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FTC CHALLENGES ROLL-UP STRATEGY AS ILLEGAL MONOPOLIZATION

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On September 21, 2023, the Federal Trade Commission ("FTC"), delivering on recent agency promises to increase scrutiny of private equity-backed transactions and strategies, released a complaint filed against private equity sponsor Welsh, Carson, Anderson, and Stowe ("Welsh Carson") and U.S. Anesthesia Partners ("USAP"), a Texas-based provider of anesthesia services and a Welsh Carson portfolio company. With this slate of claims, the FTC takes aim at Welsh Carson and USAP's serial acquisitions over a decade, post-merger conduct, and the "roll-up" strategy employed by USAP and Welsh Carson.

The complaint alleges numerous violations of Sections 1 and 2 of the Sherman Act, asserting defendants monopolized, conspired to monopolize, and entered into agreements to fix prices and allocate markets with respect to commercially-insured hospital-only anesthesiology services. The complaint also claims defendants violated Clayton Act Section 7 and Section 5 of the FTC Act through a string of serial acquisitions which allegedly lessened competition in Texas. The complaint asserts that defendants' "roll-up" strategy represented an "unfair method of competition." Finally, the complaint alleges that Welsh Carson's acquisitions, pricing actions, and horizontal agreements together represent a "scheme to reduce competition in Texas" under Section 5 of the FTC Act. The FTC has asserted in this complaint a novel test for "unfair methods of competition" that forms the basis for separate and standalone claims under Section 5.

Roll-Up Strategy

Private equity firms look for opportunities to use their deal-making, operational, and financial expertise, along with their significant equity funding resources, to create more efficient companies in competitively fragmented landscapes. One strategy, the "roll-up" (also often referred to as a "buy and build" strategy"), entails combining numerous, smaller companies in a particular

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The M&A Lawyer, April 2022, Vol. 26, Issue 4; *The M&A Lawyer*, May 2020, Vol. 24, Issue 5; *The M&A Lawyer*, May 2019, Vol. 23, Issue 5.

[2]For the complete survey, *see*: https://www.seyfarth.com/dir_docs/publications/2023_MA_SurveyBook.pdf.

DELAWARE'S CORPORATE OPPORTUNITY WAIVER COMES TO CANADA: TAKEAWAYS FOR U.S. PRIVATE EQUITY AND CROSS-BORDER M&A

By Sarah Gingrich, Brad Schneider, Grant McGlaughlin, Caitlin Rose and Paul Blyschak

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Its not unusual for Canadian courts to look to Delaware caselaw for guidance, particularly in M&A disputes. It is less common for Canadian legislators to take a page out of Delaware's statutory playbook. But this was recently done by Alberta when it adopted, *near verbatim*, Delaware's corporate opportunity waiver into the province's *Business Corporations Act* ("ABCA").

We explore the practical implications of this noteworthy development for U.S. cross-border investment into Canada, including by private equity buyers and investors. Numerous points warrant highlighting.

First, Alberta's adoption of Delaware's corporate opportunity waiver represents an additional and incrementally "private equity friendly" aspect of the ABCA. Second, the risk mitigation opportunities offered by Alberta's corporate opportunity waiver (as well as the other "private equity friendly" aspects of the ABCA) to U.S. investors *into Canada* need not necessarily be limited to investment *into Alberta*. Third, even though Alberta's corporate opportunity waiver is essentially identical to Delaware's *as written*, we caution against expecting it to be *interpreted and applied* in lockstep with its Delaware forebear.

DGCL s.122(17): The Original Corporate Opportunity Waiver

The duty of loyalty has been called "a cornerstone of Anglo-American corporate law" as well as the "most *demanding* and *litigated* fiduciary obligation" imposed on directors.[1] The decision by the Delaware legislature in 2000 to create a statutory right to waive a "crucial part" of the duty of loyalty—the corporate opportunities doctrine—has therefore been described as a "dramatic departure from tradition."[2]

That said, the motivation of Delaware lawmakers in allowing corporate opportunity waivers is well known. A "growing chorus of critics" were arguing that the "exacting requirements" of the duty of loyalty was impeding "corporations' ability to raise capital, build efficient investor bases, and secure optimal management arrangements."[3] Proponents of corporate opportunity waivers highlighted that private equity and venture capital were subjecting their financial sponsors to "fiduciary duties in profound conflict with either their larger business plans or with fiduciary obligations they owe to other business entities."[4] Such proponents also highlighted the "conundrum of allocating corporate opportunities between a parent and its partially owned subsidiary, both operating in a similar industry and sharing common board members and officers."[5]

The solution was *Delaware General Corporation Law* ("DGCL") s.122(17), which provides that:

> Every corporation . . . shall have power to. . . [r]enounce . . . any interest or expectancy of the corporation in, or in being offered an opportunity to participate in, specified business opportunities or specified classes or categories of business opportunities that are presented to the corporation or 1 or more of its officers, directors or stockholders.

ABCA s.16.1(1): Alberta Brings the DGCL North

That Alberta's recent adoption of corporate opportunity waivers was (at least in part) inspired by Delaware is manifest. In near mirror fashion to DGCL s.122(1), ABCA s.16.1(1) provides:

> [A] corporation may waive any interest or expectancy of the corporation in or to, or in being offered an opportunity to participate in, a specified business opportunity or specified classes or categories of business opportunities that are offered or presented to the corporation or one or more of its officers, directors or shareholders.

As with Delaware, the Alberta legislature was also clearly seeking to encourage increased private equity and venture capital investment in the province.[6] Among other things, in announcing the amendments the Alberta government expressly acknowledged it sought to accommodate investors who often "choose to invest in corporations in the same line of business," who "frequently . . . sit on the boards of companies they have invested in," and who "may be reluctant to invest in a company if it means they will never be able to invest in another similar venture in the future."[7]

Advantage ABCA for Private Equity in Canada?

Canada does not have a law prohibiting interlocking directorates similar to Section 8 of the *Clayton Act*. However, the Supreme Court of Canada (the country's highest court) has ruled that fiduciary duties in Canada, including the duty of loyalty, are "pervaded" by a "strict ethic" and should be "strictly applied."[8] The adoption of corporate opportunity waivers by Alberta, the first (and only) Canadian province to do so, is therefor notable: it represents a clear break from the otherwise "strict ethic" characterizing fiduciary duties in Canada.

That said, it is also important to appreciate that Alberta's adoption of Delaware's corporate opportunity waiver represents an additional and incrementally "private equity friendly" aspect of the ABCA. Perhaps most importantly, the ABCA is *also* Canada's *only* corporate statute that allows nominee directors to weigh the interests of their *nominating shareholder* alongside the interests of the corporation in honouring their directors' duties. Specifically, ABCA s.122(4) provides:

> In determining whether a particular transaction or course of action is in the best interests of the corporation, a director, if the director is elected or appointed by the holders of a class or series of shares . . . may give *special*, but *not exclusive*, consideration to the *interests of those who elected or appointed the director* (emphasis added).

Other "private equity friendly" features of the ABCA include the absence of any Canadian residency requirements for directors, the recently expanded "due diligence" defence available to directors, and the recently expanded ability of corporations to indemnify directors.

What are the key practical takeaways for U.S. private equity and cross-border M&A into Canada? We briefly consider two.

First, U.S. private equity considering the acquisition of or investment into an Alberta-incorporated company should seek to maximize the private equity friendly features of the ABCA. At the point of acquisition or investment this includes the availability of a Delaware-style corporate opportunity waiver. Over the lifecycle of the investment this includes the ability of nominee directors to give special (but not exclusive) consideration to the private equity sponsor's interests.

Second, U.S. private equity considering the acquisition of or investment into a Canadian company incorporated *outside Alberta* can consider continuing the company into Alberta to gain access to the benefits offered by the ABCA. In the case of an acquisition, this can be effected as part of closing or post-closing. In the case of an investment (as opposed to an outright acquisition), this can be made a condition of the investment. In either case, continuation into Alberta does not impede doing business outside the province, and it is not uncommon for a business incorporated in one Canadian jurisdiction to have most—or even all—of its operations in other Canadian jurisdictions.

How Much Corporate Opportunity Can an ABCA Company Waive?

Returning to the specific matter of Alberta's new Delaware-style corporate opportunity waiver, exactly how far can such waivers go?

Somewhat surprisingly, although enacted in 2000, the "footprint" of Delaware's corporate opportunity waiver in "caselaw and commentary has been surprisingly faint."[9] Stated differently, few Delaware courts have had occasion to "opine on the validity of a broad and general renunciation of corporate opportunities, as contrasted with a more tailored provision addressing a specified business op-

portunity or a well-defined class or category of business opportunities."[10]

However, even had the subject been thoroughly explored by Delaware's courts, there is reason to question whether Canadian courts would walk an identical path.

First, as noted above, Canada's highest court has held that fiduciary duties in Canada are "pervaded" by a "strict ethic" and should be "strictly applied."[11]

Second, and in what is essentially a legislative echo of the foregoing court ruling, each of Canada's common law provinces' corporate statutes (including the ABCA) specifies that "no provision in a contract, the articles, the bylaws or a resolution relieves a director" from their fiduciary duties or "from liability for a breach of that duty."[12] By contrast, DCGL s.102(b)(7) "permits a charter provision to eliminate [a director's] monetary liability for breaches of the duty of care."[13]

Third, a difference between Alberta's corporate opportunity waiver and that of DGCL s.122(1) is that, while the latter can be effected via the corporation's certificate of incorporation *or* "by action of its board of directors," the former may *only* be effected via the corporation's articles of incorporation or a unanimous shareholders agreement and *not* at the board level. This more circumscribed means of implementation arguably reflects a more guarded attitude on the part of Alberta's legislators than exhibited by Delaware's.

It may therefore be that Alberta courts will take a more restrained approach to the interpretation and application of corporate opportunity waivers than Delaware courts. For example, an Alberta court may require the "specified classes or categories of business opportunities" to which the waiver applies to be identified with greater particularity than expected by a Delaware court.

Concluding Comments: Private Equity's Card to Play

Empirical research confirms the "enormous appetite" exhibited by U.S. corporations for "contracting out of the duty of loyalty when freed to do so."[14] So too has such research confirmed the "often . . . capacious scope and reach" of the corporate opportunity waivers adopted by Delaware corporations.[15]

It remains to be seen whether Alberta's corporate opportunity waiver will encounter the same eager demand. We would, however, expect private equity, venture capital and other sophisticated financial investors to lead the charge. We also highlight that the risk mitigation opportunities presented by Alberta's corporate opportunity waiver (as well as the other "private equity friendly" aspects of the ABCA) to U.S. investors *into Canada* need not necessarily be limited to investment *into Alberta*. Finally, while corporate opportunity waivers under Delaware have often exhibited a "capacious scope and reach," we would caution towards a more conservative approach under Alberta law, at least based on current indications and a high-level comparison of broader corporate law hallmarks between the two jurisdictions.

ENDNOTES:

[1]G. Rautenberg & E. Talley, "Contracting Out of the Fiduciary Duty of Loyalty: An Empirical Analysis of Corporate Opportunity Waivers," (2017) 117 *Columbia Law Review* 1075 [Rautenberg & Talley] at page 1076 (emphasis added).

[2]Rautenberg & E. Talley p. 1075.

[3]Rautenberg & E. Talley p. 1079-1080.

[4]Rautenberg & E. Talley p. 1080.

[5]Rautenberg & E. Talley p. 1093.

[6]As a noteworthy aside, the professional commentary of one of this article's authors, Grant McGlaughlin, was cited by the Alberta legislature in approving the ABCA's corporate opportunity waiver.

[7]Government of Alberta, Service Alberta, Business Corporations Act Fact Sheet (PDF; https://www.alberta.ca/system/files/custom_downloaded_images/sa-business-corporations-act-proclamation-fact-sheet.pdf) (2022).

[8]*Can. Aero v. O'Malley*, 1973 CanLII 23 (SCC), [1974] SCR 592 at pp. 593, 607, 610.

[9]Rautenberg & E. Talley p. 1098.

[10]*Alarm.com Holdings, Inc. v. ABS Capital Partners Inc.*, 2018 Del. Ch. LEXIS 193 at *22 note 46.

[11]*Can. Aero v. O'Malley*, 1973 CanLII 23 (SCC), [1974] SCR 592 at pages 593, 607 and 610.

[12]ABCA s.122(3).

[13]*New Enterprise Associates 14, L.P. v. Rich*, 295 A.3d 520 at *549 *(Del. Ch. 2023).*

[14]Rautenberg & E. Talley p. 1075.

[15]Rautenberg & E. Talley p. 1075.

"AN OVERWHELMING CALL FOR VIGOROUS MERGER ENFORCEMENT"

By Jonathan Kanter

Jonathan Kanter is Assistant Attorney General for the Antitrust Division of the Department of Justice. The following is edited and adapted from remarks he gave at the Georgetown Antitrust Law Symposium on September 19, 2023, in Washington, D.C.

At the Third Annual Georgetown Antitrust Conference in 2009, the Federal Trade Commission and the Department of Justice announced the public comment process that led to the 2010 Horizontal Merger Guidelines. A lot has changed in those 14 years. While I'm sure the audience here at Georgetown had many thoughts, only 44 commenters wrote to the agencies in response to that initial call for comments.[1] The broader public showed little interest in increasing antitrust enforcement. Agency staffing levels were continuing a decades-long decline.

Today, we are working to revise the merger guidelines against a very different landscape. Since 2010, we have heard growing concerns about the level of competition in key sectors of the American economy. Waves of academic studies document how the public loses out when mergers lessen competition in industries across our economy.[2]

The problem is not limited to consumer markets. At the same time, a robust literature has emerged documenting how workers lose out from too little labor market competition.[3] We have the good fortune to have Ioana Marinescu at the division alongside heroic attorneys and EAG economists, helping revitalize our labor market efforts including in the merger guidelines. The health of our economy depends on the ability of workers to get competitive wages and terms for their efforts.

The biggest change since 2009, though, has been the public's awareness of consolidation and the resulting harms. Numbers in regressions are one thing, but real harms to real people are reawakening Americans to the importance of antitrust enforcement.

We are hearing that loud and clear in the public comment process. Our initial request for comment on the guidelines generated over 5,000 responses from the public. And [on Sept. 18], the comment period on the draft closed with over 3,000 comments submitted on Regulations.gov and thousands more e-mailed to the agencies. The public comments overwhelmingly call for vigorous merger enforcement.

For example, we received several hundred comments from writers and other creators concerned about the impacts of media-industry consolidation on their profession. We have so many comments like the one from a television writer who told us that "the more the media companies merge, the fewer jobs are available for writers, and less compensation is offered."[4]

We hear a startlingly similar concern from doctors, nurses and other healthcare workers who report that consolidation has made it harder to do what they love and treat patients with care and flexibility. One ICU nurse from California said what so many in her profession did. She worked for a community hospital that had "remarkable care" for patients. But after a merger, she says nursing ratios dropped, vacation time was stripped from nurses and practice expectations became "unsafe." Her comment urges the department to "prevent further mergers that limit choice for consumers, especially in healthcare," and to "enforce the antitrust laws already passed."[5]

I want the writers, nurses, farmers, concerned citizens and all the other public commenters to know—the Justice Department hears your concerns. Economic harm and suffering are not just triangles and curves, they are real human consequences for real people. Citizens are speaking up and we are listening. Our litmus test for success is whether we are serving the needs of the American people. They are now watching too and they are demanding that we do more and that we do better to protect a competitive economy.

For that reason, we will read all the comments, from lay