

THE ANTITRUST IMPLICATIONS OF "GOING PRIVATE" AND OTHER CHANGES OF CORPORATE CONTROL

THOMAS A. PIRAINO, JR.*

Abstract: Public shareholders likely have suffered billions of dollars in losses in recent years as a result of collusion among potential purchasers in change-of-control transactions. Unfortunately, the federal courts have been unable to devise an appropriate antitrust approach to collusion in change-of-control transactions. This article proposes a new approach to the antitrust regulation of the market for the control of public and private companies. Collusion among purchasers in that market has occurred in nearly every American industry. The proposed approach will effectively deter the three types of anticompetitive conduct most likely to occur in these circumstances: (1) express agreements to allocate bids among potential purchasers, (2) implicit bid rigging by potential purchasers, and (3) consortiums among potential purchasers to submit single bids in company auctions. This Article illustrates the advantages of the proposed approach by applying it to "going private" transactions, which in recent years have become the most popular—and the most controversial—of all types of acquisitions.

INTRODUCTION

A. Collusion in Change-of-Control Transactions

The potential for collusion in corporate change-of-control transactions poses one of the greatest antitrust challenges of our time. During the last few years, shareholders likely have suffered billions of dollars in losses as a result of agreements among potential purchasers to limit bidding for the purchase of control of American companies.¹ Collusion among purchasers has occurred in the market for control of both public and private entities and has involved companies in nearly every Ameri-

* Vice President, General Counsel, and Secretary, Parker Hannifin Corporation, Cleveland, Ohio; J.D., Cornell Law School, 1974; B.A., Allegheny College, 1971; Distinguished Adjunct Lecturer, Case Western Reserve University School of Law. The opinions expressed in this Article are personal to the author and do not reflect the opinions of Parker Hannifin Corporation.

¹ See *infra* notes 96-123 and accompanying text.

can industry.² Such bid rigging would constitute a "per se" violation of the Sherman Antitrust Act if it occurred for any other commodity.³ The federal courts, however, have deprived shareholders of an effective antitrust remedy against collusion in change-of-control transactions.⁴

The federal courts need to develop a new antitrust approach that will allow shareholders to recover losses incurred as a result of collusion in change-of-control transactions. This Article proposes an approach that will effectively deter the three types of anticompetitive conduct that are most likely to occur in such circumstances: (1) express agreements to allocate bids among potential purchasers, (2) implicit "bid rigging" by potential purchasers, and (3) consortiums among potential purchasers to submit single bids in company auctions.⁵

B. *Going-Private Transactions*

This Article illustrates the advantages of the proposed approach by applying it to "going-private" transactions, which, in recent years, have become the most popular and the most controversial of all types of acquisitions.⁶ In such transactions, private equity firms buy out the public shareholders, operate the company as a private entity for a short period (usually three to five years),⁷ and then "flip" it for a quick profit to a competitor in the same industry, to another private equity firm, or to the public in an initial public offering ("IPO").⁸ In 2006 and 2007,

² See *infra* notes 15–17, 59–70, 112–123 and accompanying text.

³ See *infra* notes 228–233 and accompanying text.

⁴ See *infra* notes 143–156, 262–265, 280–282 and accompanying text.

⁵ See *infra* notes 228–296 and accompanying text.

⁶ As the Delaware Court of Chancery stated in 2007 in *In re The Topps Co. S'holders Litig.*, 924 A.2d 951, 963 (Del. Ch. 2007), "Few contexts are more important to stockholders than the pendency of a transaction in which they exchange their shares for cash and the company is taken private."

⁷ See Orit Gadish & Hugh MacArthur, *Growing the "Private" Club*, WALL ST. J., May 25, 2007, at A14 ("[P]rivate-equity firms invest with a thesis for improving performance in a realistic, but aggressive time frame—three-to-five years."). Some private equity firms have an even shorter time horizon, taking companies private and then reselling them to the public within a year. Hertz, for example, was bought and resold in a twelve month period. See Michael J. de la Merced, *An I.P.O. Glut Just Waiting to Happen*, N.Y. TIMES, July 15, 2007, § 3, at 6.

⁸ See Dennis K. Berman & Henny Sender, *Big Buyout Firm Prepares to Sell Stake to Public*, WALL ST. J., Mar. 17–18, 2007, at A1 ("Private-equity firms buy either companies or divisions of companies on behalf of their own investors, take them private, and then sell them off within a few years."); Geoffrey Colvin & Ram Charan, *Private Lives*, FORTUNE, Nov. 27, 2006, at 190 ("Private-equity firms want to buy companies for their portfolio, fix them, grow them, and sell them in three to five years. The eventual buyer could be another com-

commentators, politicians, and antitrust regulators voiced their suspicions that private equity firms were colluding to artificially reduce the prices they pay for companies in going-private transactions.⁹

The structure of the private equity market facilitates collusion in going-private transactions. Only a few private equity firms have the financial capacity to bid for the largest going-private transactions.¹⁰ Markets such as private equity, in which only a small number of firms compete, are called oligopolies, and antitrust regulators examine them more closely because it is easier for competitors in such markets to engage in collusion.¹¹ Because of the small number of potential purchasers and their extended history of competing against one another, it is relatively easy for private equity buyers to allocate bids in change-of-control transactions without entering into an express agreement. By sending subtle signals to each other about their competitive intentions, such buyers can establish a pattern in which they take turns bidding for companies, thus reducing the purchase price each firm has to pay in a particular transaction. Such conduct reduces competition just as effectively as if the private equity buyers had entered into an express bid-rigging arrangement.¹²

Private equity firms can make substantial short-term profits when they are able to buy public companies at a favorable price.¹³ For example, in 2002, three private equity firms purchased Houghton Mifflin from Vivendi for \$1.7 billion.¹⁴ In 2006, the firms "sold the company again, more than tripling their investment in a few short years."¹⁵ A series of such profitable transactions has allowed private equity firms to achieve a 13% average annual return during the last decade.¹⁶ In 2006 alone, the annual return for all private equity funds was 25%, com-

pany in the portfolio company's industry, another private-equity firm, or the public, through an IPO.").

⁹ See *infra* notes 92–95, 112–123 and accompanying text.

¹⁰ See Ken MacFadyen, *Here Come the Ambulance Chasers: The DOJ's Inquiry into Private Equity Has Ignited Its 1st Class Action Lawsuit*, INVESTMENT READERS' DEALERS' DIGEST, NOV. 27, 2006, available at 2006 WLNR 2050743522265974.

¹¹ Thomas A. Piraino, Jr., *Regulating Oligopoly Conduct Under the Antitrust Laws*, 89 MINN. L. REV. 9, 9 (2004) ("In an oligopoly, a small number of sellers controls most of the sales in the relevant market.").

¹² See Andrew Ross Sorkin, *One Word Nobody Dares Speak*, N.Y. TIMES, Oct. 16, 2005, § 3, at 6.

¹³ See Dennis K. Berman, *The Game: Will Private Equity Suffer a Pushback?*, WALL ST. J., Jan. 2, 2007, at C1.

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ Edward Chancellor, *Private Equity: Hit or Miss*, WALL ST. J., Mar. 3–4, 2007, at B14.

pared to only 14% for the publicly traded companies listed on the Standard & Poor's 500 index.¹⁷ The owners of private equity funds have acquired enormous wealth by taking companies private at below-market prices and reselling them to the public shortly thereafter.¹⁸ Stephen Schwarzman, the co-founder of the Blackstone Group ("Blackstone"), the largest private equity firm, and Henry Kravis, the co-founder of Kohlberg Kravis Roberts & Co. ("KKR"), the second-largest private equity firm, have each become "a poster child of the private equity world."¹⁹ By 2007, Mr. Schwarzman had accumulated an estimated \$10 billion from going-private transactions.²⁰

There is now "a growing resentment of the buyout business,"²¹ fueled by the recognition that private equity firms are "buying public companies on the cheap so they can sell them later at a hefty profit."²² The *Wall Street Journal's* mergers and acquisitions journalist, Dennis K. Berman, has explained that "shareholders are beginning to see the money they're leaving on the table."²³ The *New York Times* has pointed out that "shareholders often feel that they are getting too low a premium when they see the private equity firms double their money seemingly overnight."²⁴ The *Wall Street Journal* has described shareholders' and regulators' conclusion that private equity firms "may be extracting too much value from publicly traded firms, leaving stockholders and customers in the lurch."²⁵ Jack LaPorte, the President of the T. Rowe Price New Horizons fund, argues that "we really feel that some of our best companies are being stolen out from under us. We

¹⁷ Lynn A. Stout, *Democracy by Proxy*, WALL ST. J., Mar. 8, 2007, at A16.

¹⁸ See Berman & Sender, *supra* note 8.

¹⁹ *Id.*

²⁰ Henny Sender, *Blackstone Plan Could Reshape Private Equity*, WALL ST. J., Mar. 19, 2007, at A1. Mr. Schwarzman's 60th birthday party in March 2007, which featured singer Rod Stewart and was emceed by actor Martin Short, was the talk of New York society. Henny Sender & Monica Langley, *Buyout Mogul: How Blackstone's Chief Became \$7 Billion Man*, WALL ST. J., June 13, 2007, at A1.

²¹ Andrew Ross Sorkin, *Of Private Equity, Politics and Income Taxes*, N.Y. TIMES, Mar. 11, 2007, § 3, at 7.

²² Berman, *supra* note 15.

²³ *Id.*

²⁴ Andrew Ross Sorkin, *Colluding or Not, Private Equity Firms Are Shaken*, N.Y. TIMES, Oct. 22, 2006, § 3, at 4; see also Shefali Anand, *Legg Mason Manager Thinks U.S. Stocks Are Inexpensive*, WALL ST. J., Jan. 12, 2007, at C1 (stating concern of mutual fund manager that "private equity groups are buying public companies at prices that are too low, short-changing existing investors").

²⁵ Henny Sender, *Dennis K. Berman & Rebecca Smith, Buyout Firms Seek Utility TXU for \$32 Billion*, WALL ST. J., Feb. 24-25, 2007, at A1.

have decided that enough is enough and we need to stand up for the rights of our shareholders."²⁶

Business history in the United States has been characterized by periods of excess, followed by periods of regulatory reform designed to redress such excesses. The anticompetitive conduct of the steel, oil, and railroad monopolies formed in the "Gilded Age" of the late nineteenth century caused Congress to enact the first federal antitrust law, the Sherman Act, in 1890.²⁷ Some commentators, eyeing the enormous fortunes being made in private equity, have named the first decade of the twenty-first century the "New Gilded Age" and have called for new federal laws to regulate such transactions.²⁸ Commenting on the position of private equity firms facing increased regulation, Steven Miller, a managing director at Standard & Poor's Leveraged Commentary and Data, has stated that "[i]t feels like Tony Soprano, sitting in the ice-cream parlor with all this trouble brewing around him, and wondering where the bullet might come from."²⁹

C. Potential Remedies for Collusion in Change-of-Control Transactions

Neither state corporate laws nor federal securities laws include remedies for collusion in change-of-control transactions.³⁰ Congress,

²⁶ Gretchen Morgenson, *Just Saying No to Lowball Buyout Offers*, N.Y. TIMES, May 20, 2007, § 3, at 1.

²⁷ See ROBERT H. BORK, *THE ANTITRUST PARADOX* 19–21 (2d prtg. 1993).

²⁸ For a description of the "New Gilded Age," see Louis Uchitelle, *The Richest of the Rich, Proud of a New Gilded Age*, N.Y. TIMES, July 15, 2007, at A1. Ben Stein has proposed that courts ban such transactions entirely, calling them "yet another sad sign of how our corporate trustees have lost their moral compass." Ben Stein, *On Buyouts There Ought to Be a Law*, N.Y. TIMES, Sept. 3, 2006, § 3, at 3. Andrew Ross Sorkin has put forth a more modest series of proposals under which investment bankers with conflicts of interest would be precluded from financing going-private transactions. Under Sorkin's proposal, a majority of shareholders would have to approve such transactions, and managements' business plans would be disclosed to shareholders so that they could decide whether the company could be operated more effectively by remaining public. Andrew Ross Sorkin, *Rewriting the Rules for Buyouts*, N.Y. TIMES, Nov. 19, 2006, § 3, at 4.

²⁹ Henny Sender & Sarah Lueck, *Tax Plan Adds to Pressures on Buyout Firms*, WALL ST. J., June 16–17, 2007, at A1. In March 2007, union officials from fifteen countries called on the industrialized countries to increase their regulation of buyout groups. *Id.* The House Financial Services Committee held hearings in 2007 on private equity transactions. The Chairman of the Committee, Barney Frank (D. Mass.), stated at that time, "When a small number of individuals benefit from a particular deal in the tens and sometimes hundreds of millions of dollars and concurrently, workers are laid off, we have a situation which seems to me wrong. . . . To the extent we see gross imbalances, then we're going to have to act." Andrew Ross Sorkin, *Sound and Fury over Private Equity*, N.Y. TIMES, May 20, 2007, § 3, at 6 (internal quotation marks omitted).

³⁰ See *infra* notes 124–135 and accompanying text.

however, need not enact any new laws to protect shareholders from such collusion. The Sherman Act already includes an adequate means of preventing such conduct. It is illegal under Section 1 of the Sherman Act for competitors to enter into any conspiracies or agreements "in restraint of trade."³¹ The classic antitrust violation involves a cartel, in which sellers agree to refrain from competing against each other on price or other terms of sale.³² Such agreements are routinely found to be per se violations of the antitrust laws.³³ In 2007, the U.S. Supreme Court pointed out in *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, that anticompetitive conduct by *purchasers* should be treated in the same manner as anticompetitive conduct by sellers.³⁴ The federal courts have held, in the context of a wide range of commercial transactions, that it is per se illegal for competing buyers to engage in bid rigging by agreeing to refrain from competing against each other for the purchase of particular goods or services.³⁵ It is now appropriate for the courts to use such precedent to preclude collusion in change-of-control transactions.

Shareholders have begun to file Sherman Act cases alleging that potential purchasers have conspired to limit competition in company auctions.³⁶ A 2006 class action complaint stated that consortiums formed by private equity firms to submit joint bids in going-private transactions reduced the price received by shareholders and that the firms unlawfully exchanged information and submitted bids at agreed-upon prices.³⁷ In September 2006, the United States Department of Justice (the "DOJ") began to investigate potential collusion among private equity firms.³⁸ The DOJ is focusing on contracts, correspondence, and e-mails in cer-

³¹ 15 U.S.C. § 1 (2006).

³² See Thomas A. Piraino, Jr., *A Proposed Antitrust Approach to Collaborations Among Competitors*, 86 IOWA L. REV. 1137, 1165-66 (2001).

³³ See *id.* at 1165-67.

³⁴ 127 S. Ct. 1069, 1075 (2007) ("[A] monopsony is to the buy side of the market what a monopoly is to the sell side." (citing Roger D. Blair & Jeffrey L. Harrison, *Antitrust Policy & Monopsony*, 76 CORNELL L. REV. 297, 301, 320 (1991))).

³⁵ See *infra* notes 234-236 and accompanying text.

³⁶ See *U.S. Investors File Lawsuit Against 13 Buyout Firms*, DAILY TELEGRAPH (London), Nov. 16, 2006, available at 2006 WLNR 19867557 (describing class-action lawsuit).

³⁷ See *id.*

³⁸ See Dennis K. Berman & Henny Sender, *Private Equity Firms Face Anticompetitive Probe*, WALL ST. J., Oct. 10, 2006, at A3; Brent Shearer, *Antitrust Inquiry Probes Club Deals*, DEAL MAKER'S JOURNAL, Dec. 1, 2006, available at 2006 WLNR 207622278; *DOJ Probes Private Equity Firms*, RED HERRING, Oct. 11, 2006, <http://www.redherring.com/Home/19112>.

tain transactions that may indicate that "buyout firms have been rigging corporate auctions."³⁹

D. *The Proposed Approach to Collusion in Change-of-Control Transactions*

The federal courts have erected several hurdles that prevent shareholders from obtaining an antitrust remedy for collusion in a change-of-control transaction. In 2007, for example, the United States Supreme Court in *Credit Suisse Securities (USA) LLC v. Billing* held that federal securities laws impliedly revoked the application of federal antitrust laws to the pricing conduct of underwriters in the IPOs of several hundred technology companies.⁴⁰ This Article explains, however, that the Court's rationale in *Credit Suisse*, when considered in the context of all the Court's decisions on implied revocation, should not preclude the lower federal courts from applying the antitrust laws to change-of-control transactions.

Once a shareholder surmounts the implied revocation issue, he will encounter other hurdles to a successful suit against potential purchasers that have colluded to reduce the purchase price in a change-of-control transaction. The federal courts, for example, have made it difficult for plaintiffs to prevail against the types of implicit conspiracies that are most likely to occur in company auctions.⁴¹ Because such implicit arrangements are often more durable than express agreements to limit competition, the courts' approach has had the perverse effect of applying the most lenient approach to the most harmful types of anti-competitive arrangements. This Article proposes a new approach to analyzing implicit bid rigging in change-of-control transactions that recognizes the adverse competitive effects of such arrangements and deters potential purchasers from continuing to engage in such conduct.⁴²

In recent years, potential purchasers have begun to form consortiums with their competitors—also known as "clubs"—to submit joint bids for companies.⁴³ In certain cases, such consortiums have a beneficial competitive effect because they allow their members to participate in bidding for a company that they did not have the ability to purchase

³⁹ Dennis K. Berman, *Cold Feet Aside, the Buyout Boom Has Legs*, WALL ST. J., July 3, 2007, at C1.

⁴⁰ 127 S. Ct. 2383, 2397 (2007); see *infra* notes 174–186 and accompanying text.

⁴¹ See *infra* notes 259–265 and accompanying text.

⁴² See *infra* notes 250–270, 311–346, and accompanying text.

⁴³ See Sorkin, *supra* note 12.

on their own.⁴⁴ In other cases, however, consortiums may reduce competition for the purchase of a company by substituting a single bid for what otherwise would have been multiple bids from each of the firms participating in the consortium.⁴⁵ Consortiums among bidders in change-of-control transactions are likely to be analyzed by the federal courts in the same manner as other "joint ventures" among competitors.⁴⁶ During the last several decades, the courts have struggled to define standards for the legality of joint ventures.⁴⁷ The courts' confusion has deterred American firms from entering into legitimate joint ventures that could enhance their efficiency.⁴⁸ This Article proposes a new approach to the analysis of consortiums in change-of-control transactions.⁴⁹ The approach should allow the courts to distinguish more effectively between legal and illegal arrangements, thereby encouraging potential purchasers to enter into consortiums that promote competition in change-of-control transactions and deterring them from participating in consortiums that limit such competition.

E. Organization of this Article

Part I of this Article discusses how private equity firms have been able to collude to reduce the prices paid for public companies to an artificially low level.⁵⁰ Part II explains why state corporate laws and federal securities laws have been unable to provide an effective remedy for collusion in change-of-control transactions, leaving the federal antitrust laws as the only potential means of preventing such conduct.⁵¹ Part III explains how, under the relevant Supreme Court precedent, the anti-

⁴⁴ See *id.*

⁴⁵ See *id.*

⁴⁶ Dennis W. Carlton & Steven A. Salop, *You Keep Knocking but You Can't Come in: Evaluating Restrictions on Access to Input Joint Ventures*, 9 HARV. J.L. & TECH. 319, 320 ("Current antitrust analysis of rules governing access to joint ventures is both confused and controversial.").

⁴⁷ See Thomas S. Jorde & David J. Teece, *Innovation, Cooperation, and Antitrust*, 4 HIGH TECH L.J. 1, 36 (1989) (stating that the courts' current approach to joint ventures "needlessly inhibits strategic alliances"); James Langenfeld & David Scheffman, *Innovation and U.S. Competition Policy*, 34 ANTITRUST BULL. 1, 19 (1989) (pointing out that U.S. competition policy has been overtly or indirectly used to penalize innovation); Alan J. Meese, *Farewell to the Quick Look: Redefining the Scope and Content of the Rule of Reason*, 68 ANTITRUST L.J. 461, 497 (2000) ("[C]ase law and enforcement policy treat many [joint ventures] as inherently suspect . . . even if they might plausibly produce the sort of efficiencies ordinarily cognizable under the Sherman Act.").

⁴⁸ See *infra* notes 323-333 and accompanying text.

⁴⁹ See *infra* notes 271-291, 347-386, and accompanying text.

⁵⁰ See *infra* notes 57-123 and accompanying text.

⁵¹ See *infra* notes 124-139 and accompanying text.

trust laws should continue to apply to anticompetitive conduct in change-of-control transactions.⁵² Part IV proposes a new antitrust approach that will effectively deter collusion in change-of-control transactions in a manner consistent with federal court precedent.⁵³ The final three parts explain how the proposed approach will deter express collusion,⁵⁴ tacit collusion,⁵⁵ and anticompetitive conduct undertaken in connection with consortiums.⁵⁶

I. ANTICOMPETITIVE CONDUCT IN GOING-PRIVATE TRANSACTIONS

A. *The Economic Rationale of Going-Private Transactions*

A new approach to the regulation of competition in change-of-control transactions should begin with an understanding of how collusion has occurred in recent years in the most prevalent type of acquisition, the going-private transaction. Private equity firms generally fund such transactions by increasing the amount of leverage in the company's capital structure, thereby increasing the risk—and potential return—to equity holders. In the last forty years, the popularity of such transactions has peaked during periods of low interest rates and high liquidity in the capital markets. Going-private transactions first became widespread in the 1970s, when they were called "bootstraps," because of buyout firms' ability to use an acquired company's assets to finance the debt used to purchase the company.⁵⁷ In the 1980s, such transactions were called "leveraged buyouts," or "LBOs."⁵⁸ The most famous leveraged buyout was the \$25 billion takeover of RJR Nabisco by KKR in 1988.⁵⁹ The transaction was immortalized in the best-selling book (and motion picture), *Barbarians at the Gate*, which criticized KKR for reducing employment, salaries, and benefits in order to repay the debt in-

⁵² See *infra* notes 142–217 and accompanying text.

⁵³ See *infra* notes 218–297 and accompanying text.

⁵⁴ See *infra* notes 298–310 and accompanying text.

⁵⁵ See *infra* notes 311–346 and accompanying text.

⁵⁶ See *infra* notes 347–386 and accompanying text.

⁵⁷ Andrew Ross Sorkin, *How to Show That You're No Gordon Gekko*, N.Y. TIMES, Mar. 25, 2007, § 3, at 8.

⁵⁸ *Id.*

⁵⁹ Dennis K. Berman et al., *KKR Is in Talks to Buy First Data*, WALL ST. J., Apr. 2, 2007, at A3.

curred in the transaction.⁶⁰ The book described the 1980s LBOs in words that are apt for today's private equity transactions:

In an LBO, a small group of senior executives, usually working with a Wall Street partner, proposes to buy its company from public shareholders, using massive amounts of borrowed money. Critics of this procedure called it stealing the company from its owners and fretted that the growing mountain of corporate debt was hindering America's ability to compete abroad. Everyone knew LBOs meant deep cuts in research and every other imaginable budget, all sacrificed to pay off debt. Proponents insisted the companies forced to meet stiff debt payments grew lean and mean. On one thing they all agreed: The executives who launched LBOs got filthy rich.⁶¹

By 2002, "private equity . . . [became] the new, sanitized name for the leveraged buyouts that had resulted in the scandals of the nineteen-eighties."⁶² From 2002 until mid-2007, economic conditions were perfectly aligned for private equity transactions, as extremely low interest rates and lax lending standards combined to make capital readily available to buyout firms.⁶³ After the September 11, 2001 terrorist attacks, the Federal Reserve Board (the "Fed") slashed interest rates, and, in 2003, cut the federal funds rate to 1% because of concerns about the possibility of deflation.⁶⁴ At the same time, there was "an unanticipated surge of capital pouring into the U.S. from overseas," as a result of what Ben Bernake, the Fed Chairman, has called a "global savings glut."⁶⁵ By 2006, driven by low interest rates and global liquidity, private equity transactions were "smashing records from the 1980s."⁶⁶ Between 2005 and mid-2007, there were 1287 private equity transactions, with a total value of \$787 billion.⁶⁷ Some of the largest and best-known American companies were acquired by private equity firms between 2002 and

⁶⁰ *Id.*; see also Jenny Anderson & Michael J. de la Merced, *Kohlberg Kravis Plans to Go Public*, N.Y. TIMES, July 4, 2007, at C1 (describing KKR as "the buyout firm immortalized in 'Barbarians at the Gate'").

⁶¹ BRYAN BURROUGH & JOHN HELYAR, *BARBARIANS AT THE GATE: THE FALL OF RJR NABISCO* 5 (1990).

⁶² James B. Stewart, *The Birthday Party*, NEW YORKER, Feb. 11 & 18, 2008, at 100, 107.

⁶³ Greg Ip & Jon E. Hilsenrath, *How Credit Got So Easy and Why It's Tightening*, WALL ST. J., Aug. 7, 2007, at A1.

⁶⁴ *Id.*

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ Merced, *supra* note 7.

2007, including Hertz Rent A Car, Neiman Marcus, Toys "R" Us, and Chrysler.⁶⁸ By 2007, private equity firms were "sitting on an estimated \$1.5 trillion of spending power."⁶⁹ KKR is "the industry doyen, flush with cash and on a worldwide hunt for prey."⁷⁰

James B. Stewart has explained the profit potential of the use of leverage in private equity transactions:

The power of leverage is vast: if you invest ten dollars in an asset and sell it a year later for twelve, you have earned twenty per cent. If you invest one dollar, borrow nine, pay a dollar in interest on the debt . . . and sell the asset for the same twelve dollars, your return is one hundred per cent.⁷¹

Henry Kravis stated in an interview in early 2007 that "I have never seen a time like this when money is so available and so global."⁷² As Gregory Zuckerman has explained, "Mostly, all the wheeling and dealing stems from lots of money sloshing around the global markets, as interest rates remain low. Investors are shoveling money at private-equity firms, which buy public companies or businesses with an eye toward reselling them later at a profit."⁷³ Ed Yardeni, the President of Yardeni Research, has stated that "the low interest rates that make bonds a relatively poor investment make it sensible to borrow and put the money to work buying stock, one company at a time."⁷⁴

By late 2007, the private equity boom began to wane, as interest rates increased and liquidity conditions in the credit markets tightened.⁷⁵ The *Wall Street Journal* explained that "the credit cycle's turn has taken the easy money out of the buyout business."⁷⁶ Economists pointed out, however, that at some point the credit cycle would again

⁶⁸ Colvin & Charan, *supra* note 8; Gina Chon, Jason Singer & Jeffrey McCracken, *Chrysler Deal Heralds New Direction for Detroit*, WALL ST. J., May 15, 2007, at A1.

⁶⁹ Jeffrey Ball, Dennis K. Berman & Joann S. Lublin, *Officials Fired at Dow Chemical for Secret Talks*, WALL ST. J., Apr. 13, 2007, at A1; *see also* Dennis K. Berman, *Unusual Buyout Offers a Piece to Shareholders*, WALL ST. J., Apr. 27, 2007, at A1 (stating that "spending power" of private equity firms has been "estimated at \$1.5 trillion by Morgan Stanley").

⁷⁰ Sender, Berman & Smith, *supra* note 25.

⁷¹ Stewart, *supra* note 62, at 107.

⁷² Sender, Berman & Smith, *supra* note 25.

⁷³ Gregory Zuckerman, *Place Your Bets, Please: Takeover Wheel Spins*, WALL ST. J., Nov. 22, 2006, at C1.

⁷⁴ Conrad de Aenlle, *Stocks Cheap? Private Equity Thinks So*, N.Y. TIMES, May 20, 2007, § 3, at 4.

⁷⁵ Lauren Silva & Rob Cox, *The Real Deal for Buyouts*, WALL ST. J., Aug. 27, 2007, at C8; *see also* Ip & Hilsenrath, *supra* note 63 (pointing out tightening conditions in the credit markets).

⁷⁶ Silva & Cox, *supra* note 75.

turn in favor of going-private transactions.⁷⁷ James Grant, the editor of *Grant's Interest Rate Observer*, stated that "[t]he history is that lenders move in great caravans between two extreme points, which we can call stringency and accommodation," and he opined that "[l]enders will move back to accommodation one day."⁷⁸ It is therefore likely that as the credit cycle turns, private equity transactions will regain their popularity, and the competitive problems raised by such transactions will re-occur, as they have regularly during the last thirty years. As Robert Pozen, the Chairman of MFS Investment Management, stated in December 2007, "Although private equity funds are currently on hold because of the credit crisis, they are very large and will return to action."⁷⁹

B. Management's Conflict of Interest in Going-Private Transactions

There is an inherent conflict of interest between the managers and the shareholders of public companies, stemming from the separation of ownership and control in a public corporation. Although management controls all of the day-to-day activities of a public company, it is expected to run the company not in its own interest, but as the agent of the company's owners—the shareholders. Because management has control of a public company, it is difficult to resist the temptation to operate the company in its own interests. Commentators have referred to this conflict of interest as the "agency problem"—management is required to act as the agent of the shareholders, but as an agent, management has the ability to act in its own interests instead.⁸⁰

The agency problem is particularly acute in going-private transactions, where managers are included as members of the buyout team and are usually promised large equity stakes in the new private entity.⁸¹ Going-private transactions possess the classic characteristics of a conflict

⁷⁷ Floyd Norris, *The Loan Comes Due*, N.Y. TIMES, Aug. 5, 2007, at WK1.

⁷⁸ *Id.*

⁷⁹ Robert C. Pozen, *Target-Proof Your Company*, WALL ST. J., Nov. 23, 2007, at A12.

⁸⁰ See Gretchen Morgenson, *It's Just a Matter of Equity*, N.Y. TIMES, Sept. 16, 2007, § 3, at 1 ("[T]he so-called agency problem[] [is] a product of corporate structures that allow managers—i.e., agents—to feather their own nests at the expense of owners—i.e., investors—whose interests they are supposed to serve."); see also Ben Stein, *Enron, the Supreme Court and Shareholders on the Brink*, N.Y. TIMES, Apr. 29, 2007, § 3, at 6 (stating that shareholders are "the ultimate owner of a public company, the ultimate boss, the ultimate trustor to whom the highest standards of fiduciary care [are] owed" and that these duties include "the duty to put the interests of the stockholder ahead of the interests of the managers and their agents in each and every situation").

⁸¹ Ball, Berman & Lublin, *supra* note 69; see also Morgenson, *supra* note 80 ("Agency problems, precisely what private equity was supposed to eliminate, are cropping up as a result of the disastrous changes made by these firms.").

of interest, with management on both sides of the deal.⁸² Instead of being aligned with the interests of the public shareholders, management's interests in a going-private transaction are most congruent with those of the private equity firms that are purchasing the company.⁸³

When a company is offered for sale to a private equity firm, management has a fiduciary obligation to attempt to obtain the highest possible price for the shareholders.⁸⁴ On the one hand, managers' stock options and other equity incentive plans will motivate managers to obtain such a high price. But, on the other hand, private equity firms usually grant management an even greater amount of equity incentives in the new private company formed after the purchase of shares from the public shareholders.⁸⁵ Such equity grants induce management to support the bid of the private equity firm that is most likely to acquire a company at a lower price more favorable to management than to the public shareholders.⁸⁶ As the *Wall Street Journal* has explained, "Private equity firms generally need the support of management when making a bid for a public company. By giving management equity, that support is usually forthcoming."⁸⁷ "Suitors . . . promise big paydays, which typically come in the form of an ownership stake—potentially 1% to 2% . . . [of larger companies]."⁸⁸ In the \$45 billion private equity buyout of the Texas utility company, TXU, in February 2007, the executives of TXU were allowed to roll over their 5% equity interest into the new company and were granted stock options that would allow them to acquire an additional 5% of the company.⁸⁹ In the recent going-private transaction involving Aramark Corporation, the company's Chief Executive Officer converted his Aramark shares, valued at \$250 million, into an equity interest in the company after it was taken private.⁹⁰

⁸² Ball, Berman, & Lublin, *supra* note 69; see also Morgenson, *supra* note 80.

⁸³ See Morgenson, *supra* note 80.

⁸⁴ See *infra* notes 124–131 and accompanying text.

⁸⁵ See *The LBO Boom's Real Fuel*, WALL ST. J., Mar. 30, 2007, at B14 ("[I]f . . . [management] decide[s] to stay on they're normally lavished with large chunks of the newly privatized company."). "After the technology firm SunGard Data Systems was taken private in the summer of 2005, senior managers received an equity stake that could be worth up to 15% of the company." *Id.*; see also *On Going Private: Investors Beware*, WALL ST. J., Nov. 18–19, 2006, at B14 ("Private-equity firms often shower executives with incentives to stay and either bring the company back to the public markets or sell it.").

⁸⁶ Ball, Berman & Lublin, *supra* note 69.

⁸⁷ Rebecca Smith, Dennis K. Berman & Henny Sender, *Power Play: Bidders Try to Pre-empt Gridlock in TXU Deal*, WALL ST. J., Feb. 26, 2007, at A1.

⁸⁸ Ball, Berman & Lublin, *supra* note 69.

⁸⁹ Smith, Berman & Sender, *supra* note 87.

⁹⁰ Joseph Neubauer, *Buyout Nets Aramark CEO \$1B*, BUCKS COUNTY COURIER TIMES (Levittown, Pa.), Feb. 2, 2007, at B1, available at 2007 WLNR 2128263.

Several commentators have pointed out management's conflict of interest in going-private transactions. James Woolery, an attorney at Cravath, Swain & Moore LLP, has explained, "It's the absolute worst way to negotiate as a public company It's like having someone from an opposing team in your locker room during half time."⁹¹ Robert Damon, a professor of finance at the Tepper School of Business at Carnegie Mellon University, has explained, "Management is supposed to serve shareholders and get the best price possible On the other side, the same management is serving as the buyer and wants to sell the company as cheaply as possible."⁹² Andrew Ross Sorkin has stated that "[i]t's hard to understand how shareholders can trust management to represent their interests when it is trying to make off with the company. It's a conflict-ridden mess."⁹³ "When you are both a buyer and a seller of your company, how can you lose?"⁹⁴ Ben Stein recently described management's conflict of interest in stark terms:

[I]n a management buyout, management is seeking to pay the least it can get away with for the assets of the public holders, while the public holders want the most they can get. On its face, this is an irreconcilable conflict of interest. . . . Why this kind of conflict is allowed is a mystery to me.⁹⁵

C. *Management's Incentive to Keep Sales Prices Low in Going-Private Transactions*

Because management often will have a greater equity interest in the new private company formed after a going-private transaction, it will have an incentive to keep the price paid for the public company in the original transaction as low as possible, in order to reap greater profits on the later resale of the company to the public.⁹⁶ Thus, instead of

⁹¹ Ball, Berman & Lublin, *supra* note 69.

⁹² *Buyouts too Good to Managers?*, BUCKS COUNTY COURIER TIMES (Levittown, Pa.), Nov. 17, 2006, at B1, available at 2006 WLNR 20119812 (internal quotation marks omitted).

⁹³ Sorkin, *supra* note 28.

⁹⁴ Andrew Ross Sorkin, *Wheeling, Dealing and Reeling*, N.Y. TIMES, Dec. 31, 2006, § 3, at 1.

⁹⁵ Stein, *supra* note 28.

⁹⁶ See Kimble Charles Cannon, *Augmenting the Duties of Directors to Protect Minority Shareholders in the Context of Going-Private Transactions*, 2003 COLUM. BUS. L. REV. 191, 221 ("Going-private transactions in which controlling shareholders are members of the acquisition group present a situation in which the opportunity for conflicts of interest is ripe. A party exercising control over directors and officers stands to profit from an acquisition transaction, and its interests diverge from those of other shareholders."). Managers faced with the possibility of participating in a going-private transaction may also have the perverse incen-

pursuing the shareholders' interest in maximizing the purchase price for a public company, management will be inclined to facilitate collusive conduct in the auction process that will reduce the price paid for a public company.⁹⁷ It will be in management's interest to work with only one potential buyer in the auction process and to exclude other potential buyers so that, with less competition, the price paid for the company is as low as possible. A low price means that management and the private equity firms will be able to acquire equity in the new private company at a lower cost basis. It also means that the company will not be as highly leveraged with debt issued to purchase shares from the public shareholders. A lower debt to equity ratio will make the company more attractive when it is sold a few years after the going-private transaction. In the proxy sent to shareholders in connection with the Aramark transaction, the buyout team even admitted that it was attempting to "negotiate the terms of a transaction that would be most favorable to themselves, and not to the stockholders of the company and, accordingly, did not negotiate the merger agreement with the goal of obtaining terms that were fair to such shareholders."⁹⁸

D. Management's Ability to Control the Auction Process

Management has considerable leeway to control the terms of the auction process in ways that limit the number of potential bidders. As Dennis K. Berman has pointed out:

[T]op executives carry enormous clout in buy out situations. Their knowledge and influence can subtly, or not so subtly, push a deal and its terms to a personally beneficial outcome. And they can advance a favored deal so far along that competing bidders won't come near it.⁹⁹

Andrew Ross Sorkin has explained:

tive to limit the company's profitability and business prospects prior to a buyout in order to minimize the price paid for the company. As Henry Ellenbogen, a manager of the T. Rowe Price Media and Telecommunications Fund, has explained, "As a marketplace, you can't have an asset where people run it poorly, and put in incentives for them to cash it out at a lower price." Dennis K. Berman & Sarah McBride, *Clear Channel Showdown Signals Investor Wariness of Private Buyouts*, WALL ST. J., Jan. 27-28, 2007, at A1.

⁹⁷ See Berman & McBride, *supra* note 96.

⁹⁸ *Buyouts too Good to Managers?*, *supra* note 92.

⁹⁹ Dennis K. Berman, *The Game: Fine Line of Selling, Selling Out, the Firm*, WALL ST. J., Jan. 30, 2007, at C1. Indeed, the chief executives of some public companies have negotiated the initial terms of going-private transactions with buyout firms without even informing their boards of directors of the potential transaction. *Id.*

The seller decides whether a bid is high enough, and if it isn't, there is no sale. The seller can typically also manage an auction process however it wants. In some cases, sellers have selected which private equity firms will be teamed up with one another, to avoid any one team from becoming too strong. If a private equity suitor objects to the process, it is invited to leave.¹⁰⁰

Management often asks an investment banker with which it already has strong business ties to run the auction process.¹⁰¹ For example, Goldman Sachs oversaw the auction process in the going-private transaction for Clear Channel Communications. Goldman had been the long-time banker for the Mays family, which controlled Clear Channel.¹⁰² In addition, Goldman provided \$10 billion of financing for the transaction.¹⁰³ The "lightning-fast auction" conducted by Goldman produced only two bids for the company.¹⁰⁴ Competing bidders were given only three weeks "for researching and arranging financing for one of the largest media transactions in history."¹⁰⁵ The only two bids were from groups of private equity firms that were willing to retain management after the company was taken private.¹⁰⁶

With its control over the auction process and the selection of the outside advisors that oversee the process, management can easily steer a transaction to a private equity firm that will provide a low price most favorable to management.¹⁰⁷ Management's ability to select its preferred private equity firm facilitates collusion in the auction process for public companies.¹⁰⁸ Once management selects its preferred firm, other potential buyers are less likely to bid, allowing the preferred buyer to obtain a favorable price.¹⁰⁹ Under such circumstances, the private equity firms excluded from the auction process have a greater incentive to reach an explicit or implicit understanding with the winning bidder that it will step aside in future transactions in which another private equity firm is selected by management as the preferred bidder.¹¹⁰

¹⁰⁰ Sorkin, *supra* note 24.

¹⁰¹ Sorkin, *supra* note 28.

¹⁰² *Id.*

¹⁰³ *Id.*

¹⁰⁴ Sarah McBride & Dennis K. Berman, *Clear Channel Buyout Talks Fuel Concern of Management Conflicts*, WALL ST. J., Nov. 14, 2006, at A1.

¹⁰⁵ *Id.*

¹⁰⁶ *Id.*

¹⁰⁷ See Berman, *supra* note 99; Sorkin, *supra* note 24; Sorkin, *supra* note 28.

¹⁰⁸ See Sorkin, *supra* note 24.

¹⁰⁹ See *id.*

¹¹⁰ See *id.*

E. Evidence of "Windfall" Profits in Going-Private Transactions

There is substantial evidence that private equity firms have benefited from purchasing companies at artificially low prices in going-private transactions.¹¹¹ The *New York Times* recently described a working paper by the National Bureau of Economic Research that analyzed acquisitions of public companies completed from 1990 through 2005.¹¹² The study concluded that "target shareholders receive 55 percent more if a public firm instead of a private equity fund makes the acquisition."¹¹³ The study "was unable to account for this disparity in terms of any observable differences in the kind of companies that were acquired."¹¹⁴ Jack LaPorte of T. Rowe Price New Horizons fund has stated that strategic mergers among operating companies "have historically been done at premiums of 20 percent to 25 percent above the target's prevailing stock price," though recent private equity deals "have resulted in premiums of only 10 percent to 15 percent."¹¹⁵

Because they are purchasing public companies at artificially low prices, managers and their favored private equity firms have been able to reap extraordinary windfall profits in short periods of time.¹¹⁶ Blackstone bought out the public shareholders of Celanese Corporation in 2004 and made back "nearly six times its investment" in the transaction when it took the company public again in 2005.¹¹⁷ The company's executives received options for 7.8 million shares in the new public company and the right to purchase another 1.6 million shares at a deep discount from the public offer price.¹¹⁸ These equity grants increased management's compensation in the IPO by \$65 million.¹¹⁹ As the *Wall Street Journal* pointed out, "[I]t's hard to believe

¹¹¹ See Mark Hulbert, *Shareholders Benefit When Managers Have a Serious Stake*, N.Y. TIMES, May 13, 2007, § 3, at 5 (discussing Leonce Barger et al., *Why Do Private Acquirers Pay So Little Compared to Public Acquirers?* (Nat'l Bureau of Econ. Research, Working Paper No. 13061, 2007), available at <http://www.nber.org/papers/w13061>).

¹¹² See *id.*

¹¹³ *Id.* (internal quotation marks omitted).

¹¹⁴ *Id.* "It was not the case, for example, that private equity firms tended to purchase less profitable companies than public bidders did. Nor did private equity firms tend to acquire companies that were growing more slowly, or ones whose recent stock performance was poorer." *Id.*

¹¹⁵ Morgenson, *supra* note 26.

¹¹⁶ Sender & Langley, *supra* note 20.

¹¹⁷ *Id.*

¹¹⁸ John Christy, Rob Cox & Edward Chancellor, *On Going Private: Investors Beware*, WALL ST. J., Nov. 18–19, 2006, at B14.

¹¹⁹ *Id.*

that Celanese's managers could have made such a pile without taking the company private and at the price they did."¹²⁰

In 1988, Kraft, Inc. sold its battery subsidiary, Duracell, to KKR and members of Duracell's management at a price of approximately \$5 per share. In 1996, Gillette bought Duracell for approximately \$55 per share, eleven times the price paid by management just eight years earlier.¹²¹ The founder of Metromedia, John W. Kluge, took the company private for approximately \$43.50 per share and "sold off the pieces of the company for about eight times as much, making himself one of the richest men in the nation off profits on assets that had belonged to [the] public stockholders."¹²² Ben Stein has described memos from a Securities and Exchange Commission ("SEC") investigation of a proposed going-private transaction involving Narragansett Capital, which revealed "how much management and its investors expected to make on their money, and how much they thought the assets were worth. The profits were going to be breathtaking, and the amounts they were paying [the shareholders] were comical compared with what the company was worth."¹²³

II. POTENTIAL REMEDIES AGAINST COLLUSION IN CHANGE-OF-CONTROL TRANSACTIONS

Currently, shareholders can look to three regulatory areas for a potential remedy against collusion in change-of-control transactions: state corporate laws on managers' fiduciary duties, federal securities statutes, and federal antitrust laws. Only the antitrust laws, however, are capable of providing an effective remedy for such collusion.

A. *State Corporate Laws on Managers' Fiduciary Duties*

Under the relevant state corporate laws, managers of an acquired company should not be liable when the purchase price for their company is reduced as a result of collusion among potential purchasers. State corporate laws require management to observe its fiduciary duties to shareholders by attempting to obtain the highest "available" price in a change-of-control transaction.¹²⁴ In a change-of-control transaction,

¹²⁰ *Id.*

¹²¹ Cannon, *supra* note 96, at 200.

¹²² Stein, *supra* note 28.

¹²³ *Id.*

¹²⁴ See, e.g., *Paramount Commc'ns v. QVC Network, Inc.*, 637 A.2d 34, 43, 45 (Del. 1994) (holding that directors' approval of a merger transaction was subject to "enhanced

however, managers can protect themselves from fiduciary liability by observing certain procedural due process standards, such as disclosing their conflict of interest in the transaction,¹²⁵ referring the approval of the transaction to a committee of independent directors, avoiding "no-shop" or similar agreements that prevent competing bids,¹²⁶ and obtaining an opinion on the "fairness" of the transaction from an investment bank.¹²⁷ Fairness letters are often tailored to benefit management because it is management that selects and pays the fees of an investment banker. As Ben Stein has explained, "Investment banks never cross management any more than appraisers cross lenders. Fairness letters, like appraisals, are usually 'M.A.I.'—made as instructed."¹²⁸ Jack LaPorte of T. Rowe Price has pointed out:

[D]irectors are increasingly hiding behind "independent committees" of the boards and fairness opinions which Wall Street firms will gladly provide, creating an outcome that while technically meeting the legal requirements is really not allowing companies to realize their long-term value.¹²⁹

Corporate managers can avoid the application of state fiduciary laws entirely simply by proving that they made their best efforts to obtain the highest available price in a change-of-control transaction.¹³⁰ They can, for example, assert that they attempted to convince the win-

scrutiny" because the stockholders were losing the opportunity to obtain a control premium in the future); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182–85 (Del. 1986); *In re Netsmart Techs., Inc. S'holders Litig.*, 924 A.2d 171, 199 (Del. Ch. 2007) (holding that, in a going-private transaction, board likely violated its fiduciary duty by failing to adequately explore alternative transaction with strategic buyer).

¹²⁵ See *In re Lear Corp. S'holder Litig.*, 926 A.2d 94, 98 (Del. Ch. 2007) (requiring disclosure in proxy statement for going-private transaction of benefits CEO would receive in transaction).

¹²⁶ See *id.* at 97–98 (finding that, in going-private transaction, board did not violate fiduciary duties because it retained "broad leeway to shop the company after signing, and negotiated deal protection measures that did not present an unreasonable barrier to any second-arriving bidder").

¹²⁷ See, e.g., *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711–14 (Del. 1983); *Solar Cells, Inc. v. True North Partners, LLC*, 2002 WL 749163, at *6 (Del. Ch. 2002); Cannon, *supra* note 96, at 216 (stating that officers and directors can protect themselves against liability in change-of-control transactions by obtaining "an opinion as to the fairness of the acquisition bid from a financial advisor of the [Board's] choosing"); Stein, *supra* note 28 ("[M]anagement and its worthy friends say that all is solved because it gets a 'fairness letter' from an investment bank saying that the price it is offering for the stock is fair").

¹²⁸ Stein, *supra* note 28.

¹²⁹ Morgenson, *supra* note 26.

¹³⁰ See Sorkin, *supra* note 28.

ning bidder to "bump" its bid above its original offer.¹³¹ Even if private equity firms agree among themselves to refrain from competing in an auction or to form consortiums to submit joint bids, management can argue that it had nothing to do with such decisions and was unable to obtain additional offers for the company. If shareholders are disappointed in the price received in a going-private transaction, their remedy should lie against the private equity firms that colluded to limit competition in the bidding process and not against the managers or directors of the company, whose only recourse was to negotiate with the firms willing to participate in the process.

B. Federal Securities Law Remedies

Neither federal securities laws nor SEC rules preclude potential purchasers from conspiring to limit competition in auctions for the sale of shares of public companies.¹³² Indeed, they do not contain any regulation of bid rigging in transactions for the sale of public companies.¹³³ The Williams Act merely precludes "fraudulent, deceptive, or manipulative" practices in the sale of the shares of a public company and requires disclosure of any joint offer to purchase the shares of such a company.¹³⁴ As the U.S. Court of Appeals for the Second Circuit acknowledged in 1990 in *Finnegan v. Campeau Corp.*, the SEC, in its regulations implementing the Williams Act, has "chosen not to prohibit agreements between rival bidders as fraudulent or manipulative practices once shareholders are properly informed of them."¹³⁵ As long as bidders observe the disclosure provisions of the Williams Act, they will be deemed to be in compliance with that law, even if they engage in an express bid-rigging conspiracy that would be per se illegal under the Sherman Act.¹³⁶

C. Antitrust Remedies

Unlike either state corporate law or federal securities laws, federal antitrust laws were intended to compensate parties injured as a result of anticompetitive conduct, including conspiracies among actual or potential competitors in the purchase of goods or services.¹³⁷ By imposing

¹³¹ See *id.*

¹³² See Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (2006).

¹³³ See *id.*

¹³⁴ *Id.*

¹³⁵ 915 F.2d 824, 831 (2d Cir. 1990).

¹³⁶ See *id.*

¹³⁷ See *infra* notes 228-236 and accompanying text.

substantial sanctions (including treble damages and criminal liability), antitrust laws could deter potential purchasers from limiting competition in the market for the purchase of control of public companies. Indeed, in late 2006, the DOJ began to investigate the competitive practices of private equity firms in going-private transactions.¹³⁸ Referring to letters directed to four large private equity firms in connection with the investigation, Andrew Ross Sorkin has concluded, "While it was never asked directly, the letters could have been only one sentence long: 'Are you colluding to drive down buyout prices?'"¹³⁹

Unfortunately, the federal courts have erected several hurdles against a successful antitrust suit by shareholders for the diminution in the value of their shares caused by collusion in change-of-control transactions.¹⁴⁰ The most significant hurdle will be defendants' arguments that, under *Credit Suisse*, the antitrust laws cannot apply to such collusion at all because they have been impliedly revoked by the federal securities laws.¹⁴¹ As the next Section of this Article explains, however, a proper reading of all the Supreme Court's decisions on implied revocation, including *Credit Suisse*, reveals that the antitrust laws can provide an effective remedy against collusion in change-of-control transactions.

III. APPLYING ANTITRUST LAWS IN CHANGE-OF-CONTROL TRANSACTIONS

The issue of implied revocation arises when antitrust laws potentially preclude conduct that is permitted by another federal law or regulation, and the law or regulation does not explicitly state whether it precludes application of antitrust laws.¹⁴² As the U.S. Supreme Court stated in 2007 in *Credit Suisse*, in such cases the "courts must determine whether, and in what respects [regulatory statutes] implicitly preclude application of the antitrust laws."¹⁴³ In 1990, in *Finnegan v. Campeau Corp.*, the U.S. Court of Appeals for the Second Circuit held that the antitrust laws were impliedly revoked by the federal securities laws when potential purchasers for a public company agreed to end their bidding in an auction process.¹⁴⁴ The Second Circuit's

¹³⁸ See DOJ Probes Private Equity Firms, *supra* note 38.

¹³⁹ Sorkin, *supra* note 24.

¹⁴⁰ See, e.g., *Credit Suisse Sec. (USA) LLC v. Billing*, 127 S. Ct. 2383, 2389 (2007) (holding that federal securities laws impliedly revoked application of federal antitrust laws in pricing conduct of IPO underwriters).

¹⁴¹ See *id.*

¹⁴² See, e.g., *id.*; *Finnegan v. Campeau Corp.*, 915 F.2d 824, 829-30 (2d Cir. 1990).

¹⁴³ 127 S. Ct. at 2389.

¹⁴⁴ 915 F.2d at 829-30.

decision in *Finnegan* has broad implications for the enforcement of the antitrust laws when potential purchasers engage in bid rigging in change-of-control transactions. If *Finnegan* were applied in such cases, shareholders would have no remedy for the diminution in the value of their shares resulting from such anticompetitive conduct.¹⁴⁵ The Supreme Court's recent decision in *Credit Suisse*, however, has clarified the standard for determining whether the federal securities laws impliedly revoke the antitrust laws.¹⁴⁶ Although the Supreme Court's decision is not directly applicable to change-of-control transactions, the Court's approach should ensure that *Finnegan* will no longer be considered good law and that the antitrust laws will apply to bid rigging in change-of-control transactions for public companies.¹⁴⁷

A. *Finnegan* & Antitrust in Change-of-Control Transactions

In *Finnegan*, the shareholders of Federated Department Stores ("Federated") alleged that two rival bidders, R.H. Macy & Co., Inc. ("Macy's") and Campeau Corp. ("Campeau"), violated Section 1 of the Sherman Act by agreeing to discontinue their bidding to purchase Federated.¹⁴⁸ In March 1988, Macy's and Campeau pushed up the price of Federated stock as they each submitted progressively higher bids.¹⁴⁹ In April 1988, Macy's agreed to withdraw its bid in exchange for an agreement by Campeau to pay Macy's \$60 million for banking and legal expenses and to allow Macy's to purchase two divisions of Federated.¹⁵⁰ As a result of this agreement, Campeau was able to purchase Federated for \$172 million less than Macy's most recent bid.¹⁵¹

The Second Circuit concluded that the bidding arrangement between Macy's and Campeau could not be illegal under the Sherman Act because it was permitted under the Williams Act.¹⁵² The court pointed out that the Williams Act gave the SEC the authority to (1) require the disclosure of bidding arrangements among the purchasers of public companies, such as the one between Macy's and Campeau, and (2) regulate any fraudulent, deceptive, or manipulative practices by

¹⁴⁵ See *id.*

¹⁴⁶ See *Credit Suisse*, 127 S. Ct. at 2390.

¹⁴⁷ See *id.*

¹⁴⁸ *Finnegan*, 915 F.2d at 826.

¹⁴⁹ *Id.*

¹⁵⁰ *Id.* (taking Macy's agreement to withdraw its bid as fact for the purposes of its review).

¹⁵¹ *Id.*

¹⁵² *Id.* at 830-31.

bidders for public companies.¹⁵³ The Second Circuit concluded that, because the SEC had the power to regulate bidders' agreements, it had implicitly authorized such agreements.¹⁵⁴ Permitting an antitrust suit against such agreements "would foster a direct conflict between the securities and antitrust laws."¹⁵⁵ Accordingly, the court found that the antitrust laws were impliedly revoked by the securities laws and that the complaints of the Federated shareholders against Macy's and Campeau should be dismissed.¹⁵⁶

B. Supreme Court Precedent Prior to *Credit Suisse*

There is a long history of Supreme Court jurisprudence on implied revocation, stretching back to the early 1960s.¹⁵⁷ The Court's decisions indicate that the antitrust laws should only be deemed to be impliedly revoked in those narrow circumstances in which the SEC has exercised its authority to permit a specific type of competitive conduct that would have been illegal under the antitrust laws.¹⁵⁸

In 1963, in *Silver v. New York Stock Exchange, Inc.*, the Court considered whether the federal securities laws impliedly revoked the application of the antitrust laws to the refusal by the New York Stock Exchange ("NYSE") to permit nonmembers to access its private telephone connections.¹⁵⁹ Emphasizing the "cardinal principle of construction that repeals by implication are not favored," the Court concluded that "repeal [of the antitrust laws] is to be regarded as implied only if necessary to make the . . . [securities laws] work, and even then only to the minimum extent necessary."¹⁶⁰ Because the SEC had no power to supervise enforcement of the rules regulating the NYSE, the Court held that enforcement of the antitrust laws would not disturb the SEC's regulatory scheme.¹⁶¹

¹⁵³ *Finnegan*, 915 F.2d at 830-31.

¹⁵⁴ *Id.* at 831.

¹⁵⁵ *Id.* at 830 ("We cannot presume that Congress has allowed competing bidders to make a joint bid under the William Acts and the SEC's regulations and taken that right away by authorizing suit against such joint bidders under the antitrust laws.")

¹⁵⁶ *Id.* at 832.

¹⁵⁷ See generally *United States v. Nat'l Ass'n of Sec. Dealers, Inc.*, 422 U.S. 694 (1975); *Gordon v. N.Y. Stock Exch., Inc.*, 422 U.S. 659 (1975); *Silver v. N.Y. Stock Exch.*, 373 U.S. 341 (1963).

¹⁵⁸ See *Nat'l Ass'n of Sec. Dealers*, 422 U.S. at 719-20; *Gordon*, 422 U.S. at 682; *Silver*, 373 U.S. at 357.

¹⁵⁹ 373 U.S. at 342-43.

¹⁶⁰ *Id.* at 357.

¹⁶¹ *Id.* at 360.

In 1975, in *Gordon v. New York Stock Exchange, Inc.*, the Court considered whether it was illegal under the Sherman Act for the NYSE and the American Stock Exchange to set fixed commission rates.¹⁶² The exchanges argued that, because the SEC was given direct authority under the Securities and Exchange Act to regulate and fix reasonable commission rates, the antitrust laws could not also regulate such rates.¹⁶³ The Court acknowledged that an "implied repeal" of the antitrust laws could only be found "where there is a 'plain repugnancy' between the antitrust and regulatory provisions."¹⁶⁴ The Court, however, agreed with the exchanges that the antitrust laws were inapplicable to their conduct, emphasizing the active role that the SEC had taken in ensuring that commission rates were adequately regulated.¹⁶⁵ In the Court's opinion, subjecting brokers' commissions to antitrust regulation would conflict with the SEC's regulation of such commissions.¹⁶⁶

United States v. National Association of Securities Dealers, Inc., which the Supreme Court decided on the same day as *Gordon*, involved various restrictions imposed by the National Association of Securities Dealers ("NASD"), mutual fund companies, and broker-dealers on the trading of mutual fund shares in the secondary market after the initial distribution of mutual fund shares.¹⁶⁷ The defendants argued that the antitrust laws were impliedly repealed by the Investment Company Act of 1940, which gave the SEC the right to regulate the sale of mutual fund shares.¹⁶⁸ As in *Gordon*, the Court concluded that the SEC had exercised regulatory authority over the relevant conduct.¹⁶⁹ The SEC's decision not to prohibit the restrictions on trading securities in the secondary market reflected its implicit authorization of such conduct.¹⁷⁰ That authorization could not be reconciled with application of the antitrust laws, under which the restrictions would have been per se illegal.¹⁷¹

¹⁶² 422 U.S. 659, 660 (1975).

¹⁶³ *Id.* at 688-89.

¹⁶⁴ *Id.* at 682 (quoting *United States v. Phila. Nat'l Bank*, 374 U.S. 321, 350-51 (1963)).

¹⁶⁵ Congress had specifically granted the SEC "the power to fix and insure reasonable rates" of commission, *id.* at 666, and the SEC had effectively authorized the use of fixed rates during the relevant time period. *Id.* at 667-75.

¹⁶⁶ *Id.* at 689.

¹⁶⁷ 422 U.S. at 701-03.

¹⁶⁸ *Id.* at 704.

¹⁶⁹ *Id.* at 721.

¹⁷⁰ *Id.* at 728, 733.

¹⁷¹ *Id.* at 729, 733.

C. The Supreme Court's Current Approach: Credit Suisse

The plaintiffs in *Credit Suisse* were sixty investors in stock issued by internet and technology companies during the stock market bubble of the late 1990s.¹⁷² They filed two class actions alleging that, at the heart of the dot-com boom, ten leading investment banks, acting as underwriters, conspired to inflate aftermarket stock prices in IPOs for several hundred technology companies.¹⁷³ The suits alleged that the underwriters had, among other things, agreed among themselves to require investors to pay anticompetitive charges "over and above the agreed-upon IPO share price plus underwriting commission."¹⁷⁴ The plaintiffs claimed that such conduct was designed to inflate the price of securities in the aftermarket after the completion of an IPO and that the conduct constituted a conspiracy in restraint of trade under Section 1 of the Sherman Act.¹⁷⁵ The defendants argued that, because the SEC regulated their conduct in IPOs, the conduct should be exempt from antitrust liability.¹⁷⁶ In its 2007 decision, the Supreme Court agreed with the defendants, holding that the antitrust laws were impliedly revoked by the securities laws for the conduct challenged in the complaints.¹⁷⁷

The Court acknowledged that its prior cases had established that the antitrust laws could only be impliedly revoked by the federal securities laws when there was "a plain repugnancy" between antitrust and securities regulation.¹⁷⁸ The Court set forth a strict four-factor test for determining when the antitrust laws are impliedly revoked by the federal securities laws: (1) the conduct at issue must be "squarely within the heartland of securities regulation," (2) the SEC must have "clear and adequate . . . authority to regulate" the conduct, (3) the SEC must be engaged in "active and ongoing . . . regulation," and (4) there must exist "a serious conflict between the antitrust and regulatory regimes."¹⁷⁹

The Court held that all four of these factors were satisfied in *Credit Suisse*.¹⁸⁰ First, the underwriters' efforts "jointly to promote and sell newly issued securities . . . were central to the proper functioning of

¹⁷² *Credit Suisse*, 127 S. Ct. at 2388.

¹⁷³ *Id.*

¹⁷⁴ *Id.* at 2389.

¹⁷⁵ *Id.*

¹⁷⁶ *Billing v. Credit Suisse First Boston*, 426 F.3d 130, 137 (2d Cir. 2005), *rev'd*, 127 S. Ct. 2383.

¹⁷⁷ *Credit Suisse*, 127 S. Ct. at 2389.

¹⁷⁸ *Id.* at 2390.

¹⁷⁹ *Id.*

¹⁸⁰ *Id.* at 2397.

well-regulated capital markets."¹⁸¹ Second, "the law grants the SEC authority to supervise" the underwriters' conduct.¹⁸² Third, "the SEC has continuously exercised its legal authority to regulate" the conduct in which the underwriters had engaged.¹⁸³ Fourth, the Court concluded that there was a "serious conflict between the antitrust and regulatory regimes."¹⁸⁴ The Court believed that, if antitrust suits against underwriters were permitted for IPO-related conduct, it would be difficult for fact-finders to separate conduct that the SEC permits from conduct that it forbids.¹⁸⁵ Under such circumstances, courts were likely to apply the antitrust laws too broadly, causing underwriters to avoid "a wide range of joint conduct that the securities law permits or encourages."¹⁸⁶

D. Applying Supreme Court Precedent to Collusion in Change-of-Control Transactions

The entire body of Supreme Court precedent supports the conclusion that the antitrust laws are not impliedly revoked by the securities laws with respect to collusion in public change-of-control transactions.¹⁸⁷ Indeed, it is impossible to reconcile the Second Circuit's decision in *Finnegan*, which found the antitrust laws inapplicable in such situations, with the Supreme Court's decisions in *Silver*, *Gordon*, *NASD*, and *Credit Suisse*.¹⁸⁸ In those cases, the Court emphasized that implied revocation of the antitrust laws was never favored and that it should only occur when there was a clear conflict between the antitrust laws and the specific provisions of another regulatory statute.¹⁸⁹ The Court only found implied revocation in *Gordon*, *NASD*, and *Credit Suisse* because the SEC had been granted specific authority to regulate the conduct at issue and had affirmatively exercised that authority to approve conduct that would have been prohibited by the antitrust laws.¹⁹⁰ In *Credit Suisse*, the SEC had allowed underwriters to engage in

¹⁸¹ *Id.* at 2392.

¹⁸² *Credit Suisse*, 127 S. Ct. at 2392.

¹⁸³ *Id.*

¹⁸⁴ *Id.* at 2393-97.

¹⁸⁵ *Id.*

¹⁸⁶ *Id.* at 2396.

¹⁸⁷ See *Credit Suisse*, 127 S. Ct. at 2390; *Nat'l Ass'n of Sec. Dealers*, 422 U.S. at 719-20; *Gordon*, 422 U.S. at 682; *Silver*, 373 U.S. at 357.

¹⁸⁸ See *Credit Suisse*, 127 S. Ct. at 2390; *Nat'l Ass'n of Sec. Dealers*, 422 U.S. at 719-20; *Gordon*, 422 U.S. at 682; *Silver*, 373 U.S. at 357; *Finnegan*, 915 F.2d at 831.

¹⁸⁹ See *Credit Suisse*, 127 S. Ct. at 2390; *Nat'l Ass'n of Sec. Dealers*, 422 U.S. at 719-20; *Gordon*, 422 U.S. at 682; *Silver*, 373 U.S. at 357.

¹⁹⁰ See *Nat'l Ass'n of Sec. Dealers*, 422 U.S. at 721; *Gordon*, 422 U.S. at 667-75.

the challenged pricing activities in the IPO aftermarket;¹⁹¹ in *Gordon*, the SEC had authorized the use of fixed commission rates on the stock exchanges;¹⁹² and in *NASD*, the SEC had decided to allow the mutual fund companies and broker-dealers to restrict the trading of mutual fund shares in the secondary market.¹⁹³ In such cases, there was a clear potential for the antitrust laws to conflict with the enforcement activities of a federal agency.¹⁹⁴

Contrary to the Second Circuit's reasoning in *Finnegan*, there is no such potential for conflict in change-of-control transactions. The Williams Act, which regulates the trading of securities in change-of-control transactions, requires disclosure of joint-bidding arrangements and gives the SEC the authority to regulate fraudulent or manipulative practices.¹⁹⁵ The Williams Act, however, does not include any provisions designed to protect competition,¹⁹⁶ and the SEC has not issued any rules regulating competition in change-of-control transactions.¹⁹⁷ As the *Finnegan* court conceded, the SEC has "chosen not to prohibit agreements between rival bidders as fraudulent or manipulative practices."¹⁹⁸ Because the SEC has declined to prescribe any remedy other than disclosure for joint-bidding arrangements, the role it plays in the tender-offer process does not conflict with the antitrust laws.¹⁹⁹ As William T. Reid IV has pointed out,

The mere contemplation of bidding arrangements [under the Williams Act] does not justify the preclusion of the antitrust laws. . . . Since the SEC's authority extends solely to issues related to disclosure, and it is not empowered to protect competition affirmatively, the Sherman Act can function without impeding the SEC's authority.²⁰⁰

None of the four factors set forth in *Credit Suisse* as preconditions to implied antitrust revocation applies to collusion in change-of-

¹⁹¹ See *Credit Suisse*, 127 S. Ct. at 2392.

¹⁹² See *Gordon*, 422 U.S. at 667-75.

¹⁹³ See *Nat'l Ass'n of Sec. Dealers*, 422 U.S. at 704, 721.

¹⁹⁴ See *Credit Suisse*, 127 S. Ct. at 2392-97; *Nat'l Ass'n of Sec. Dealers*, 422 U.S. at 719-20; *Gordon*, 422 U.S. at 682.

¹⁹⁵ See 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (2006).

¹⁹⁶ See William T. Reid IV, *Implied Repeal of the Sherman Act via the Williams Act: Finnegan v. Campeau Corp.*, 65 ST. JOHN'S L. REV. 965, 974 (1991).

¹⁹⁷ See 17 C.F.R. §§ 200-301 (2008).

¹⁹⁸ 915 F.2d at 831.

¹⁹⁹ See Reid, *supra* note 196, at 974.

²⁰⁰ *Id.* at 971, 974.

control transactions.²⁰¹ First, the competitive behavior of potential purchasers of public companies is not even remotely "an area of conduct squarely within the heartland of securities regulation."²⁰² Rather, collusion lies at the heart of the Sherman Act's prohibition of conspiracies in restraint of trade.²⁰³ Second, the SEC does not have "clear and adequate . . . authority to regulate" collusion in change-of-control transactions.²⁰⁴ Indeed, the SEC has no authority at all to regulate competitive conduct; its authority extends only to regulating disclosure of joint-bidding agreements and any fraudulent, deceptive or manipulative conduct in connection with tender offers.²⁰⁵ Third, the SEC is not engaged in "active and ongoing . . . regulation" of collusion.²⁰⁶ In fact, as the *Finnegan* court pointed out, the SEC has affirmatively declined to prohibit agreements between rival bidders in change-of-control transactions.²⁰⁷

The fourth factor—a serious conflict between antitrust and other regulatory regimes—gave the Court the greatest concern in *Credit Suisse*.²⁰⁸ The Court believed that, with respect to underwriters' conduct in IPOs, "only a fine, complex, detailed line separates activity that the SEC permits or encourages . . . from activity that the SEC must . . . forbid."²⁰⁹ Thus, "by permitting plaintiffs to dress what is essentially a securities complaint in antitrust clothing,"²¹⁰ the courts could deter "a wide range of joint conduct that the securities law permits or encourages."²¹¹

These concerns are not applicable to collusion among potential purchasers in change-of-control transactions. The lines between collusive conduct and failures to disclose joint-bidding arrangements in change-of-control transactions are much easier to draw. Unlike the IPO-related conduct in *Credit Suisse*, fact-finders cannot confuse collusion in the bidding process for a public company with a failure to properly disclose a joint-bidding arrangement under the Williams Act. The antitrust laws deal with an entirely different aspect of joint bidding than is

²⁰¹ See *Credit Suisse*, 127 S. Ct. at 2390.

²⁰² See *id.* at 2397.

²⁰³ See Piraino, *supra* note 32, at 1165–66.

²⁰⁴ *Id.*

²⁰⁵ See 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f).

²⁰⁶ *Credit Suisse*, 127 S. Ct. at 2397.

²⁰⁷ *Finnegan*, 915 F.2d at 831.

²⁰⁸ *Credit Suisse*, 127 S. Ct. at 2393–97.

²⁰⁹ *Id.* at 2394.

²¹⁰ *Id.* at 2396.

²¹¹ *Id.*

regulated by the securities laws.²¹² The antitrust laws preclude collusion in changes of control, whereas the federal securities laws regulate disclosure of joint bidding.²¹³ Thus, antitrust enforcement against collusion carries no risk of deterring conduct that the Williams Act permits or encourages.²¹⁴ Indeed, the SEC's requirement that joint-bidding arrangements be disclosed includes no express or implied approval of anticompetitive behavior occurring in connection with such arrangements.²¹⁵

If the antitrust laws did not apply in change-of-control transactions, public shareholders would have no remedy for the diminution in the value of their shares resulting from collusion to limit competition for the purchase of public companies.²¹⁶ Furthermore, if federal courts allowed disclosure statutes such as the securities laws to revoke the antitrust laws, there would be no limit to conduct that was immunized from antitrust review. Certain joint ventures, for example, must be disclosed to the government for review under the Hart-Scott-Rodino Act.²¹⁷ A defendant accused of conspiring with its joint venture partner to fix prices should not be able to argue that the antitrust laws do not apply to such conduct simply because the joint venture was disclosed under the Hart-Scott-Rodino Act.

²¹² See 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f); *United States v. Topco Assocs.*, 405 U.S. 596, 608 (1972) (applying per se rule to territorial restraints implemented by group of grocery stores); *United States v. Sealy, Inc.*, 388 U.S. 350, 355 (1967).

²¹³ See 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f); *Topco*, 405 U.S. at 608 (applying per se rule to territorial restraints implemented by group of grocery stores); *Sealy*, 388 U.S. at 355.

²¹⁴ See 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f); *Topco*, 405 U.S. at 608 (applying per se rule to territorial restraints implemented by group of grocery stores); *Sealy*, 388 U.S. at 355.

²¹⁵ See 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f).

²¹⁶ See *supra* notes 124–132 and accompanying text. Even if *Finnegan* were good law, it should not be construed to impliedly revoke the antitrust laws in cases involving express agreements to limit bidding in auctions for public companies. A naked agreement among potential purchasers to refrain from bidding would not constitute a joint-bidding arrangement within the meaning of the Williams Act. The Williams Act only requires disclosure of bidding arrangements when purchasers join forces to submit a common bid for the purchase of a company. See *supra* note 134 and accompanying text. There is no disclosure requirement when potential purchasers simply agree to refrain from participating in the auction process. See *supra* note 134 and accompanying text. Thus, a defendant could not point to any possible conflict between the antitrust laws and the federal securities laws under such circumstances.

²¹⁷ See Hart-Scott-Rodino Antitrust Improvements Act, 15 U.S.C. § 18(a) (2006).

IV. A PROPOSED ANTITRUST APPROACH TO COLLUSION IN CORPORATE CHANGES OF CONTROL

A. Recognizing the Price-Depressing Effects of Bid Rigging

The federal courts should adopt a new approach to corporate change-of-control transactions recognizing that the federal antitrust laws are the only viable means of protecting shareholders against the price depressing effects of bid rigging. State corporate laws focus on corporate governance processes and are not designed to ensure a competitive market for corporate control.²¹⁸ Under state corporate law, management can insulate itself from liability for collusion in change-of-control transactions simply by following certain procedural due process guidelines.²¹⁹ Federal securities laws protect investors in change-of-control transactions by requiring disclosure of joint-bidding arrangements; however, they do not deal with the substantive competitive conduct of potential purchasers in change-of-control transactions.²²⁰ After *Credit Suisse*, however, there should be no question that the antitrust laws can provide a remedy for the economic loss suffered by shareholders as a result of collusion in change-of-control transactions.²²¹ Thus, it is now appropriate for the federal courts to develop a more effective approach to such conduct.

The new approach to change-of-control transactions should recognize what economists have emphasized for years: collusion in change-of-control transactions harms shareholders by artificially reducing the price they receive in such transactions.²²² Economic studies have demonstrated that collusion among bidders in an auction process for any commodity has the effect of reducing the price received by a seller.²²³ These studies indicate that "even a mild degree of collusion" can result in larger sale price differences—"on the order of 20%"—for sellers.²²⁴ In any auction, competing bidders drive up the price for the relevant commodity. The situation is no different in auctions for the

²¹⁸ See Edward B. Rock, *Antitrust and the Market for Corporate Control*, 77 CAL. L. REV. 1365, 1386 (1989).

²¹⁹ See *In re Lear Corp. S'holder Litig.*, 926 A.2d 94, 97–98 (Del. 2007).

²²⁰ See Williams Act, 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f) (2006).

²²¹ See *Credit Suisse Sec. (USA) LLC v. Billing*, 127 S. Ct. 2383, 2390 (2007).

²²² See Hulbert, *supra* note 111.

²²³ See, e.g., Susan Athey & Philip A. Haile, *Empirical Models of Auctions*, Lecture for the Ninth World Congress of the Economic Society 36 (Mar. 13, 2006) (on file with author) ("[C]ollusion can easily depress ascending auction prices below the observed levels.").

²²⁴ *Id.*

purchase of control of a company. If there are fewer bidders, the price for a company, like that of any other commodity, will fall. One study has found that "target shareholders receive a premium of 42–46% in multiple-bidder tender offers, compared to a premium of 26–30% in single-bidder offers."²²⁵ Joshua Fried has emphasized the adverse effects of collusion among potential purchasers in change-of-control transactions: "Collusive bidding . . . tends to reduce the price paid to shareholders . . . because it eliminates the competition."²²⁶ Edward Rock has pointed out that "an agreement among bidders competing for control [of a company], like a bidding agreement in any other market, transfers wealth from target shareholders to acquirers. The seller loses a benefit of competition, namely, the chance to play one buyer off against others, in an attempt to increase the bid."²²⁷

Potential purchasers can collude in three different ways to reduce the price paid in a change-of-control transaction: (1) by expressly agreeing among themselves to avoid competition, (2) by reaching an implicit understanding on limiting competition, and (3) by participating in bidding consortiums that eliminate competition. The following Subsections explain how the proposed approach would deter each of these forms of anticompetitive conduct.

B. *Deterring Express Collusion*

Naked agreements among competing sellers to fix the prices of their products have been considered per se illegal since the earliest days of the Sherman Act.²²⁸ Courts and commentators refer to such price fixing arrangements as "cartels."²²⁹ Although the federal courts have taken a less aggressive approach in many antitrust areas during the last three decades, they have never wavered in their condemna-

²²⁵ Rock, *supra* note 218, at 1372–73.

²²⁶ Joshua M. Fried et al., *Collusive Bidding in the Market for Corporate Control*, 79 NEB. L. REV. 48, 73 (2000).

²²⁷ Rock, *supra* note 218, at 1373.

²²⁸ See *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 293 (6th Cir. 1898) (refusing to consider possible justifications for horizontal price fixing).

²²⁹ See Diane P. Wood, Circuit Judge, U.S. Court of Appeals for the Seventh Circuit, Presentation Before the Antitrust Section of the A.B.A.: The Incredible Shrinking Per Se Rule: Is an End in Sight? (Mar. 2004) (on file with author) ("The area in which the per se rule continues to be invoked most often, and continues to have real bite, is that of the hard-core cartel. By the term 'hard-core cartel,' antitrust lawyers normally mean an agreement between horizontal competitors . . . to fix prices or to engage in equivalent behaviors.").

tion of price fixing by sellers.²³⁰ In 2004, Justice Scalia (rarely an advocate of aggressive antitrust enforcement) described cartels among sellers as "the supreme evil of antitrust,"²³¹ and the U.S. Court of Appeals for the Ninth Circuit has concluded that "no antitrust violation is more abominated than the agreement to fix prices."²³² Because the anticompetitive effects of seller cartel arrangements are so clear, the courts have not been willing to consider any procompetitive justifications offered by sellers engaged in price fixing.²³³

The courts and agencies should take a similarly harsh approach to express agreements among buyers to limit competition. The Supreme Court pointed out in its 2007 decision in *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, that the courts should treat anticompetitive conduct by purchasers no more leniently than anticompetitive conduct by sellers.²³⁴ Bid-rigging arrangements among buyers are just as harmful to competition as agreements among sellers to fix prices.²³⁵ The only effects of such conspiracies are to prevent competition among buyers on input prices and to reduce the price of inputs, to the detriment of sellers. As Edward Rock has pointed out, "Bidding agreements are simply one form of price fixing, the archetypal example of a *per se* violation of the Sherman Act. . . . Price fixing among buyers is every bit as illegal as price fixing among sellers."²³⁶

In other markets, bid-rigging arrangements have been precluded on their face as *per se* violations of the antitrust laws.²³⁷ Indeed, bid rigging is routinely prosecuted by the Department of Justice (the "DOJ")

²³⁰ See *NCAA v. Bd. of Regents*, 468 U.S. 85, 110 (1984) ("We have never required proof of market power in such a case."); *Arizona v. Maricopa Co. Med. Soc'y*, 457 U.S. 332, 347 (1982) ("We have not wavered in our enforcement of the *per se* rule against price fixing."); *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 218 (1940) (applying *per se* rule to price fixing).

²³¹ *Verizon Commc'ns., Inc. v. Trinko*, 540 U.S. 398, 408 (2004).

²³² *Dagher v. Saudi Ref., Inc.*, 369 F.3d 1108, 1116 (9th Cir. 2004), *rev'd sub nom*, *Texaco, Inc. v. Dagher*, 547 U.S. 1 (2006).

²³³ See *NCAA*, 468 U.S. at 110; *Maricopa*, 457 U.S. at 347; *Socony-Vacuum*, 310 U.S. at 218.

²³⁴ *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069, 1075 (2007) (citing John B. Kirkwood, *Buyer Power and Exclusionary Conduct: Should Brooke Group Set the Standards for Buyer-Induced Price Discrimination and Predatory Bidding?*, 72 ANTITRUST L.J. 625, 652 (2005); Thomas A. Piraino, Jr., *A Proposed Antitrust Approach to Buyers' Competitive Conduct*, 56 HASTINGS L.J. 1121, 1125 (2005)).

²³⁵ See Rock, *supra* note 218, at 1407.

²³⁶ *Id.*

²³⁷ See, e.g., *United States v. Seville Indus. Mach. Co.*, 696 F. Supp. 986, 989 (D.N.J. 1988).

as a criminal violation of the Sherman Act.²³⁸ There is no reason why bid rigging in change-of-control transactions should be treated more leniently. Shareholders of American companies should be entitled to the same protection from bid rigging as the sellers of other commodities. Such agreements are just as anticompetitive as any other bid-rigging arrangements, and they can cause substantial economic harm to the shareholders of companies that receive a lower price as a result of collusion among potential bidders. For example, in the 1988 battle for control of Federated, Campeau and Macy's agreed to stop bidding against each other after concluding that a "bidding frenzy" for the company had begun to build.²³⁹ This agreement allowed Campeau to purchase Federated from its shareholders for \$172 million less than Macy's most recent bid.²⁴⁰ The conspiracy among these two potential purchasers fixed the price for Federated at a *lower* level just as surely as price-fixing agreements among sellers fix prices at *higher* levels.²⁴¹

Express bid rigging in change-of-control transactions is most likely to occur among strategic buyers who have already begun to participate in a company auction process.²⁴² In the typical case, one bidder agrees to drop out of the auction process in exchange for cash or an agreement by the successful bidder to sell a portion of the company to the withdrawing bidder after the transaction is completed.²⁴³ In the Federated transaction, for example, Macy's agreed with Campeau to withdraw from the bidding process, and Campeau agreed, in return, to pay Macy's \$60 million and to sell two divisions of Federated to Macy's.²⁴⁴ There have been many other examples of express agreements among strategic buyers to terminate the bidding process in a company auction. In 2002, both Global Crossing and Qwest Communications bid to acquire two communications companies: Frontier and US West.²⁴⁵ "Rather than engage in a bidding war, the rival suitors agreed to split the prizes, with Global Crossing getting Frontier while Qwest acquired U.S. West."²⁴⁶ Similarly, Bethlehem Steel and Allegheny Teledyne each

²³⁸ See R. Preston McAfee et al., *Collusive Bidding in Hostile Takeovers*, 2 J. ECON. & MGMT. STRATEGY 449, 450 (1993).

²³⁹ Rock, *supra* note 218, at 1368.

²⁴⁰ *Finnegan v. Campeau Corp.*, 915 F.2d 824, 826 (2d Cir. 1990).

²⁴¹ See *id.*

²⁴² See *id.*

²⁴³ See *id.*

²⁴⁴ *Id.*

²⁴⁵ Fried, *supra* note 226, at 50.

²⁴⁶ *Id.*

attempted to acquire Lukens Steel.²⁴⁷ Allegheny Teledyne agreed to drop out of the bidding after Bethlehem agreed to sell certain assets of Lukens to Allegheny Teledyne.²⁴⁸ Finally, when Comcast and AT&T each bid to acquire MediaOne, Comcast agreed to withdraw its offer after AT&T agreed to sell its cable systems in Baltimore and Washington D.C. to Comcast.²⁴⁹

Express bid-rigging arrangements in change-of-control transactions have no purpose other than to limit competition and no effect other than to artificially decrease the price received by shareholders. Assume, for example, that KKR and the Blackstone Group each made separate bids to purchase General Motors and take the company private. Henry Kravis, concerned that a bidding war for Blackstone would raise the price for General Motors, calls Stephen Schwarzman and suggests that, if Blackstone drops out of the bidding for General Motors, KKR would decline to bid on the next large transaction in which Blackstone is interested. Mr. Schwarzman acquiesces to Mr. Kravis' suggestion, and KKR, as the sole bidder, is successful in purchasing General Motors. Such an agreement would eliminate all competition among the firms for the purchase of General Motors. Instead of receiving a full market price, the shareholders of General Motors would only receive the lower price that KKR was willing to pay. A court or agency should not have to inquire any further to conclude that such an arrangement constitutes an illegal conspiracy in restraint of trade under Section 1 of the Sherman Act.

C. *Detering Implicit Collusion*

"Game theory" has explained how firms in oligopolistic markets make their decisions "in reference to the likely reaction of competitors."²⁵⁰ It is easier tacitly to communicate, monitor, and observe a consensus form of conduct when only a few firms are involved. Oligopolists are more likely to know each other well, to understand each other's business strategies, and to be able to anticipate the reaction of their rivals to particular competitive conduct.

The private equity market possesses the classic characteristics of an oligopoly that facilitates implicit collusion. Approximately seven U.S.-

²⁴⁷ *Id.*

²⁴⁸ *Id.*

²⁴⁹ *Id.* at 50-51.

²⁵⁰ Robert A. Milne & Jack E. Pace III, *The Scope of Expert Testimony on the Subject of Conspiracy in a Sherman Act Case*, ANTI-TRUST, Spring 2003, at 36, 37 (emphasis omitted).

based private equity firms have the financial capacity to bid alone on transactions with a value of more than \$4 billion: KKR, Blackstone, the Goldman Sachs Group ("Goldman"), TPG (formerly the Texas Pacific Group), Bain Capital, the Carlyle Group ("Carlyle"), and Providence Equity Partners ("Providence").²⁵¹ In 2007, KKR and Blackstone were the largest private equity firms, "[h]aving just finished raising new supersize funds . . . each worth more than \$20 billion."²⁵² Goldman is close behind KKR and Blackstone, with a \$19 billion fund, followed by TPG, with \$15 billion in assets.²⁵³

The same seven private equity firms will usually be the only financial buyers capable of pursuing a going-private transaction with the largest American companies. These firms are able to observe each others' conduct over an extended period, as they compete to purchase a series of companies that are interested in going private. This familiarity makes it easier for the private equity firms to anticipate their rivals' interest in a particular transaction. These firms can subtly signal to each other the companies for which each firm is willing to bid aggressively. Over a period of time, the firms can establish a pattern under which they take turns in bidding for their preferred companies. The implicit understanding reached by the firms can reduce competition in change-of-control transactions just as effectively as an express bid-rigging arrangement.

Business executives as sophisticated as Messrs. Kravis and Schwartzman are not likely to propose overt conduct that constitutes a bald violation of the antitrust laws. They are much more likely to coordinate their conduct by implicitly signaling their intentions as to whether they plan to bid for a particular company. Consider a hypothetical going-private transaction for General Motors.²⁵⁴ If KKR and

²⁵¹ See MacFadyen, *supra* note 10; *PEI50: The List*, PRIVATE EQUITY INT'L, May 2007, at 2, available at http://www.peinedia.com/resources/Conference/downloads/PEI50_Brochure_final.pdf (listing the top-fifty private equity firms' capital raised over the 2002–2007 period). The determination that approximately seven private equity firms can bid on such transactions is an assumption. It uses the *PEI50* data and assumes that a firm (1) would use equity capital to finance at least 40% of the bid price and (2) would invest no more than 10% of its capital in any one transaction. Thus, only firms with at least \$16 billion in committed capital would be able to bid alone on transactions of \$4 billion and above.

²⁵² Andrew Ross Sorkin & Clifford Krauss, *At \$45 Billion, New Contender for Top Buyout*, N.Y. TIMES, Feb. 24, 2007, at A1.

²⁵³ Sender, Berman & Smith, *supra* note 25, at A1; Henny Sender, *Goldman Joins Private Equity's Upper Echelon*, WALL ST. J., Feb. 9, 2007, at C1.

²⁵⁴ A going-private transaction involving General Motors may be more than theoretical. In the summer of 2007, takeover speculation "made investors believe that GM could be next" in going private. Gregory Zuckerman, *After GM's Labor Pact, It's Time to Kick the*

Blackstone wanted to avoid competition that could increase the price for General Motors, they would be better served by an implicit rather than an express understanding as to which party would be allowed to bid for General Motors. The parties could reach such an implicit understanding by engaging in a pattern of conduct making clear their mutual intention to avoid head-to-head competition. Because only approximately seven private equity firms are currently capable of bidding for companies as large as General Motors, it would be easy for KKR to signal to Blackstone and to the other five private equity firms that, if they declined to bid for General Motors, KKR would refrain, in turn, from bidding on the next large transaction. A pattern of "you take this one, I will take the next one" could be established in several different ways. It may, for example, become evident over a period of time that KKR was only going to bid for automobile companies, while Blackstone was only going to bid for steel companies. Alternatively, the seven private equity firms could simply establish a pattern of conduct under which they alternated in their bidding for large companies.

Such tacit bid rigging will likely have an even greater adverse effect than explicit bid rigging because tacit arrangements are usually more durable than express noncompetition agreements. Explicit noncompetition agreements are usually not long lasting.²⁵⁵ Furthermore, if a cartel does not fall of its own accord, it usually must be sustained by overt conduct that is easy to detect and to punish.²⁵⁶ By contrast, oligopolists' tacit collusion is both more durable and more difficult to discover than an explicit arrangement. Thus, in change-of-control transactions, shareholders will be harmed more by implicit agreements among potential purchasers to refrain from competing against each other. Implicit agreements are likely to extend for a significant period because they are based on a long pattern of conduct and are not designed only for a particular change-of-control transaction.²⁵⁷ In the private equity market, a firm's decision not to participate in auctions for particular public companies will be the result not of explicit bargaining, but of each firm's own decision about the types of transactions in which it is

Tires—Investor Focus Will Turn to the Car Operations, Where Picture Is Blurry, WALL ST. J., Sept. 27, 2007, at C1.

²⁵⁵ See BORK, *supra* note 27, at 183 ("Changing market conditions and the temptation to 'cheat' frequently result in outbreaks of price competition that either destroy the cartel or must be repaired by further meetings and agreements.").

²⁵⁶ See *id.*

²⁵⁷ See Sorkin & Krauss, *supra* note 252; Sender, Berman & Smith, *supra* note 25; Sender, *supra* note 253; MacFadyen, *supra* note 10.

likely to be the preferred bidder. Because each firm will be deciding which transaction is best for it, the firms will be less likely to cheat on a tacit arrangement to take turns in bidding in successive company auctions.

Despite the potentially serious effects of tacit collusion in the market for the purchase of control of American companies, the anti-trust laws do not currently provide an effective remedy for shareholders harmed by such conduct.²⁵⁸ The federal courts have been reluctant to infer the existence of an illegal conspiracy in restraint of trade from the type of circumstantial evidence that is usually available in cases involving tacit conspiracies among oligopolists.²⁵⁹ The courts have emphasized that oligopolists should not be liable for engaging in "conscious parallelism": i.e., for independently determining their own competitive conduct with a full understanding that their rivals are likely to follow suit.²⁶⁰ When an oligopolist simply takes its rivals' likely actions into account, it is merely recognizing its interdependence with other firms, and not even the most expanded definitions of "agreement" have been deemed to encompass such conduct.²⁶¹

The lower federal courts have been overly protective of coordinated conduct among oligopolists, placing burdens on plaintiffs that preclude a finding of conspiracy in cases where the presence of tacit collusion should have been clear.²⁶² For its part, the Supreme Court has

²⁵⁸ See, e.g., *Williamson Oil Co. v. Philip Morris USA*, 346 F.3d 1287, 1299 (11th Cir. 2003); *infra* note 262.

²⁵⁹ John Lopatka has posed the oligopoly dilemma as follows: "[S]ection 1 could not be used to punish [oligopolists] simply for pricing interdependently, but . . . they usually will have done more and could then be attacked under section 1. The devil is in deciding whether they did enough more." John E. Lopatka, *Solving the Oligopoly Problem: Turner's Try*, 41 ANTITRUST BULL. 843, 907 (1996).

²⁶⁰ See, e.g., *Williamson Oil*, 346 F.3d at 1299 ("When they are the product of a rational, independent calculus by each member of the oligopoly, as opposed to collusion, these types of synchronous actions have become known as 'conscious parallelism.'" (emphasis omitted)). "There are no cases in which mere parallel behavior was found by the courts to constitute collusion." ROGER D. BLAIR & DAVID L. KASERMAN, ANTITRUST ECONOMICS 208 (1985).

²⁶¹ Judge (now-Justice) Breyer has explained that interdependent pricing by oligopolists, without more, does not violate § 1: "Courts . . . have almost uniformly held . . . that . . . individual pricing decisions (even when each firm rests its own decision upon its belief that competitors will do the same) do not constitute an unlawful agreement under Section 1 of the Sherman Act." *Clamp-All Corp. v. Cast Iron Soil Pipe Inst.*, 851 F.2d 478, 484 (1st Cir. 1988) (emphasis omitted).

²⁶² See *In re Ethyl Corp.*, 101 F.T.C. 425, 481-84 (1983), *vacated sub nom. E.I. DuPont de Nemours & Co. v. FTC*, 729 F.2d 128, 142 (2d Cir. 1984) (reversing FTC decision that found requisite factors in practices that facilitated coordination among manufacturers of antiknock compounds); *United States v. Chas. Pfizer & Co.*, 367 F. Supp. 91, 101 (S.D.N.Y.

held that a plaintiff in an implicit conspiracy case will not be able to get to a jury unless it can introduce direct and uncontradicted evidence of an agreement among the defendants.²⁶³ Such evidence, of course, is rarely, if ever, available in cases of implicit oligopoly conduct. These cases have placed oligopoly regulation on its head, making it easier for plaintiffs to prove the existence of express cartels, which are least harmful to consumers, and erecting the highest hurdles for proving implicit cartels, the most harmful types of arrangements.²⁶⁴ As Judge Posner has explained, the Supreme Court's cases have "produce[d] the paradox that the more conducive the market's structure is to collusion without express communication, the weaker the plaintiff's case."²⁶⁵

The courts and agencies should adopt a new approach that more effectively deters tacit arrangements that are harmful to shareholders in change-of-control transactions. The approach should be similar to the standard I have proposed for analyzing implicit price fixing arrangements among sellers. I have argued that, when an oligopolist engages in conduct that is contrary to its legitimate self interest, it sends a signal to its rivals that it is safe for them to engage in the same conduct. The courts should infer an illegal arrangement of tacit price collusion whenever all of the firms in an oligopolistic market engage in identical practices contrary to their independent self interest. Oligopolists gain confidence in their rivals' commitment to a consensus course of action when their rivals engage in actions that are against their immediate self interest and make no economic sense other than as an invitation to join in a collusive arrangement. Indeed, actions by rivals against their own self interest can communicate their consent to an implicit course of action just as clearly as a cartel's express commitment to a price fixing arrangement. When a firm risks an immediate loss of volume, profits,

1973) (finding nothing more than conscious parallelism when pharmaceutical companies excluded competitors from antibiotics market by maintaining similar prices and using patent licenses as barrier to entry).

²⁶³ *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 768 (1984) (holding that, in order to avoid summary judgment, plaintiffs must present "evidence that tends to exclude the possibility" that the defendants were acting independently in pursuing the relevant conduct).

²⁶⁴ See *Bell Atlantic v. Twombly*, 127 S. Ct. 1955, 1974 (2007) (finding insufficient proof of conspiracy when regional telephone companies made parallel decisions not to allow competitors to access their systems and not to compete in each other's territories); *Matsushita Elec. Indus. Corp. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1985); *Monsanto*, 465 U.S. at 768.

²⁶⁵ David L. Meyer, *The Seventh Circuit's High Fructose Corn Syrup Decision—Sweet for Plaintiffs, Sticky for Defendants*, ANTITRUST, Fall 2002, at 67, 71 (quoting RICHARD A. POSNER, ANTITRUST LAW 94-95 (2d ed. 2001)).

or customer goodwill in announcing a particular course of action, it sends a strong signal to its rivals that it is safe for them to engage in the same conduct. Such rivals will then be more likely to take the risk of acting against their own interests and falling in line with the consensus course of conduct.²⁶⁶ Under such circumstances, it is reasonable for the courts to infer that, through their signaling of such a consensus, the parties have entered into a tacit price fixing conspiracy in violation of Section 1 of the Sherman Act.²⁶⁷

The courts and agencies should be willing to infer an illegal arrangement of tacit collusion whenever bidders for companies engage in identical conduct contrary to their independent self-interest. Consider the hypothetical example above in which KKR and Blackstone implicitly signal their intention to allow KKR to be the winning bidder for General Motors. Allowing KKR to purchase General Motors without any competition would be contrary to Blackstone's legitimate independent interest. Declining to bid on a company that meets its investment criteria would conflict with Blackstone's interest in maximizing its return on capital. Max King, a strategist at Investec Asset Management, has stated that "private equity investors have to go and find the deals rather than just wait for the deals to come to them."²⁶⁸ Private equity firms such as Blackstone have an enormous amount of capital that they must put to work quickly and profitably in order to convince potential investors that they will continue to be successful in acquiring and selling companies at a profit. Paul Bracken, a professor of management at Yale University, has explained, "If you establish one of these funds, you can't sit on the money for too long because it sends a signal that you're not good at spotting opportunities."²⁶⁹ Because there are "few companies with noncore businesses to divest and few distressed sellers,"²⁷⁰ it would be unnatural for Blackstone to avoid bidding for a favorable acquisition candidate. If a private equity firm such as Blackstone was act-

²⁶⁶ Some lower federal courts have been willing to infer illegal oligopoly pricing conspiracies from circumstantial evidence that defendants acted in a manner contrary to their independent self interest. For example, in *Milgram v. Loew's, Inc.*, 192 F.2d 579, 583 (3d Cir. 1951), eight film distributors refused to license first-run films to a drive-in theater. The refusal appeared suspicious because the theater had offered to pay a premium for such films. The court concluded, "Each distributor has thus acted in apparent contradiction to its own self-interest. This strengthens considerably the inference of conspiracy, for the conduct of the distributors is . . . inconsistent with decisions independently arrived at." *Id.*

²⁶⁷ See Piraino, *supra* note 11, at 9, 37-39.

²⁶⁸ *Id.*

²⁶⁹ *Id.*

²⁷⁰ Conrad de Aenlle, *Some Experts at Timing Go For Cash*, N.Y. TIMES, July 7, 2007, at C6 (quoting Max King, strategist at Investec Asset Management).

ing in its legitimate independent interest, it would not take a pass on a potentially profitable investment such as General Motors.

It would thus be reasonable for a court to conclude that a private equity firm such as Blackstone would only be willing to forego a potentially profitable investment in General Motors because it was expecting some implicit assurance from its rivals that, in return, they would refrain from bidding on certain future transactions in which Blackstone was interested. In declining to bid for a company that it had the capability to purchase, Blackstone would be sending a signal to its rivals in the private equity market that it was willing to acquiesce in a "you take this one, I will take the next one" pattern of conduct. Blackstone's implicit calculation would be that, in future transactions, it could recover the profits that it lost in the General Motors deal by acquiring another company at a below-market price when other private equity firms declined to bid for that company.

D. *Deterring Anticompetitive Consortiums*

In many going-private transactions, private equity funds have formed consortiums in which they combine their resources to submit a single bid for a company.²⁷¹ Such consortiums can reduce competition in change-of-control transactions just as severely as express or implicit bid-rigging arrangements. Some commentators have opined that the formation of these consortiums "has the potential to artificially depress buyout prices and hurt corporate shareholders."²⁷² As the *Wall Street Journal* has explained, "While the ostensible goal of forming buyout clubs has been to spread the risk of larger investments among the members of the club, some takeover professionals have voiced concern that clubs may also limit the number of competing bidders and the value of potential bids."²⁷³

In recent years, joint ventures among competitors have become increasingly popular for firms in a great number of American industries.²⁷⁴ Unfortunately, however, the federal courts have not been able

²⁷¹ See Sorkin, *supra* note 12.

²⁷² *Id.* (stating that "[w]hile no buyout executives will say on the record that the purpose of forming a team is to keep the asking price from going too high, privately, most will concede that reducing the final takeover price is sometimes the result").

²⁷³ Randall Smith & Kathryn Kranhold, *GE Sets Private-Equity Limits*, WALL ST. J., Jan. 9, 2007, at A3.

²⁷⁴ See Charles P. Weller, A "New" Rule of Reason from Justice Brandeis' "Concentric Circles" and Other Changes in Law, 44 ANTITRUST BULL. 881, 882 (1999) (stating that such competitor collaborations "are becoming the dominant form of economic integration in the world

to develop a consistent means of analyzing joint ventures. The courts' difficulty stems from the fact that competitors' collaborative arrangements can be structured in a wide variety of ways. Indeed, the term "joint venture" itself has been used rather loosely to describe collaborations ranging from mere agreements among firms to coordinate their activities—such as information exchanges or joint advertising—to complete mergers of the parties' operations in the relevant market.²⁷⁵ As Robert Pitofsky, a former Chairman of the Federal Trade Commission, has stated, "A joint venture could involve any business enterprise in which two or more persons collaborate to achieve some commercial goal—a definition that includes all of antitrust, except, perhaps, some single firm attempts to monopolize. . . ."²⁷⁶ Charles Weller has concluded that "[f]or over 100 years, antitrust joint venture law has been a morass of confusion and ambiguity."²⁷⁷ Ernest Gellhorn and W. Todd Miller have pointed out that "the legal rules and policies applied to competitor collaborations are often confused and confusing. . . . Where competitor combinations result in mergers, they are assessed under well-established rule of reason standards. . . . Where combinations result in joint ventures, however, . . . the legal framework [for analyzing joint ventures] is neither consistent nor rational."²⁷⁸

The courts have applied widely divergent antitrust standards to collaborative arrangements.²⁷⁹ In certain cases, courts have concluded that such arrangements are nothing more than vehicles to facilitate price fixing cartels among competitors, and they have found them to be per se illegal.²⁸⁰ In other cases, however, courts have found that collaborative arrangements have legitimate efficiency objectives, and they have applied a more lenient "rule of reason" standard, under which a

economy" (quoting PETER F. DRUCKER, *MANAGING IN A TIME OF GREAT CHANGE* 152 (1995)).

²⁷⁵ See Robert Pitofsky, *A Framework for Antitrust Analysis of Joint Ventures*, 74 GEO. L.J. 1605, 1605 (1986).

²⁷⁶ *Id.*

²⁷⁷ Weller, *supra* note 274, at 881.

²⁷⁸ Ernest Gellhorn & W. Todd Miller, *Competitor Collaboration Guidelines—A Recommendation*, 42 ANTITRUST BULL. 851, 853 (1997).

²⁷⁹ Compare *United States v. Topco Assocs.*, 405 U.S. 596, 608 (1972) (applying per se rule to territorial restraints implemented by group of grocery stores), and *United States v. Sealy, Inc.*, 388 U.S. 350, 355 (1967) (applying per se rule to territorial restraints among manufacturers of bedding), with *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 459 (1986) (applying rule of reason to refusal by an association of dentists to supply x-rays of their members' patients to insurance companies), and *Nw. Wholesale Stationers, Inc. v. Pac. Stationery & Printing Co.*, 472 U.S. 284, 295–96 (1985) (applying rule of reason to decision by purchasing cooperative to expel one of its members).

²⁸⁰ See, e.g., *Topco Assocs.*, 405 U.S. at 608; *Sealy*, 388 U.S. at 355.

plaintiff cannot prevail until it has demonstrated that the anticompetitive effects of the venture will likely outweigh its efficiencies in the relevant market.²⁸¹ In most cases, plaintiffs have not been able to meet that burden of proof, and fact-finders have allowed the arrangements to proceed.²⁸²

The lack of clear authority on the applicable legal standards for collaborative arrangements will make it difficult for shareholders to prove whether potential purchasers have violated the Sherman Act by forming consortiums in change-of-control transactions. If the courts concentrate on the consortiums' potential to limit competition in company auctions, they may find them illegal as naked cartels;²⁸³ if the courts conclude that consortiums have a legitimate efficiency objective, they may uphold them as joint ventures.²⁸⁴ When a court finds that a consortium constitutes a legitimate joint venture, it will be difficult, if not impossible, for a shareholder to prove under the rule of reason that the arrangement unreasonably restrained competition in the relevant market. In a rule of reason case, it will be insufficient for a shareholder to demonstrate that it suffered individual economic harm as a result of decreased competition for the purchase of a particular company.²⁸⁵ In addition, the shareholder will have to prove that competition in the market as a whole was adversely affected by the defendants' conduct.²⁸⁶ If a court defines the relevant market as the nationwide market for the sale of public securities, the shareholder of a single public company will be unable to meet that standard.²⁸⁷

In a series of articles, I have proposed an effective way for the courts to distinguish between illegal cartels and permissible joint ventures.²⁸⁸ The distinction should depend upon whether the collabora-

²⁸¹ See, e.g., *Ind. Fed'n of Dentists*, 476 U.S. at 459; *Nw. Wholesale Stationers*, 472 U.S. at 295-96.

²⁸² See Piraino, *supra* note 32, at 1146-51.

²⁸³ See *Topco Assocs.*, 405 U.S. at 608; *Sealy*, 388 U.S. at 355.

²⁸⁴ See, e.g., *Ind. Fed'n of Dentists*, 476 U.S. at 459; *Nw. Wholesale Stationers*, 472 U.S. at 295-96.

²⁸⁵ See Piraino, *supra* note 32, at 1146-51.

²⁸⁶ See *id.* at 1148-49.

²⁸⁷ In his concurring opinion in *Credit Suisse*, Justice Stevens stated that the underwriting syndicates should not be liable under the Sherman Act because they lacked the power to restrain trade "among the vast multitude of other securities traded in a free market." 127 S. Ct. at 2398 (Stevens, J., concurring in the judgment).

²⁸⁸ See generally Piraino, *supra* note 32; Thomas A. Piraino, Jr., *A Proposed Antitrust Analysis of Telecommunications Joint Ventures*, 1997 WIS. L. REV. 639; Thomas A. Piraino, Jr., *The Antitrust Analysis of Network Joint Ventures*, 47 HASTINGS L.J. 5 (1995); Thomas A. Piraino, Jr., *Reconciling Competition and Cooperation: A New Antitrust Standard for Joint Ventures*, 35 WM. & MARY L. REV. 871 (1994) [hereinafter Piraino, *Reconciling*]; Thomas A. Piraino, Jr., *Beyond*

tive arrangement at issue involves any integration of the parties' resources. In a cartel, competitors agree to coordinate their competitive activities without integrating their resources in any manner.²⁸⁹ Because the parties have not pooled their resources or contributed any assets to the arrangement, a cartel has neither the objective nor the possibility of generating any procompetitive efficiencies.²⁹⁰ For example, the only effect of a naked agreement among competitors to fix prices, unaccompanied by any combination of the parties' marketing organizations, will be to raise prices, to the detriment of consumers.²⁹¹ Such an arrangement should be deemed illegal on its face.

Joint ventures, on the other hand, involve some integration of the parties' resources.²⁹² By virtue of such integration, the joint venture partners can enhance their efficiency in the relevant market.²⁹³ By contributing complementary resources to the venture, the partners give the venture the ability to achieve efficiencies beyond their individual capacities.²⁹⁴ In many cases, the legality of a legitimate joint venture should be obvious. Joint ventures should be per se legal when they permit their partners to combine their resources to enter a market from which they would have been individually foreclosed. Since the parties could not have participated in the relevant market in the absence of the joint venture, such arrangements have no adverse competitive effects.²⁹⁵ The only effect of such ventures is to enhance competition by introducing new competitors to the relevant market, thereby benefiting consumers.²⁹⁶

Similarly, the distinction between illegal and legitimate consortiums in change-of-control transactions should depend upon whether

Per Se, Rule of Reason or Merger Analysis: A New Antitrust Standard for Joint Ventures, 76 MINN. L. REV. 1 (1991).

²⁸⁹ See Gregory J. Werden, *Antitrust Analysis of Joint Ventures: An Overview*, 66 ANTITRUST L.J. 701, 712 (1998) ("If two competitors formed a venture that did nothing but set their prices, the arrangement would be nothing more than a price fixing cartel, and it would be treated as such under the antitrust laws.")

²⁹⁰ *Id.*

²⁹¹ See Piraino, *supra* note 32, at 1166 ("Naked . . . agreements not to compete, unaccompanied by any efficiency-enhancing integration, have no compensating efficiency benefits and can be summarily prohibited without any consideration of the parties' justifications or market power.")

²⁹² See Piraino, *Reconciling*, *supra* note 288, at 876.

²⁹³ See *id.*

²⁹⁴ See *id.*

²⁹⁵ See *id.* at 883-84.

²⁹⁶ See *id.* In his concurring opinion in *Credit Suisse*, Justice Stevens stated that agreements among underwriters on the terms for marketing IPOs should be deemed per se legal joint ventures. 127 S. Ct. at 2398 (Stevens, J., concurring in the judgment).

the relevant arrangement permits its partners to bid for a company which they otherwise could not have purchased. The courts and agencies should permit a bidding arrangement whenever it allows smaller bidders to pool their financial resources and bid for a company that they could not have afforded to purchase on their own. In such a case, the consortium will integrate the parties' financial resources to achieve a legitimate efficiency objective. The only effect of such a consortium is beneficial: to allow its participants to enter an auction process from which they otherwise would have been foreclosed.

The courts and agencies should not, however, allow joint-bidding arrangements among firms that have the ability to bid for a company on their own. Such arrangements have no legitimate efficiency objective. They do not add any new bidder to the auction process. Their only effect is to eliminate competition among the potential purchasers of a company. In the absence of the bidding arrangement, each of the participants could have entered the auction on its own, driving the price of the company higher as they competed to submit the highest bid. Bidding consortiums among firms that have the capability to bid for the relevant company on their own do not involve any efficiency-enhancing integration of the parties' financial resources and should be treated in the same manner as any other naked cartel.

E. Advantages of the Proposed Approach

The approach proposed in this Article would improve the bidding process in change-of-control transactions in several ways. First, because express agreements to limit bidding would be illegal on their face, strategic buyers would no longer attempt to negotiate arrangements (such as the agreement between Macy's and Campeau in the Federated transaction) to terminate aggressive bidding contests prematurely. Secondly, the proposed approach would no longer treat implicit bid-rigging arrangements more leniently than express agreements. As a result, competing bidders would be deterred from signaling to each other their intention to avoid bidding under certain circumstances. Without the ability to send such signals, private equity firms could no longer establish an implicit pattern of conduct limiting bidding for certain companies to only one or a very few firms. Finally, the proposed approach would enhance competition by clarifying the legality of consortiums in change-of-control transactions. The approach strikes an appropriate balance between encouraging consortiums that enhance competition in the bidding process and deterring consortiums that limit such competition. Consortiums that allow bidders to participate in

transactions from which they otherwise would have been foreclosed will be legal on their face; consortiums that do nothing more than eliminate competition among viable bidders will be illegal.

The proposed approach should mitigate most of the problems caused by management's conflict of interest in going-private transactions. Since more firms would be likely to bid aggressively in particular transactions, management would be less able to control the bidding process and steer a transaction to the private equity firm that it favors. All interested firms would have an equal opportunity and incentive to bid for a company, and shareholders would be more likely to receive a full and fair price rather than the artificially low premiums that have been offered in recent transactions by bidders preselected by management.²⁹⁷

The final three Sections of this Article explain how the proposed approach is likely to prevent express collusion, tacit collusion, and anticompetitive consortiums in change-of-control transactions.

V. PREVENTING EXPRESS COLLUSION IN CHANGE-OF-CONTROL TRANSACTIONS

Express agreements among bidders to limit competition for the purchase of a company should be illegal on their face. Fact-finders should dispense with a market power inquiry in such cases because the market power analysis has been the most complex of all the factors considered under the rule of reason.²⁹⁸ Avoiding a market power analysis will make liability more certain, thus deterring potential purchasers from expressly colluding to limit competition in change-of-control transactions. There is ample precedent for dispensing with a market power inquiry into conduct with such obvious anticompetitive effects as bid rigging; the federal courts have consistently applied the per se rule to bid-rigging arrangements, finding them illegal on their face without any consideration of defendants' justifications or market power.²⁹⁹ There is no reason for the courts to apply a more lenient

²⁹⁷ See *supra* notes 99–123 and accompanying text.

²⁹⁸ See Thomas A. Piraino, Jr., *Making Sense of the Rule of Reason: A New Standard for Section 1 of the Sherman Act*, 47 VAND. L. REV. 1753, 1763 (1994) ("Proof of market power is 'difficult, complex, expensive and time-consuming,' involving a fact-intensive assessment of the relevant product and geographic market, each of the parties' shares of those markets, and their competitors' market shares." (quoting Phillip Areeda, *The Changing Contours of the Per Se Rule*, 54 ANTITRUST L.J. 27, 28 (1985))).

²⁹⁹ See *Mandeville Island Farms, Inc. v. Am. Crystal Sugar Co.*, 334 U.S. 219, 242–43 (1948) (applying per se rule to agreement among sugar refiners to pay uniform price to

approach to express agreements among potential purchasers to limit competition in change-of-control transactions. As Edward Rock has concluded, "[S]uch agreements between actual bidders should be per se illegal because their anticompetitive effects are clear, while their pro-competitive effects are speculative or nonexistent."³⁰⁰

Shareholders suffer substantial economic loss when active bidders for public companies expressly agree to short-circuit a bidding process. Compare the experience of the shareholders of Federated, who were deprived of the benefits of a full auction by a no-bid agreement, with that of the shareholders of RJR Nabisco, who received full value for their shares in a competitive bidding process.³⁰¹ In the sale of Federated, the bidders agreed to stop competing "when the high bid was \$75.51 per share, and then lowered the bid to \$73.50."³⁰² By contrast, in the RJR Nabisco sale, the bidders were unable to reach agreement on stopping the bidding process.³⁰³ "The bidders were played off against each other," and the bidding escalated from \$90 per share to \$109 per share.³⁰⁴ Edward Rock has pointed out that "[t]he bidders' failure to reach an agreement to halt the bidding made the RJR Nabisco shareholders more than \$4 billion richer. By contrast, the Federated shareholders lost at least \$178 million and probably more by virtue of the bidding agreement."³⁰⁵

There are many examples of bid-rigging agreements in recent public change-of-control transactions that should have been per se illegal.³⁰⁶ In these cases, companies that had already submitted bids in a public auction subsequently agreed with a rival bidder to drop out of the process.³⁰⁷ In the battle for J.P. Stevens, West Point-Pepperell and

growers of sugar beets); *Vogel v. Am. Soc'y of Appraisers*, 744 F.2d 598, 601 (7th Cir. 1984) ("[B]uyer cartels, the object of which is to force the prices that suppliers charge the members of the cartel below the competitive level, are illegal per se."); *Live Poultry Dealers Protective Ass'n v. United States*, 4 F.2d 840, 842-43 (2d Cir. 1924) ("We should have supposed that, if one thing were definitely settled, it was that the Sherman Act forbade all agreements preventing competition in price among a group of buyers, otherwise competitive, if they are numerous enough to affect the market.").

³⁰⁰ Rock, *supra* note 218, at 1422.

³⁰¹ *Id.* at 1374.

³⁰² *Id.*

³⁰³ *Id.*

³⁰⁴ *Id.*

³⁰⁵ Rock, *supra* note 218, at 1374.

³⁰⁶ See, e.g., *id.* at 1402; Bryan Burrough, *Lazard Frères Has \$1.55 Billion Pool for Equity Stakes*, WALL ST. J., Aug. 10, 1988, § 1, at 10.

³⁰⁷ We only know about these arrangements because, as agreements between active bidders for public companies, they had to be disclosed under the Williams Act. See 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (2006). It is quite possible that, prior to the beginning

Odyssey Partners agreed to stop bidding against each other and divide up the assets of J.P. Stevens.³⁰⁸ In the take-over battles for Fruehauf, American Standard, and Pabst, the prevailing bidder paid substantial sums to the competing bidder to drop out of the auction process.³⁰⁹ In each of these cases, shareholders lost the ability to sell their company in a full auction process. The express agreements among active purchasers constituted the actions of a naked cartel with no purpose or effect other than to limit competition. Courts should be able to preclude such agreements on their face without having to waste time or resources in considering the parties' market power or purported justifications for their conduct.

The *per se* illegality of express bid rigging should have a substantial deterrent effect in change-of-control transactions. Any express agreements among bidders to terminate the auction process for public companies must be disclosed under the federal securities laws.³¹⁰ Once potential purchasers become aware that these agreements will be deemed illegal on their face, they will more likely refrain from engaging in such public, and easily prosecuted, transactions.

Private equity firms may argue that agreements to limit bidding in an auction process were effected pursuant to a joint venture with legitimate efficiency objectives. Yet the courts should never view an agreement among incumbent bidders to terminate an ongoing auction as a legitimate joint venture. Whenever two bidders agree to terminate a bidding process that has already begun, it will be clear that they had both the capability and the intention to purchase the relevant company on their own. Under such circumstances, the parties could make no valid efficiency arguments for their agreement to end the bidding process. The agreement by one of the firms to drop out of the bidding would constitute nothing more than a naked agreement with a rival not to compete that should be summarily condemned by the courts.

of auction processes, firms have secretly agreed not to compete in such auctions. In most cases, the public would be unaware of such arrangements because they do not have to be disclosed under the securities laws.

³⁰⁸ Burrough, *supra* note 306.

³⁰⁹ Rock, *supra* note 218, at 1402.

³¹⁰ See 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f).

VI. PREVENTING IMPLICIT BID RIGGING IN CHANGE-OF-CONTROL TRANSACTIONS

A. *A New Approach to Implicit Bid Rigging*

Though most express agreements to limit bidding in change-of-control transactions have occurred among firms already participating in an auction, implicit agreements are almost always reached before firms engage in the bidding process at all. Implicit agreements are characterized by understandings among potential purchasers, achieved over a period of years, as to which firms will bid on particular transactions.

Implied agreements to limit competition among potential purchasers in change-of-control transactions should be just as illegal as express agreements. There is now a consensus among economists that tacit price fixing agreements are at least as harmful to consumers as explicit ones.³¹¹ Commentators have concluded that, because "there is no vital difference between formal cartels and tacit collusive arrangements . . . the tacit colluder should be punished like the express colluder."³¹² Tacit collusion, like express price fixing, should be illegal on its face under Section 1 of the Sherman Act. The courts need not inquire into the specific economic effects of such conduct because it harms consumers without offering the possibility of any efficiency benefits.³¹³

In the early twentieth century, U.S. antitrust policy toward express price fixing arrangements among competitors was relatively permissive.³¹⁴ As a result, overt price fixing cartels regularly occurred in several industries, including steel, aluminum, sugar, and shipping.³¹⁵ Recent U.S. antitrust policy, however, has become "considerably more antagonistic" to express price fixing arrangements, as the federal government has more aggressively prosecuted such cartels as criminal antitrust violations.³¹⁶ This increased enforcement has made it much more likely that competitors in the U.S. will avoid express bid rigging in favor of tacit arrangements to limit competition in purchas-

³¹¹ See, e.g., BLAIR & KASERMAN, *supra* note 260, at 205-06 ("Section 1 attacks collusion because it is a joint effort to reap monopoly profits, and tacit collusion has a very similar impact.")

³¹² *Id.*

³¹³ See Piraino, *supra* note 32, at 1166.

³¹⁴ See Susan Athey & Kyle Bagwell, *Optimal Collusion with Private Information*, 32 RAND J. ECON. 428, 428 (2001).

³¹⁵ *Id.* at 428 n.1.

³¹⁶ *Id.* at 428-29.

ing goods and services.³¹⁷ As Susan Athey and Kyle Bagwell have explained, "[W]hen the antitrust policy is antagonistic, the organization of collusive activity may be more secretive and less formal. Firms may avoid direct meetings altogether. Or they may communicate surreptitiously, in 'smoke-filled rooms.'"³¹⁸

Private equity firms are much more likely to engage in implicit than explicit bid rigging. These firms are well aware of the severe antitrust penalties against express bid rigging, and they are too sophisticated to engage in express agreements to limit competition before an auction starts. "It is hard to imagine Henry R. Kravis, co-founder of Kohlberg Kravis, calling up David M. Rubinstein, co-founder of Carlyle, to scheme about how to keep a lid on the bidding for a particular company."³¹⁹ In their public statements, the managers of private equity firms profess nothing less than an intention to compete as aggressively as possible against each other. Stephen Schwartzman has indicated that Blackstone always aims to get what it wants, stating "I want war—not a series of skirmishes. . . . I always think about what will kill off the other bidder." Instead of expressly agreeing not to compete, private equity firms can send subtle signals to each other as to their intentions on whether or not to bid for a particular company. As Andrew Ross Sorkin has explained,

A more likely scenario is that a private equity titan bails out of an auction when it gets too heated, figuring that there will always be another auction for something else. And maybe, just maybe, in the back of his head, the titan is thinking that if he does back out of an auction he will score brownie points from his rival for averting a bidding war.³²⁰

There will rarely be any direct evidence of a conspiracy in such cases. No witnesses will be available to testify that they were aware of any meetings, telephone calls, or e-mails in which the private equity firms directly communicated to each other a plan for allocating winning bids.³²¹ In nearly every case of tacit bid rigging, the only evidence of conspiracy will be indirect and ambiguous, yet the price-depressing ef-

³¹⁷ See *id.* at 429.

³¹⁸ *Id.*

³¹⁹ Sorkin, *supra* note 24.

³²⁰ *Id.*

³²¹ See RICHARD A. POSNER, ANTITRUST LAW: AN ECONOMIC PERSPECTIVE 71 (1976) (pointing out that oligopolists are more likely to collude without any express communication).

fects on shareholders will be no different than if the private equity firms had expressly agreed to allocate winning bids among themselves.³²²

In an oligopolistic market such as the private equity market, buyers can, over a period of time, establish an implicit pattern of conduct under which they take turns in bidding for particular companies. By anticipating their rivals' approach to a particular auction, private equity firms can avoid bidding wars that increase the purchase prices for public companies. Indeed, there is substantial evidence that private equity firms have been successful in limiting bidding for public companies in recent years.³²³ The problem in such tacit price fixing cases has been in distinguishing between permissible parallel conduct and per se illegal implicit price fixing.³²⁴ Too often the courts have engaged in a fruitless search for "plus factors" that has prevented them from condemning implicit cartels harmful to consumers.³²⁵ Indeed, because implicit price fixing arrangements are often more durable than explicit cartels, the courts' approach has had the perverse effect of allowing conduct that is most harmful to consumers to escape anti-trust regulation.³²⁶

The courts need to adopt a new approach that recognizes the pernicious nature of implicit price fixing. When private equity firms pursue identical conduct that is contrary to each firm's legitimate independent interest, they can signal to each other their mutual acquiescence in a market-allocation scheme. In such cases, a court can reasonably infer an illegal conspiracy among the participating firms.

B. "No-Bid" Patterns Justifying an Inference of Conspiracy

The structure of the private equity market makes it easier for firms to implement and sustain implicit bid-rigging arrangements. In a per-

³²² Sorkin, *supra* note 12.

³²³ See Ball, Berman & Lublin, *supra* note 69.

³²⁴ See *Theatre Enters., Inc. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 540 (1954) (noting that "[t]he crucial question" is whether the challenged anticompetitive conduct "stem[s] from independent decision or from agreement").

³²⁵ See, e.g., *Bell Atl. Corp. v. Twombly*, 127 S. Ct. 1955, 1970-74 (2007) (holding that claim of anticompetitive conspiracy among regional telephone service providers amounted to bare assertion of parallel conduct and thus failed to survive 12(b)(6) motion to dismiss); *Williamson Oil Co. v. Phillip Morris USA*, 346 F.3d 1287, 1319-20 (11th Cir. 2003) (affirming trial court's finding that plaintiffs cigarette wholesalers had failed to demonstrate existence of plus factors to establish price-fixing conspiracy among cigarette manufacturers); *Hall v. United Air Lines, Inc.*, 296 F. Supp. 2d 652, 680-81 (E.D.N.C. 2003).

³²⁶ See *supra* notes 259-265 and accompanying text.

fectly competitive market, with many competing sellers and easy terms of entry and exit, it is hard for firms to coordinate their activity without an express agreement. In an oligopolistic market, however, such as the private equity market—where there are few firms with the capability to bid on the largest transactions—firms are able to coordinate their conduct implicitly, without any express agreement, simply by observing the conduct of their rivals. Thus private equity firms can refrain from bidding on a particular transaction, under the implicit understanding that they will be given an opportunity by their rivals to bid on a future transaction—and at a lower price than would occur in a competitive bidding situation. The *Wall Street Journal* has characterized private equity as “an industry that often has shied away from open competition between rival firms for deals.”³²⁷ Indeed, David Bonderman, the founder of the Texas Pacific Group, recently admitted at a merger conference that “[t]here’s [now] less competition for the biggest [going-private] deals.”³²⁸

Achieving a consensus on a particular course of action is facilitated by the information legitimately available in an oligopoly market such as the market for going-private transactions. Approximately seven private equity firms are capable of bidding on the largest going-private transactions, and they are likely to be aware of the same information on pending transactions. These firms frequently communicate with each other, through the consortiums in which they participate and in day-to-day business interactions. For example, Henry Kravis of KKR and Lloyd Blankfein, the chief executive officer of Goldman Sachs (which, with a \$20 billion fund, is the third largest private equity firm), “now get together every few months.”³²⁹ Because of the disclosure requirements of the federal securities laws, private equity firms will know in advance which firms will be bidding for particular public companies.³³⁰ All private equity firms are required under the Williams Act to publicly disclose their participation in the bidding process for a public company.³³¹ Thus, all the firms interested in a transaction will know who their rivals are and are not. Under such circumstances, it will be easy for the firms to establish a pattern of conduct under which certain firms refrain from bidding on a transaction and let a rival obtain the company at a

³²⁷ Sender & Langley, *supra* note 20. The *Wall Street Journal* also stated that “Mr. Schwartzman is willing to play hardball when a rival guns for one of his deals.” *Id.*

³²⁸ Sorkin, *supra* note 24.

³²⁹ Jenny Anderson, *Goldman Runs Risks, Reaps Rewards*, N.Y. TIMES, June 10, 2007, § 3, at 1.

³³⁰ See Williams Act, 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f) (2006).

³³¹ *Id.*

low price, expecting that the rival will extend them a similar "courtesy" in future transactions.³³²

When private equity firms engage in a pattern of conduct that is contrary to their legitimate economic interest, they can send strong signals to each other that all the firms can benefit from an industry-wide agreement to limit bidding in change-of-control transactions. Consider a hypothetical situation in which, over a period of years, such firms engage in a bidding pattern under which only one or two firms submit a bid in each auction for the purchase of a public company. Different firms participate in each bid, so that, over a period of time, each firm has the opportunity to purchase companies with a similar aggregate value. Such a pattern of bidding would be contrary to each firm's legitimate economic interest. In a competitive market, it would be in each firm's interest to bid on any company that it had the ability to purchase and that offered a favorable return, in order to maximize its investment opportunities. No private equity firm would refuse to bid on a favorable transaction and forego a potentially profitable investment opportunity unless it had some implicit assurance from its rivals that, in return, they would assure that firm the opportunity to bid on favorable terms in a future transaction. When firms act contrary to their individual interests and refrain from bidding on companies that they have the capability to purchase, they signal to their rivals that they share a common purpose to limit the price paid for public companies. Such conduct reinforces firms' confidence that, if they avoid a particular bidding situation, they will profit in the future by being able to purchase another company at a lower price, as their rivals in turn refrain from bidding in that transaction.

The courts and agencies can determine whether private equity firms have engaged in a course of implicit collusion by examining the pattern of their conduct over a series of transactions. With a finite amount of funds, private equity firms cannot afford to bid on every transaction, and they know that if they wait their turn, they are likely to receive a more favorable price in future deals. As Andrew Ross Sorkin has explained, "Unlike deals when two rival companies with strategic interests compete—say, Google and Yahoo jockeying for YouTube—private equity is not a zero-sum game. There's always another company to aim for."³³³ Thus, firms will have the incentive to pass up a particular transaction if they have some assurance that more favorable deals will

³³² See *id.*

³³³ Sorkin, *supra* note 24.

be available to them in the future. Private equity firms can receive such assurance if each firm is successful in winning a similar number of bids for companies over an extended period of time. The courts and agencies should be able to infer implicit collusion from a pattern of conduct under which firms decline to bid, or drop out of the bidding, for a particular company and then become the winning bidders in subsequent transactions. Such an implicit sharing of future deals will give private equity firms the assurance they need to refrain from bidding aggressively in particular transactions.

The federal courts have been willing to infer illegal Section 1 conspiracies from similar patterns of conduct in other markets. In 1999, in *Re/Max International, Inc. v. Realty One, Inc.*, the U.S. Court of Appeals for the Sixth Circuit inferred illegal collusion under Section 1 of the Sherman Act when two real estate agents gave each other an implicit assurance that it was safe to implement a commission arrangement that was contrary to their "independent economic interest."³³⁴ Instead of splitting commissions between buying and selling agents on the customary fifty-fifty basis, the defendants adopted a policy providing for a split of seventy-thirty, in their favor, when one of the plaintiff's agents was on the other side of a transaction.³³⁵ The court pointed out that, without assurance that other real estate brokers would adhere to the one-sided arrangement, no broker would want to continue the policy because it would lose business to other brokers that treated all agents equally.³³⁶ Continued adherence to the special commission arrangement only made sense if a broker had some assurance that it rivals would impose the same arrangement on their customers.³³⁷

The proposed approach to inferring implicit bid rigging in change-of-control transactions is also consistent with the U.S. Supreme Court's approach to oligopoly conduct in its 2007 decision in *Bell Atlantic Corp. v. Twombly*, in which the Court refused to infer a Section 1 conspiracy when a group of regional telephone companies declined to compete in each other's territories.³³⁸ The Court pointed out that, in doing so, the companies were simply "sitting tight, expecting their neighbors to do the same thing," and this conduct amounted to nothing more than lawful parallel behavior.³³⁹ When potential purchasers in

³³⁴ 173 F.3d 995, 1009 (6th Cir. 1999) (emphasis omitted).

³³⁵ *Id.* at 1003.

³³⁶ *Id.* at 1010.

³³⁷ *Id.* at 1009.

³³⁸ 127 S. Ct. 1955, 1971 (2007).

³³⁹ *Id.* at 1972.

a change-of-control transaction take turns in bidding for particular companies, however, they are not engaging in independent parallel conduct. A particular private equity firm will only refrain from bidding on a transaction that it is capable of funding if it has some implicit assurance that the successful bidder for that transaction would then step aside in a future transaction. Once a pattern of "you take this one, I will take the next one" becomes established, the conduct of the participating private equity firms will no longer be independent, but interdependent. In such a case, the private equity firms will not be merely "sitting tight" and independently refusing to compete, as the regional telephone companies were in *Bell Atlantic*; rather, they will be signaling to each other when it is appropriate for a particular firm to bid on a transaction. Such signaling, and the pattern of conduct which it establishes, constitutes a form of conspiracy that should be illegal under Section 1 of the Sherman Act.

C. *The Effect of Public Announcements*

Private equity firms may make certain public announcements that send signals to their rivals that it is safe to refrain from bidding on particular going-private transactions. A firm may, for example, announce the types of transactions on which it will consider bidding in the future. It is hard to conceive of a legitimate business reason for such an announcement. It would be in a private equity firm's interest to keep its options open and to decide on a case-by-case basis whether to bid on particular future transactions. When a firm pre-announces its future bidding intentions, it may be reasonable for a court or agency to conclude that the only reason for the announcement was to signal to other private equity firms which transactions they could concentrate on without facing competition from the announcing firm.³⁴⁰

³⁴⁰ The courts and agencies have inferred price fixing conspiracies from pre-announcements of future pricing plans that had no apparent purpose other than to facilitate implicit collusion among competitors. See *In re Coordinated Pretrial Proceedings in Petroleum Prods. Antitrust Litig.*, 906 F.2d 432, 446 (9th Cir. 1990) ("[T]here was essentially no purpose for publicly announcing [future prices] other than to facilitate either interdependent or plainly collusive price coordination."); *FTC v. Abbott Labs.*, 853 F. Supp. 526, 527 (D.D.C. 1994) (describing charges in FTC complaint against three leading manufacturers of infant formula for disclosing information that reduced uncertainty as to the consensus price); *United States v. Airline Tariff Publ'g Co.*, 836 F. Supp. 9, 12 (D.D.C. 1993) (consent decree prohibiting airlines from publishing new fares prior to their effective dates as means of signaling consensus price).

D. The Effect of "Quid Pro Quos"

In certain cases, the federal courts can infer implicit collusion from a specific quid pro quo in a going-private transaction. For example, in return for agreeing not to bid on a going-private transaction, a firm may be offered a favorable position in a consortium formed for a future transaction, or it may ultimately be permitted to join the original consortium after the transaction is completed. One commentator has speculated whether "the Justice Department may want to know if [consortiums] sometimes influence a firm to drop out of the bidding process on a deal or help keep the ultimate buyout price lower than it otherwise would be."³⁴¹ Andrew Ross Sorkin has described a 2004 transaction in which KKR outbid a consortium led by the Carlyle Group for PanAmSat.³⁴² Several months after the transaction closed, the Carlyle Group received an offer from KKR to buy into the group operating the company.³⁴³ Sorkin concluded that "[s]ome would say this is simply good business. Cynics may be tempted to think that unspeakable word [collusion]."³⁴⁴

E. Protecting Legitimate Conduct From Liability

The proposed approach will ensure that firms that have legitimate reasons to pass up particular auctions are not liable under antitrust laws. When a private equity firm decides not to bid on a transaction for a legitimate reason, it will not be acting contrary to its independent self-interest and thus, under the proposed approach, there would be no inference that the firm was engaging in tacit bid rigging. Many private equity firms, for example, will be precluded from bidding individually for a large public company because they lack the resources to finance such transactions on their own. When such firms consistently decline to bid on larger transactions, there should be no inference that they are participating in an implicit bid-rigging arrangement. Indeed, some commentators have speculated that the limited amount of competition among private equity firms for the larger going-private transactions may result not from collu-

³⁴¹ See DOJ Probes Private Equity Firms, *supra* note 38.

³⁴² Sorkin, *supra* note 12.

³⁴³ *Id.*

³⁴⁴ *Id.*

sion, but simply from the fact that there are only a small number of firms capable of bidding for such deals.³⁴⁵

There may be legitimate reasons even for the largest private equity firms to refrain from bidding in certain transactions. For example, most private equity firms will want to avoid transactions in which the target company has agreed to pay a substantial "break-up" fee to an earlier bidder if the transaction with that bidder is not consummated. Because such fees are a liability of the target company, they directly increase the premium that any other bidders must pay for the company. Ken McFadyen has pointed out that, in the bidding war for HCA Hospital Corp., Blackstone would have had no interest in making a bid for the company because "the breakup fee of . . . as much as \$500 million would have meant that any competing party would have had to find considerably more value in HCA than the original suitors."³⁴⁶

VII. PREVENTING ANTICOMPETITIVE CONSORTIUMS IN CHANGE-OF-CONTROL TRANSACTIONS

A. *The Anticompetitive Effects of Consortiums*

In recent years, private equity firms have become increasingly willing to form consortiums to submit a single bid for public companies in going-private transactions.³⁴⁷ Depending upon the circumstances, such consortiums can either enhance or limit competition for the purchase of a public company. Under the proposed approach, the courts should easily be able to distinguish between consortiums that reduce the number of bidders in the auction process and those that add new bidders to the process. Courts should uphold any consortiums that allow bidders to participate in an auction process from which they would have been individually foreclosed, and they should preclude any consortiums among bidders that could have participated in the auction process on their own.

The anticompetitive effects of consortiums can be quite severe in change-of-control transactions. Indeed, such consortiums can limit competition for the purchase of a company just as surely as express or implicit agreements to refrain from bidding. When several potential

³⁴⁵ See, e.g., Sorkin, *supra* note 24 ("Because there are only a few firms big enough to be acquirers in large deals—and many strategic buyers are sitting on the sidelines—they are getting better buys.").

³⁴⁶ MacFadyen, *supra* note 10.

³⁴⁷ See Sorkin, *supra* note 12.

purchasers join a consortium and agree to submit a single bid for a public company, the shareholders of that company lose the advantage of receiving competing bids from each member of the consortium, a process that likely would have increased the price paid for their company. Consortia also discourage other bidders from competing in an auction because of the perceived advantages of a consortium in the bidding process. As Edward Rock has explained,

Once two or more bidders enter into a bidding agreement, they are able to pool their strengths against the remaining bidder or any other bidder who enters the fray. . . . Once . . . [bidders] combine forces, any additional bidders face[] a discouraging prospect. . . . The prospect of competing against such an adversary would likely discourage even higher valuing bidders. . . . As a result, bidding agreements may dissuade higher valuing third parties from entering the contest at all.³⁴⁸

A recent survey of going-private transactions by Dealogic revealed that the prices paid to public shareholders are higher in going-private transactions that do not involve consortia among private equity firms.³⁴⁹ The survey concluded that "buyouts of companies worth \$100 million to \$1 billion (typically deals that do not involve . . . [consortiums]) had an average premium of 27.4 percent; deals over \$1 billion (which usually involved . . . [consortiums]) had an average premium of only 16.5 percent."³⁵⁰ In a 2006 presentation to investors, David Bonderman, the founder of TPG, admitted that "[c]onsortia often limit bidding" for the larger going-private transactions.³⁵¹ Despite such evidence, private equity firms continue to argue that consortia among bidders do not reduce the price paid for public companies.³⁵² As one private equity executive has stated, "As long as two girls show up to the dance, there's enough competition."³⁵³

³⁴⁸ Rock, *supra* note 218, at 1377.

³⁴⁹ See Sorkin, *supra* note 24.

³⁵⁰ *Id.*

³⁵¹ *Id.*

³⁵² Sorkin, *supra* note 12.

³⁵³ *Id.*

B. *Per Se* Legal Bidding Consortiums

1. Consortiums Among Noncompetitors

Any bidding consortiums among noncompetitors in change-of-control transactions should be *per se* legal, because they do not pose any dangers to competition. The only effects of such consortiums will be neutral or positive. No antitrust problem, for example, should arise when a private equity firm teams in a bidding consortium with a banker or institutional investor. Banks and institutional investors do not participate individually in the market for the purchase of public companies. Thus such firms would not be competitors with a private equity firm in a change-of-control transaction, and a bidding consortium among such firms would not reduce competition in the auction for a company.

2. Consortiums That Eliminate Financial Impediments to Bidding

If a bidding consortium gives its participants the ability to bid jointly for a commodity that they could not have purchased on their own, it will have no anticompetitive effects. Herbert Hovenkamp has pointed out that "joint bidding is not the same thing as bid rigging or price-fixing."³⁵⁴ Professor Hovenkamp explains a hypothetical involving bids for a warehouse by two potential purchasers.³⁵⁵ If "one simply agreed to stand down, letting the other win the bid, the two would be involved in criminal bid rigging."³⁵⁶ The two bidders would, however, be promoting competition if they formed a joint-bidding arrangement that allowed them to purchase a warehouse that they did not have the ability to purchase independently because the warehouse was too costly or too large. Under such circumstances a joint bid would allow the parties to "operate the warehouse together or perhaps divide it, and each use half."³⁵⁷

Similarly, consortiums may allow potential purchasers to bid for companies that they could not have purchased on their own. "If neither [partner] had been able to enter the bidding independently, the formation of the group may introduce a new competitor into the

³⁵⁴ Herbert Hovenkamp, *Antitrust Violations in Securities Markets*, 28 J. CORP. L. 607, 619 (2003).

³⁵⁵ *Id.*

³⁵⁶ *Id.*

³⁵⁷ *Id.*

market for corporate control"³⁵⁸ Such arrangements should be upheld on their face because their only effect is to increase competition in the bidding process. Firms may only be able to participate in a bidding process through a consortium because they lack the resources to bid for a company individually. Andrew Ross Sorkin has explained that "private equity consortiums are being driven in large part by the desire of firms to bag bigger game than they could manage on their own."³⁵⁹ Brent Shearer has pointed out the need for a regulatory approach that encourages the formation of consortiums for the largest going-private transactions: "If fear of regulators poking around their deals chills future . . . [consortiums], it also would have the effect of placing companies with market caps of \$10 billion or more out of the reach of buyers for the time being."³⁶⁰

Thus, courts should uphold bidding consortiums that allow small- or medium-sized firms to pool their resources so that they can afford to bid on the purchase of a company with a large market capitalization. Morgan Stanley, for example, entered the private equity market in 2007 with a relatively small buyout fund of approximately \$6 billion.³⁶¹ The fund is not large enough to allow Morgan Stanley to bid on the largest going-private transactions. If Morgan Stanley joined a consortium with other relatively small private equity players to bid for a company with a market capitalization over \$10 billion, the consortium would enhance competition by allowing firms to participate in a company auction from which they would otherwise have been foreclosed.

The courts, however, should not allow consortiums simply because they allow participants who are otherwise capable of purchasing a company to reduce the financial risk of investing in that company. Edward Rock has asserted that joint-bidding arrangements may allow firms to "diversify their investments in an optimal fashion; this in turn may make each more willing to participate in bids for control."³⁶² Such arguments are easy to assert but difficult to confirm. Indeed, it would be extremely difficult for a fact-finder to confirm whether a private equity firm entered a consortium to mitigate its financial risk

³⁵⁸ Rock, *supra* note 218, at 1413.

³⁵⁹ Sorkin, *supra* note 12.

³⁶⁰ Brent Shearer, *Antitrust Inquiry Probes Club Deals*, DEAL MAKER'S JOURNAL, Dec. 1, 2006, available at 2006 WLNR 207622278.

³⁶¹ See Anita Raghavan, *At Morgan Stanley, A Game of Catch-Up*, WALL ST. J., May 29, 2007, at A1.

³⁶² Rock, *supra* note 218, at 1405.

and diversify its investments or simply to help ensure that it paid a lower price for the target company as a result of reduced competition in the auction process.

3. Consortiums That Divide A Target Company's Unrelated Businesses

Firms may also form legitimate bidding arrangements when they would not have been interested, for strategic reasons, in purchasing all the businesses in which a particular company is engaged. Many buyers will not be willing to purchase an entire company if they have to divest one or more of its businesses after the closing. Consider, for example, an auction for the sale of a conglomerate such as United Technologies, which operates several unrelated businesses, including aerospace, air conditioning, and elevators.³⁶³ Few buyers may be interested in purchasing all of the business lines in which United Technologies is engaged. In such a case, companies involved in aerospace, air conditioning, and building construction businesses legitimately could enter into an arrangement to bid jointly for United Technologies and then divide the company's businesses among themselves after the closing of the transaction. Such a bidding arrangement would constitute an efficiency-enhancing integration of the parties' interests in complementary portions of the business. The arrangement would allow each of the parties to participate in an auction process for a company that they otherwise would not have purchased, and the shareholders of United Technologies would benefit by having an additional bidder for their company.

If a firm anticipates antitrust problems because of a market overlap with a particular part of a company, it can team with another firm that is interested in that business, thereby avoiding an antitrust challenge. Consider a hypothetical consortium formed by General Motors and Caterpillar to purchase a company that manufactures light trucks and has developed a new technology for fuel-efficient "hybrid" automobiles. Assume that General Motors would be foreclosed under the antitrust laws from purchasing the light truck portion of the business because of the significant collective market shares of General Motors and the target company, but that General Motors is interested in acquiring the company's technology for hybrid automobiles. For its part, Caterpillar is interested in diversifying into the light truck business but

³⁶³ See J. Lynn Lunsford, *Boss Talk: Transformer in Transition*, WALL ST. J., May 17, 2007, at B1 (interview with George David, the CEO of United Technologies, in which he states, "We cool things, heat things, fly things, elevate things, send people to the moon.").

would not be interested in the new fuel technology. Under such circumstances, the bidding consortium would allow General Motors to purchase the new fuel technology for hybrids and Caterpillar to purchase the light truck business, thereby convincing those companies to participate in an auction they otherwise would have avoided.

Some bidding consortiums ostensibly designed to provide for a more efficient division of a company's assets may amount to nothing more than a per se illegal cartel. There would be no reason for potential purchasers to form such a consortium if they were already directly competing with each other. In such a case, it would be no more efficient for the bidders to divide up the target company's assets than for one bidder to operate all of the assets on its own. Thus "it would be difficult to ascertain whether the prospect of efficiently dividing the target's assets, and not of capping the amount they must pay for them, was the parties' predominant motivation for agreeing not to bid competitively."³⁶⁴ Consider a consortium formed by Macy's and Nordstrom's to bid for the purchase of Target Brands, Inc. ("Target"). Assume that, in an antitrust suit by the shareholders of Target, Macy's and Nordstrom argued that they formed the consortium in order to allow for a more efficient division of the assets of Target rather than to reduce the price paid for Target. A court should easily be able to appreciate the weakness of such an argument. There is no reason why either Macy's or Nordstrom could not operate Target just as effectively as a whole. Both companies have extensive experience in the department store business and would be equally effective as owners of Target. It would therefore be reasonable for a fact-finder to conclude that the real purpose of the consortium was to reduce the price that Macy's and Nordstrom would each have to pay for the assets of Target.

4. Consortiums That Combine Complementary Competencies

A joint-bidding arrangement may allow two strategic buyers to combine their complementary skills in a way that permits them to manage an acquired company more effectively.³⁶⁵ Assume that Wal-Mart and John Deere form a consortium to purchase the Jaguar automobile brand from the Ford Motor Company. The companies may be able to demonstrate that, with Wal-Mart's expertise in distribution and John Deere's expertise in manufacturing, they could operate Jaguar more effectively as partners than as individual companies. The courts

³⁶⁴ Rock, *supra* note 218, at 1411.

³⁶⁵ *Id.* at 1410.

should not, however, allow consortiums among private equity firms on grounds that they could allow for the more efficient operation of an acquired company. Private equity firms usually do not have any special operational expertise in a particular industry.³⁶⁶ Their expertise is largely in the areas of financing and general management oversight.³⁶⁷ Private equity firms rely on the management of acquired companies for the specific operational expertise necessary to run the company. Thus, it is unlikely that two or more private equity firms would have to team with each other to improve their capabilities in managing a company.

C. *Per Se Illegal Bidding Consortiums*

If the firms in a consortium have the ability to bid on their own in the relevant transaction, the consortium will limit competition in the bidding process without generating any countervailing efficiencies. Such consortiums constitute nothing more than naked cartels that should be illegal on their face. Indeed, when private equity firms form a consortium to bid for a company they could have purchased on their own, the consortium has the same purpose and effect as an express bid-rigging arrangement. Such a consortium substitutes a single bid for the multiple competing offers that otherwise would have been available to the selling shareholders.

In 2007, the largest private equity firms had sufficient assets to bid on their own in most public company auctions.³⁶⁸ Goldman Sachs, Blackstone, and KKR each had funds of approximately \$20 billion;³⁶⁹ TPG's fund reached \$15 billion;³⁷⁰ and Bain Capital's fund was approximately \$10 billion.³⁷¹ The *Wall Street Journal* pointed out in 2007 that "These large pools . . . [gave the private equity firms] enough heft to do deals on their own."³⁷² Firms could leverage these substantial pools of equity through bank borrowings. John Lynch, chief market analyst at Evergreen Investments, estimated in 2007 that such borrowing permitted private equity funds to invest at a rate of approximately

³⁶⁶ Rick Newman, *Private Equity: An Expert Tells How It's Done*, U.S. NEWS & WORLD REP., Nov. 22, 2006, available at <http://www.usnews.com/usnews/biztech/articles/061122/22daniello.htm>.

³⁶⁷ See *id.*

³⁶⁸ See Sender, Berman & Smith, *supra* note 25; Sorkin & Krauss, *supra* note 252.

³⁶⁹ Sorkin & Krauss, *supra* note 252; see also Sender, *supra* note 253 (describing Goldman Sachs's \$19 billion fund).

³⁷⁰ Sender, Berman & Smith, *supra* note 25.

³⁷¹ *Id.*

³⁷² Berman, *supra* note 39.

four times the value of their equity funds, "which means that there [was] \$600 billion chasing the market."³⁷³

In 2007, private equity firms were able to access additional equity financing by selling a portion of their own funds to the public. Blackstone, for example, conducted an IPO for a portion of its management fund in 2007, and KKR announced that it would finally go public in 2008.³⁷⁴ By going public, these firms gained a source of permanent capital and no longer "need[ed] to depend on endless rounds of time-consuming fund raising from . . . investors. . . ."³⁷⁵ The firms also gained the ability to offer their stock as well as cash to finance acquisitions.³⁷⁶ The *Wall Street Journal* estimated in 2007 that, given their access to broad sources of both equity and debt financing, the "buying range" of the largest private equity firms was "closing in on transactions valued at upward of \$50 billion each."³⁷⁷ With such financial clout, the large private equity firms should not have had to form consortiums with their rivals to bid even for the largest of America's public companies. As the *Wall Street Journal* explained in 2007, KKR's IPO reduced "the need [for the firm] to partner with large consortiums of private equity firms on large leveraged buyouts."³⁷⁸

Recent transactions illustrate the importance of preventing bidding consortiums among larger private equity firms. In February, 2007, Blackstone was required to raise its initial offer for Equity Office Properties by \$3 billion in order to beat a competing offer from Vornado Realty Trust.³⁷⁹ If Blackstone and Vornado had formed a bidding consortium, they would have eliminated all competition for the purchase of Equity Office Properties, and the shareholders of the company would have lost \$3 billion in economic value. There are several recent examples of consortiums among private equity firms that likely reduced the prices paid in going-private transactions. In February, 2007, KKR and TPG teamed up to purchase the TXU Corpora-

³⁷³ E.S. Browning, *What Could Topple Bulls' "Wall of Worry"?*, WALL ST. J., July 16, 2007, at C1.

³⁷⁴ Berman & Sender, *supra* note 8; see also Andrew Ross Sorkin, *After Delay, KKR Finds a Way to Go Public*, N.Y. TIMES, July 28, 2008, available at <http://www.nytimes.com/2008/07/28/business/28kk.html?dbk>.

³⁷⁵ Berman & Sender, *supra* note 8.

³⁷⁶ *Id.*

³⁷⁷ *Id.*

³⁷⁸ Dennis K. Berman & Henny Sender, *KKR's IPO May Set Firm on Rugged Path*, WALL ST. J., July 5, 2007, at C1.

³⁷⁹ See Andrew Ross Sorkin, *The Biggest Buyout Ever Could Have Been Bigger*, N.Y. TIMES, Feb. 11, 2007, § 3, at 8 (referring to the "additional \$3 billion over Blackstone's original takeover proposal").

tion, a Texas utility, for \$45 billion, including the assumption of \$12 billion in debt.³⁸⁰ In addition, it was projected that the consortium would have to raise another \$30 billion in debt to finance the transaction, which would have left only \$3 billion in equity for the consortium to contribute on its own.³⁸¹ The consortium was granted the exclusive right to negotiate with TXU, making "a rival bid more difficult," if not impossible.³⁸² Given the size of their own private equity funds (\$20 billion and \$15 billion, respectively),³⁸³ both KKR and TPG could have invested \$3 billion on their own for TXU. A consortium formed to purchase another Texas energy company, Kinder Morgan, in 2006 was no less anticompetitive. The consortium included, among others, Goldman and Carlyle, either of which could have afforded to purchase Kinder Morgan on its own.³⁸⁴ In 2006, KKR, Bain Capital and Merrill Lynch teamed up to acquire hospital operator HCA Hospital Corp. for \$21 billion.³⁸⁵ Each of these firms had the capacity to bid individually for HCA. If they had done so instead of forming a consortium, the price paid to the shareholders of HCA would likely have been higher.

There is no legitimate reason for firms to enter into joint-bidding arrangements after they have already begun to participate in the bidding process for a company. At that point, it will be clear that the firms have the ability to bid individually for the company that is in play. Any consortium formed among active bidders can only be designed to limit competition for the purchase of a controlling interest in the company. In the Federated transaction, for example, Campeau and Macy's had already submitted rival bids for Federated when they agreed to halt all future bidding in exchange for Campeau's agreement to allow Macy's to purchase two divisions of Federated from Campeau after the transaction was completed.³⁸⁶ The agreement between Macy's and Campeau possessed none of the characteristics of a legitimate joint venture. The parties did not combine any resources or attempt to achieve any efficiency objective. Because the parties had already elected to enter the bidding process on their own, it was clear that they did not need to form a joint-bidding arrangement in order

³⁸⁰ Smith, Berman & Sender, *supra* note 87.

³⁸¹ Sorkin & Krauss, *supra* note 252.

³⁸² Sender, Berman & Smith, *supra* note 25.

³⁸³ See *supra* notes 252–253 and accompanying text.

³⁸⁴ See Sorkin & Krauss, *supra* note 252.

³⁸⁵ Berman et al., *supra* note 59.

³⁸⁶ See *Finnegan v. Campeau Corp.*, 915 F.2d 824, 826 (2d Cir. 1990).

to compete in the auction for Federated; their only purpose was to eliminate competition between them for the purchase of Federated. By virtue of the agreement, the parties were able to ensure that the company was sold for a lower price than it would have fetched in an unfettered auction. Such an agreement constituted a naked cartel that would have been illegal on its face under the proposed approach.

CONCLUSION

Public shareholders likely have suffered billions of dollars in losses in recent years as a result of collusion among potential purchasers in change-of-control transactions. Neither state corporate laws nor the federal securities laws provide an effective remedy for the economic harm resulting from such conduct. The only potential remedy for shareholders is a Sherman Act case against the firms that have colluded to hold down the price paid for their shares.

Unfortunately, the federal courts have been unable to devise an appropriate antitrust approach to collusion in change-of-control transactions. Indeed, the Second Circuit's decision in *Finnegan* could be interpreted to completely exempt collusive conduct in such transactions from antitrust regulation. The U.S. Supreme Court's earlier antitrust cases, however, as well as its most recent decision in *Credit Suisse*, make it clear that there should be no implied revocation of the antitrust laws in change-of-control transactions. Applying the antitrust laws to such transactions will not interfere with the SEC's enforcement of the disclosure provisions of the securities laws. Thus there is no reason to deprive public shareholders of the remedies available under the antitrust laws.

After *Credit Suisse*, the federal courts should be free to develop a new antitrust approach to collusion among purchasers in change-of-control transactions. This Article proposes an approach that would effectively protect the shareholders of American companies. Express agreements among active or potential purchasers to refrain from bidding in company auctions would be illegal on their face. Tacit agreements to limit bidding, which pose an even greater threat to shareholders, would be no less illegal. In contrast to the current lenient standards of the federal courts, which allow many cases of tacit collusion to escape liability, the proposed approach would deter private equity firms from implicit arrangements to limit competition in change-of-control transactions. The proposed approach also provides an effective means of distinguishing between illegal and permissible consortiums among potential bidders for companies. The approach

will encourage potential bidders who could not otherwise participate in company auctions to form joint-bidding arrangements. At the same time, the proposed approach will deter bidders from using consortiums as a means of facilitating agreements to limit the price paid for companies in change-of-control transactions.