strategy

October 2, 2023

What happened?

On Sept. 21, 2023, the Federal Trade Commission (“FTC”) sued US Anesthesia Partners (“USAP”) and its private equity backer, Welsh, Carson, Anderson & Stowe LP (“Welsh Carson”), alleging that USAP and Welsh Carson violated antitrust law through a three-pronged scheme to monopolize the anesthesiology market in Texas to drive up prices and increase profits. In its [complaint](#), filed in the Southern District of Texas, the FTC alleges that USAP and Welsh Carson:

- Executed a “roll-up” strategy, buying up over a dozen large anesthesia practices in Texas over about a decade to create a single dominant provider (with allegedly ~70 percent share by revenue and ~60 percent share of cases for hospital-only anesthesia services in several geographies) that commanded higher prices;
- Drove up anesthesia prices further through price-setting agreements with independent providers that allowed USAP to bill payers for anesthesia services offered by both groups at USAP’s higher rates; and
- Eliminated competition by securing a large rival anesthesiology provider’s agreement to stay out of USAP’s territory.

According to the FTC, this anticompetitive conduct, along with high switching costs for hospitals and high barriers to entry, allowed USAP to retain nearly all of its hospital contracts even while charging the highest rates for anesthesia services. The complaint alleges this conduct violates Section 1 of the Sherman Act (prohibiting agreements in restraint of trade), Section 2 of the Sherman Act (prohibiting monopolization), Section 7 of the Clayton Act (prohibiting transactions that may substantially lessen competition or tend to create a monopoly) and Section 5(a) of the FTC Act (prohibiting unfair methods of competition).

“Private equity firm Welsh Carson spearheaded a roll-up strategy and created USAP to buy out nearly every large anesthesiology practice in Texas. Along with a set of unlawful agreements to set prices and allocate markets, these tactics enabled USAP and Welsh Carson to raise prices for anesthesia services — raking in tens of millions of extra dollars for these executives at the expense of Texas patients and businesses,” said FTC Chair Lina Khan.

The FTC’s suit against USAP and Welsh Carson is only the latest salvo in the government’s campaign to increase scrutiny of private equity deals. While this case appears to have some extreme facts, with a roll-up strategy being used to create a dominant anesthesia provider and the protection of that dominance through price-setting and market allocation agreements, it highlights the need for private equity firms to carefully consider antitrust issues at the outset of a roll-up strategy.

It is important to note that the FTC lawsuit does not mean that all private equity firms engaging in serial acquisitions should expect an investigation, as the allegations here involve both market concentration and market conduct. As Rahul Rao, deputy director of the FTC’s Bureau of Competition, noted in his remarks



during the American Bar Association antitrust law section's most recent annual spring meeting, private equity is "not a monolith" and not all firms use the tactics that concern the agencies. Catherine Reilly, the DOJ Antitrust Division's counsel for civil operations, also acknowledged that private equity firms are not all alike and that some could even be considered as divestiture buyers.

Why is this important?

The *FTC's lawsuit against USAP and Welsh Carson* is notable in a few respects.

First litigated challenge to serial acquisitions. While both the [FTC](#) and the [Department of Justice](#) ("DOJ") have expressed concern over the potential cumulative impact of serial or roll-up acquisitions, the suit is the FTC's first litigated challenge directed at this strategy. Individually, these smaller acquisitions often fall below the notification thresholds of the Hart-Scott-Rodino ("HSR") Act, which can allow an acquiring firm to grow market share without antitrust scrutiny — at least until now. The FTC asserts in its complaint that roll-up acquisitions violate the antitrust laws whether considered individually or in the aggregate. In an [opinion piece](#) for the *Financial Times*, Chair Khan argues that federal antitrust laws "can be squarely applied to a wide range of business practices, including serial acquisitions" and states in the FTC's accompanying [press release](#) that the agency "will continue to scrutinize and challenge serial acquisitions, roll-ups, and other stealth consolidation schemes that unlawfully undermine fair competition and harm the American public."

Targeting of minority private equity investor. Alongside USAP, the FTC is suing one of the company's private equity backers. Despite the fact that Welsh Carson is a minority stakeholder (alongside Berkshire Partners and GIC Capital), the FTC alleges that Welsh Carson effectively controls USAP and that it masterminded the "multi-year anticompetitive scheme." Consistent with Chair Khan's assertion in her *Financial Times* op-ed that the antitrust laws "may apply to parent companies and investors if they directly participate or conspire to participate in anti-competitive conduct," the FTC claims that Welsh Carson "formulated, directed, controlled, had the authority to control, dictated, encouraged, or actively and directly participated" in USAP's allegedly anticompetitive conduct. In particular, the complaint focuses on Welsh Carson general partner Brian Regan's role in allegedly facilitating the USAP's scheme by signing deal documents, leading negotiations for USAP's alleged market allocation agreement with a rival provider, identifying acquisition targets, securing funding and negotiating with insurers.

Pattern of heightened regulatory concern over private equity roll-ups continues. As we discussed in a [previous Alert](#), private equity transactions, once considered unlikely to raise significant antitrust concerns, have been put in the crosshairs by the Biden administration. Agency leadership consistently has signaled in public statements its distrust of roll-ups and, in recent months, has moved beyond "talking the talk" to "walking the walk." Their actions include proposing changes to the HSR notification form to gather information about private equity structures and proposing changes to the merger guidelines enabling the review of serial acquisitions and partial ownership, as well as imposing broad prior approval and prior notice requirements in a consent decree for another private equity deal.

Agency rhetoric targeting private equity roll-ups. Both the FTC and the DOJ have been vocal about the need to examine private equity transactions, particularly in the healthcare space and particularly with regard to serial acquisitions. Assistant Attorney General Jonathan Kanter [argued](#) in May 2022 that the roll-up model is "often very much at odds with the law and very much at odds with the competition we're trying to protect," and has warned that a fuller assessment of these deals is "top of mind." Deputy Assistant Attorney General Andrew Forman stated in a June 2022 [speech](#) that the DOJ is "focused on potential antitrust enforcement on private equity 'roll-ups,' namely whether in particular circumstances a



series of often smaller transactions can cumulatively or otherwise lead to a substantial lessening of competition or tendency to create a monopoly.” Chair Khan [echoed](#) those comments, advocating for a more “muscular” approach to reviewing private equity deals and stating that “a huge private equity firm controlling, say, veterinary clinics” could be of concern even if the individual acquisitions might not raise issues.

Prior approval and prior notice requirements. In June 2022, the FTC [announced](#) a consent agreement with JAB Consumer Partners (“JAB”) in connection with its acquisition of a series of veterinary clinics that included a prior approval requirement for future acquisitions in the relevant markets, as well as a broad and “first of its kind” requirement that JAB provide advance notice to the FTC before the acquisition of any US veterinary clinic within 25 miles of any clinic owned by JAB. The requirements were imposed to curtail JAB’s ability to continue with what Chair Khan [termed](#) “‘buy-and-buy’ tactics” that allow firms to “roll up sectors” and “accrue market power and reduce incentives to compete, potentially leading to increased prices and degraded quality.” Chair Khan stated that these types of prior approval and prior notice remedies will “allow the FTC to better address stealth roll-ups by private equity firms.”

Proposed changes to HSR form and merger guidelines. The agencies also focused on private equity roll-ups in their proposed changes to both the [premerger notification form](#) required by the HSR Act and the [draft merger guidelines](#), which we have written about previously. The expanded obligations proposed in June 2023 by the FTC to the HSR form would include requirements aimed at uncovering roll-up strategies through the disclosure of acquisitions in the preceding 10 years in any industry where the parties report a horizontal overlap, even if those transactions were not previously reported to the agencies due to their smaller size. The draft merger guidelines jointly released in July 2023 by the FTC and the DOJ include a guideline specifically allowing the agencies to consider the cumulative effect of an entire series of acquisitions, rather than just an individual deal, to determine if a firm may have violated antitrust laws.

Takeaways

- The FTC’s suit against USAP and Welsh Carson gave teeth to increasing rhetoric from both agencies against private equity consolidation in the healthcare space. The lawsuit also made good on the FTC’s stated intentions to enforce antitrust laws against serial acquisitions. Given the provisions specific to roll-ups in both the proposed changes to the HSR notification form and the proposed draft merger guidelines, as well as statements made by DOJ and FTC leadership, we can expect similar lawsuits or enforcement actions challenging the cumulative effect of roll-up or serial acquisitions to follow.
- The legitimacy of the agencies’ position will be determined in court. Although the agencies’ recent litigation track record may not bode well for the FTC, regardless of the ultimate outcome of the suit against USAP and Welsh Carson, firms that have pursued or are considering roll-up strategies, particularly in healthcare, should evaluate their market positions and assess the risk that they might be targeted by a similar action. The risk of investigation increases if market consolidation is accompanied by price hikes or other conduct that may reduce or eliminate competition (e.g., price fixing or setting, market allocation agreements, etc.).
- Even though the FTC does not allege anticompetitive acts by USAP or Welsh Carson in markets outside of Texas (or other markets in Texas outside of anesthesiology), the FTC seeks to enjoin Welsh Carson “from engaging in similar and related conduct in the future,” in addition to the equitable relief it seeks from USAP (including divestitures). The complaint alleges that Welsh



Carson has pursued and will continue to pursue similar rollup strategies in anesthesiology and other medical specialties, such as emergency medicine and radiology, in violation of the antitrust laws. If the FTC is successful, the court could issue an injunction similar to the JAB consent decree requiring Welsh Carson to seek prior approval from the FTC before making acquisitions of anesthesiology practices in Texas and also to give prior notice to the FTC of acquisitions of anesthesiology practices in other states or perhaps acquisitions of any medical specialties in the US. This broad relief would potentially interfere with Welsh Carson's ability to make future acquisitions in other markets.

Authored by [Peter Jonathan Halasz](#) and [Ngoc Pham Hulbig](#).

If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

Schulte Roth & Zabel
New York | Washington DC | London
srz.com

This communication is issued by Schulte Roth & Zabel LLP for informational purposes only and does not constitute legal advice or establish an attorney-client relationship. In some jurisdictions, this publication may be considered attorney advertising. © 2023 Schulte Roth & Zabel LLP. All rights reserved. SCHULTE ROTH & ZABEL is the registered trademark of Schulte Roth & Zabel LLP.