CEPR
CENTER FOR ECONOMIC AND POLICY RESEARCH

October 19, 2021

Sen. Elizabeth Warren
Hart Senate Office Building, 317
Washington, DC 20510

Re: Stop Wall Street Looting Act

Dear Senator Warren,

I am writing regarding your proposed Stop Wall Street Looting Act, which would prevent private funds from imposing all the costs of their risky investments on investors, workers, and communities while profiting from all the gains. Despite the millions of jobs lost during the pandemic and the hundreds of thousands of lives lost to COVID-19, in the two years since the Stop Wall Street Looting Act was first introduced, private equity has experienced explosive growth. After a brief pause in the first half of 2020, global assets under management renewed their upward trend to reach new highs and are predicted to double from $4 trillion in 2020 to over $9 trillion in 2025.[1] Dry power – capital committed to global buyout firms but still waiting to be deployed – has risen to $3 trillion.[2] PE firms in the U.S. are selling off companies in their fund portfolios at a frenzied pace. The total value of companies sold in the first three-quarters of 2021 is $633 billion. This is nearly double the $323 billion for all of 2019 and the $366 billion in 2020. The 2021 results are driven, in part, by a large number of high-priced IPOs as PE-owned companies are sold into a booming stock market. PE-backed companies are going public at a higher rate than has been the case for many years; prices in the stock market in 2021 are 18.0 times earnings (EBITDA), an astonishing multiple.[3] These highly profitable PE exits in the fourth quarter of 2020 and the first three quarters of 2021 have likely raised the returns of PE funds that were barely keeping up with the stock market. Fundraising by PE firms remains

---

[1] Cameron Joyce. 2020. "Future of Alternatives 2025: Private Equity AUM Will Top $9tn in 2025." *Prequin,* November 4. https://www.preqin.com/insights/research/blogs/private-equity-aum-will-top-9tn-in-2025
[2] Benjamin Robertson. 2020. "Private Equity Turns to $3 trillion in Unlocked Value for Loans." *Bloomberg News*, December 11. https://www.bloomberg.com/news/articles/2020-12-31/private-equity-turns-to-3-trillion-in-unlocked-value-for-loans
[3] Rebecca Springer. 2021. "US PE Breakdown: Q3 2021." *PitchBook*, October. https://files.pitchbook.com/website/files/pdf/PitchBook_Q3_2021_US_PE_Breakdown.pdf#page=1 P. 18 and 20

brisk, though not as robust as in recent years. Between 400 and 500 PE funds were launched in every year from 2014 to 2020. Fewer but larger funds, including mega funds that have raised $5 billion or more, were closed in the first three-quarters of 2021 with a combined value of $237 billion compared to $327 billion for full year 2019 and $270 billion for 2020. KKR raised $18.5 billion for its buyout fund, North America Fund XIII. Carlyle has announced a target of $27 billion for its Fund VIII, which will be the largest buyout fund ever.[4] Americans in every community are affected by the industry. Today, more than 11.7 million people are employed by private equity-firms and the companies they own.[5] With its coffers overflowing, private equity is poised to buy out companies in every state and industry.

Over the last decade, an increasing number of private equity and other private funds have taken controlling interests in hundreds of viable companies, using their assets to secure unsustainable loads of debt that the companies, and not their PE owners, will have to repay. The lack of transparency has made these transactions murkier than ever. Middle market PE funds that actively engage in buying out Main Street companies and taking over local brands now finance these leveraged buyouts mainly through private credit funds such as Blackstone Credit, Owl Rock Capital Advisors and Apollo Capital Management rather than through investment banks. The result is little to no public information about these buyouts, including the price paid or the amount of debt used in the transaction. In addition to loading acquired companies with debt, PE owners may strip the company of its wealth via monitoring and transaction fees, collecting dividends, or selling off its physical assets. The sale of junk bonds to finance dividend payouts to companies' owners reached a record in the first nine months of 2021, surpassing the full-year record set in 2013.[6] This transfer of wealth from the company to its PE owners prevents it from investing in the products and people that will allow it to thrive in the future. PE funds charge their limited partner investors high fees without providing them visibility or control into their activities and feed a growing market for risky corporate debt that is reaching dangerous levels. Your proposed legislation would address the worst abuses of this business model while preserving productive investments by requiring PE firms to face accountability for their management decisions;

[4] Ibid. P. 26 and 27
[5] https://www.investmentcouncil.org/
[6] Sebastian Pellejero. 2021. "Junk Loan Sales Fuel Dividend Payouts" *Wall Street Journal*, October 3. https://www.wsj.com/articles/record-junk-loan-sales-fuel-dividend-payouts-11633223949

limiting their ability to loot the companies they take over; empowering investors to fully understand private equity and other private funds; and protecting workers, vendors, suppliers, creditors, customers and other stakeholders and businesses across the country.

The Leveraged Buyout Model

Leveraged buyouts are a central feature of the private equity business model, but have also been used by hedge funds (ESL and Sears) and real estate investment trusts (Vornado and Toys 'R Us). In a leveraged buyout, a private equity firm sponsors an investment fund that acquires a target company for its portfolio using capital supplied by investors as the down payment or equity contribution to the deal. It finances the balance of the purchase using large amounts of debt ("leverage") that the acquired company — not the PE firm or the PE investment fund — is responsible to repay. The PE firm, via the General Partner (a committee of principals in the PE firm), contributes very little to the transaction — typically 2 cents to the private equity fund for every dollar contributed by the Limited Partner investors, which are pension funds, endowments, sovereign wealth funds, and wealthy individuals. For example, if a private fund finances the acquisition of the target company with 50 percent debt, the private equity firm has just 1 percent (.02*.5 = .01) of the purchase price of the business at risk.

Thus, the PE firm is playing with other people's money while facing little accountability for its decisions. Despite putting up only 2 percent of the equity used to purchase the target company for its PE fund's portfolio, the PE firm typically collects 20 percent of any profit from the subsequent resale of the company. Debt boosts returns from a successful exit from the company. Meanwhile, through fees and other forms of asset stripping, PE firms drain value from target companies, hurting their workforce, customers, suppliers, and creditors and forcing cuts to research, training, and other important investments that facilitate long-term success for a company and its stakeholders. With little to lose, but much to gain by loading the target company with debt, the PE firm is in a low risk, high return situation. A high debt burden puts the target company, its employees and its creditors at increased risk of bankruptcy.[7]

[7] Eileen Appelbaum and Rosemary Batt. 2014. *Private Equity at Work: When Wall Street Manages Main Street*, NY: Russell Sage Press.

Your bill would align the incentives of the PE firm and the target company by requiring the PE firms to share liability with the target company for debt. PE funds will still make money from deals that provide investments in target companies that allow them to grow and thrive, but deals that rely on financial engineering and aggressive asset stripping of companies will no longer be viable. This critical reform will end the most abusive practices of the industry while preserving economically valuable transactions.

Financial Leverage Is In Record High Territory

During the 2008–09 financial crisis, highly leveraged firms experienced a disproportionate share of bankruptcies.[8] In March 2013, banking regulators made clear their concerns that debt in excess of 6 times company earnings increased the risk of bankruptcy to unacceptably high levels.[9] Leverage declined during and in the immediate aftermath of the crisis, but it soon began rising to high levels again.[10]

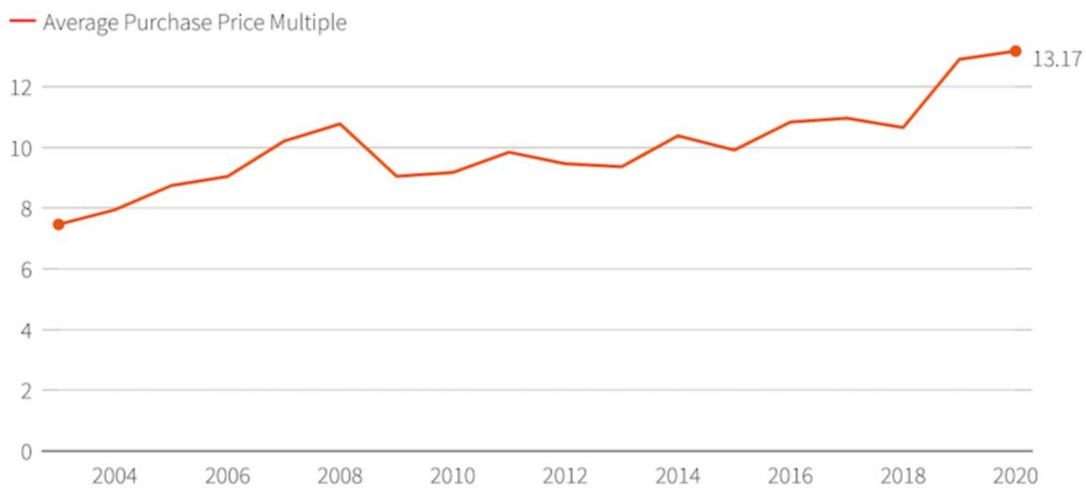
One of the drivers of the use of high levels of debt is the price that PE firms pay to acquire companies. The figure below shows the median price PE firms paid to buyout companies in each year expressed as a multiple of company earnings. These are average prices paid for large companies with sufficient assets to serve as collateral for leveraged loans. Half of the deals for these companies are priced above the median, and half are priced below. After hovering just under 10 times earnings for a few years, these multiples began rising in 2014. By 2020, they reached more than 13 times earnings.

In line with this increase in prices paid for companies acquired in PE buyouts, the leveraged lending market has grown rapidly. It reached $1.2 trillion in 2018, double its peak of $600 billion at the time

[8] Edith Hotchkiss, David C. Smith and Per J. Strӧmberg. 2012. "Private Equity and the Resolution of Financial Distress." Working Paper. www.law.uchicago.edu/files/files/Stromberg.pdf
[9] Board of Governors of the Federal Reserve Board, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency. 2013. "Interagency Guidance on Leveraged Lending." Washington, DC: Board of Governors of the Federal Reserve Board. https://www.federalreserve.gov/supervisionreg/srletters/sr1303a1.pdf
[10] PitchBook. 2019. "2018 Annual US PE Breakdown." Seattle, WA: PitchBook, p. 4. https://pitchbook.com/news/reports/2018-annual-us-pe-breakdown

of the financial crisis.[11] This year – through September 23 of 2021 – companies have issued $120 billion of leveraged loans to finance corporate buyouts by private equity firms. This is just under the record of $124 billion set in the first nine months of 2007.[12] Financial market regulators acknowledged concern about the growth of leveraged lending in 2019, but no actions have been taken to address the

U.S. leverage buyout multiples



Note: Average purchase price multiples for large corporates

Sources: Data from Refinitiv; graphic from Reuters

Source: Reuters (March 16, 2021)[13]

threat these loans pose to the economy if growth were to slow and the companies bought by private equity were to be unable to repay the loans.[14]

---

[11] PitchBook. 2019. "2018 Annual US PE Breakdown." Seattle, WA: PitchBook, p. 4. https://pitchbook.com/news/reports/2018-annual-us-pe-breakdown.

[12] Matt Wirz. 2021. "Corporate Buyout Loans Near Highs of 2007." Wall Street Journal, September 26. https://www.wsj.com/articles/corporate-buyout-loans-near-highs-of-2007-11632648602?st=06tt9z753ktmaut&reflink=article_email_share.

[13] Chibuike Oguh. 2021. "Analysis: private equity investors fret over record U.S. buyout prices." Reuters, March 16, https://www.reuters.com/article/us-private-equity-deals-valuations-analy-idUSKBN2B81EA

[14] Kristen Haunss. 2019. "Update 1 – Leveraged loan credit risk warrants attention, regulators testify," Loan Pricing Corporation, *Reuters*, May 15. https://www.reuters.com/article/levloan-risk/update-1-leveraged-loan-credit-risk-warrants-attention-regulators-testify-idUSL2N22R0XP; Jesse Hamilton. 2019. "Fed Challenged Over View that

Still, high leverage poses a threat to target companies, investors, creditors and workers, even if it doesn't yet threaten the financial system. The spate of bankruptcies, store closings, and even liquidations in what has been termed the 'retail apocalypse' makes it clear that a slowdown in the economy or a change in market dynamics threatens the viability of highly leveraged firms, financial crisis or not. To take a familiar example, private equity firms own only a fraction of U.S. retail chains, but they are behind a disproportionate share—nearly 63 percent between 2015 and 2019, according to one study[15]—of retail bankruptcies. In recent years, these include Toys 'R Us, Payless Shoes, Gymboree, Claire's Stores, PetSmart, Radio Shack, Staples, Sports Authority, Shopko, The Limited, Charlotte Russe, Rue 21, Nine West, Aeropostale and, more recently, J.Crew, Guitar Center, and Art Van Furniture.

PE funds also have major positions in other industries. Community newspapers across the country have seen local news and editorial offices closed. Alden and Chatham, the big players in the newspaper industry, own 104 daily newspapers with a total average daily circulation of about 4 million.[16] This is one-sixth of the daily circulation of 24.3 million. [17] Nursing homes are another industry in which PE firms have been active investors. The nation's second largest nursing home chain, HC Manor Care, went bankrupt while in private equity hands.[18] In one study of New Jersey nursing homes, private equity-owned nursing homes were responsible for a disproportionate share of COVID-19 deaths.[19]

By aligning the interests of Wall Street investment funds with those of the Main Street businesses that produce and distribute goods and services, your proposal reduces the risky use of financial leverage

Leveraged Loans Won't Cause Crisis," *Bloomberg*, May 15. https://www.bloomberg.com/news/articles/2019-05-15/fed-s-quarles-challenged-over-view-of-leveraged-lending-s-threat; Dean Baker. 2018. "Corporate Debt Scares," *CEPR*, October 11. http://cepr.net/blogs/beat-the-press/corporate-debt-scares.

[15] Americans for Financial Reform. 2020. "Double Exposure: Retail workers hammered by combo crisis of pandemic and private equity." December. https://ourfinancialsecurity.org/wp-content/uploads/2020/12/double-exposure-PE-retail-jobs-12-2020-1.pdf/

[16] Editor & Publisher Databook. 2021. https://www.editorandpublisher.com/databook/

[17] Pew Research Center. 2021. "Newspapers Fact Sheet." Pew, June 29. https://www.pewresearch.org/journalism/fact-sheet/newspapers/

[18] Tracy Rucinski. 2018. "HCR ManorCare files for bankruptcy with $7.1 billion in debt." Reuters, March 5, https://www.reuters.com/article/us-hcrmanorcare-bankruptcy-quality-care/hcr-manorcare-files-for-bankruptcy-with-7-1-billion-in-debt-idUSKBN1GH2BU.

[19] Americans for Financial Reform, 2020. "The Deadly Combination of Private Equity And Nursing Homes During A Pandemic." August 6. https://ourfinancialsecurity.org/2020/08/report-3-private-equity-nursing-homes-coronavirus/.

by private equity and other investment funds and brings the debt of target companies into line with their business requirements. Your proposal also restores risk-retention requirements from the Dodd-Frank Act on corporate debt, requiring securitizers to have skin in the game so that they don't make dangerous loans and immediately pass the risk on to unknowing investors.

Private Equity's Extraction of Wealth from Portfolio Companies Disadvantages Workers and Creditors

PE firms often recoup their own outlay on the acquisition of a target company by a PE fund it sponsors within the first few years of owning it by requiring payments from the company. Many PE firms sign agreements with target companies that require the companies to pay monitoring and transaction fees. In 2018, 58.0 percent of private equity firms required their portfolio companies to pay them monitoring fees; 85.8 percent required payment of transactions fees.[20] These payments deplete resources that the companies could use to make competitive investments in technology and workers' skills. The agreements lack transparency. Neither PE fund investors nor the company's creditors know how much the PE firm is collecting.

In addition to paying fees, the funds may require a portfolio company to take on more debt by issuing junk bonds and using the proceeds to pay a dividend to its private equity owners — a so-called dividend recapitalization. It is not unusual for PE owners to pay themselves a dividend in the first year or two after acquiring a company. In a dividend recapitalization so large that it shocked even seasoned PE observers (who are used to a world where PE firms routinely extract large sums from their portfolio companies), Sycamore Partners had Staples, a company it acquired in 2017, refinance its debt in April 2019 and pay its PE owners a $1 billion dividend. In combination with a payment it took in January 2019, in less than two years Sycamore has extracted more than 80 percent of the equity its PE fund originally contributed to the deal.[21]

20 PitchBook. 2018. "2018 Annual Global PE Deal Multiples." Seattle, WA: PitchBook, p. 3. https://files.pitchbook.com/website/files/pdf/PitchBook_2018_Annual_Global_PE_Deal_Multiples.pdf
[21] Eliza Ronalds-Hannon and David Scigliuzz*o*. 2019. ""Sycamore Pockets $1 Billion from Deal that Amazed Wall Street," *Bloomberg*, April 11. https://www.bloomberg.com/news/articles/2019-04-11/sycamore-pockets-1-billion-from-deal-that-amazed-wall-street

Sales of real estate or other portfolio company assets are another way private equity owners can extract wealth prior to a resale of the company. Proceeds of these sales repay any loans for which the asset was collateral. Typically, the asset sells for more than the loan, with the difference going to the portfolio company's PE owners. The portfolio company now has to lease the real estate (or other assets) that it previously owned, and is saddled with rent payments. This differs from the sale-leaseback transaction in which the company, not its shareholders, gets the proceeds from the sale and can use the funds to improve business operations. In September 2006, Sun Capital Partners acquired Marsh Supermarkets, with 116 groceries and 154 convenience stores, in a leveraged buyout. Soon after it acquired the chain, Sun did a sale-leaseback deal for the real estate of many of Marsh's stores, raising tens of millions of dollars for itself and its investors, and obligating the supermarket stores to pay rent on locations they had previously owned. Sun also sold Marsh's headquarters building and saddled the grocery company with a 20-year lease to 2026 at an annual rent of $2.8 million, scheduled to increase 7 percent five years later. In 2017, with just 44 stores remaining, Marsh went bankrupt.[22] While not all private equity sale-leaseback deals drive portfolio companies into bankruptcy, they do extract wealth and hollow out the companies, reducing their ability to make necessary investments to remain competitive.

In their quest for profits, private equity firms may also resort to outsourcing as an extreme cost-cutting measure. In May 2021, Hufcor, a longtime manufacturer in Janesville, Wisconsin, announced it would close its plant and move its jobs and operations to Mexico.[23] Hufcor had been acquired by private equity firm OpenGate less than four years prior.[24] Buying up companies, especially manufacturing businesses, only to move their operations offshore does even more damage than wiping out jobs and impoverishing communities. As the pandemic has made clear, global supply lines lack resiliency and can be disrupted by events, from serious recession to large-scale climate events. Losing the capacity to produce everything from computer monitors to Christmas toys weakens the economy.

---

[22] Rosemary Batt and Eileen Appelbaum. 2018. "Private Equity Pillage: Grocery Stores and Workers at Risk," *The American Prospect*, October 26. https://prospect.org/article/private-equity-pillage-grocery-stores-and-workers-risk

[23] Neil Johnson. 2021. "Hufcor to shutter its Janesville manufacturing plant." *The Gazette,* May 27. https://www.gazettextra.com/news/local/hufcor-to-shutter-its-janesville-manufacturing-plant/article_a2d0f99d-1505-59e4-9b6c-2f87ac1af102.html

[24] Shelley K. Mesch. 2017. "Janesville-based Hufcor bought by global private equity firm." *Wisconsin State Journal*, September 8, https://madison.com/wsj/business/janesville-based-hufcor-bought-by-global-private-equity-firm/article_cd9ca273-3a54-5541-b4b6-c3596fa2e60e.html.

Provisions of the Stop Wall Street Looting Act address the negative consequences of these transfers of resources from the portfolio company to its PE owners and protect the interests of the company and its workers both directly and indirectly. In addition to requiring PE firms to share liability for target firm obligations, your legislation confronts the most egregious looting by prohibiting dividend payments in the first two years post-acquisition, taxing private equity firms for the full value of the monitoring fees they charge, allowing creditors to claw back other transfers to the firm in bankruptcy, preventing new owners from quickly offshoring a company, and ending the tax code's favorable treatment of debt in highly leveraged companies. These steps to limit actions that strip value from target companies would force private equity firms to focus on what they claim to prioritize in the first place: making improvements to the target firm's business model to better position it for medium- and long-term growth, benefitting workers, customers, investors, and creditors in the process. The legislation would also end the federal policy that currently *encourages* companies to load up on risky, unsustainable levels of debt by allowing them to deduct interest on that debt from their taxes.

While a portfolio company's PE owners may not wish it to become bankrupt and most PE deals do not involve bankruptcy, the PE firms often have little or no skin in the game after collecting these dividends and fees. The costs of bankruptcy are borne by the portfolio company, its workers and its creditors. Many provisions of the Stop Wall Street Looting Act protect the interests of workers and creditors in bankruptcy, while also reducing the incentives for PE owners to drive companies into bankruptcy in the first place, such as by extending liability for the portfolio company's debt to the PE firm owners themselves. It would also ensure that workers receive legally required payments owed to them such as the 60 days' pay and benefits required by the WARN Act in the event of a plant closing or mass layoff by making the PE firm jointly liable for those obligations. Under current law, workers do not receive these benefits if the portfolio company cannot afford the payments. Similarly, it holds the PE firm jointly liable with the bankrupt portfolio company for any pension obligations and severance payments.

Letter, Eileen Appelbaum, CEPR
October 19, 2021

Performance of Private Equity Funds

Private equity firms contend that their freewheeling behavior results in returns that beat the stock market by a wide margin and help fund retirees' pensions. They caution against killing the goose that lays the golden eggs. In 2019, before the pandemic-fueled frenzy in private equity exits, analyses of PE fund returns by finance economists found that the median private equity fund's performance for funds launched in every year after 2006 just tracked the stock market.[25] The appropriate performance measure is the Public Market Equivalent (PME), and not the internal rate of return (IRR) that is widely used by PE industry participants. The PME provides the most accurate information on PE fund returns and is the measure that is most often used by finance professors in their research. The IRR has well-known flaws that make it easy to manipulate.[26]

A PME equal to 1 means that the return from investing in the buyout fund exactly matches the return from an equivalent investment in the stock market. A PME greater than 1 indicates that the return from investing in the PE fund was greater than the stock market return; a PME less than 1 means that the investor would have been better off in the stock market. A PME of 1.27, for example, means that the PE fund outperformed the stock market by 27% over the life of the fund. For a PE fund that lasts 10 years — the typical lifespan of PE funds — the cumulative outperformance implies an average

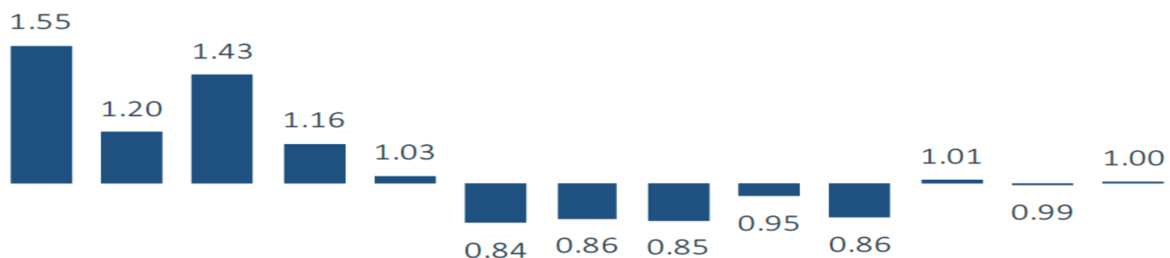
[25] Many of these studies are reviewed in Eileen Appelbaum and Rosemary Batt. 2018. "Are Lower Private Equity Returns the New Normal?" in Michael Wright et al. (editors), *The Routledge Companion to Management Buyouts*, Routledge. Important articles include: Robert S. Harris, Tim Jenkinson, and Steven N. Kaplan. 2015. "How Do Private Equity Investments Perform Compared to Public Equity?" *Journal of Investment Management.* Darden Business School Working Paper No. 2597259, June 15. Available at http://ssrn.com/abstract=2597259; Jean-Francois L'Her, Rossitsa Stoyanova, Kathryn Shaw, William Scott and Charissa Lai. 2016. "A Bottom-Up Approach to the Risk-Adjusted Performance of the Buyout Fund Market." Financial Analysis Journal, 73(4), July/August. https://www.cfainstitute.org/en/research/financial-analysts-journal/2016/a-bottom-up-approach-to-the-risk-adjusted-performance-of-the-buyout-fund-market; Ludovic Phalippou. 2020. "An Inconvenient Truth: Private Equity Returns and the Billionaire Factory." *Journal of Investing*, Volume 29, December. Available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3623820.

[26] A major problem with the IRR is that distributions from a PE fund to investors made early in the life of the fund raises the IRR but not the financial returns an investor receives. For example, the sale of a highly successful portfolio company early in the lifespan of a PE fund, which is typically 10 years, can raise the fund's IRR more than a sale of the same firm a few years later, even if would have brought a higher price if sold later. Similarly, dividend recapitalizations in the early years boost the fund's IRR even if this transfer of resources to the PE owners weakens the company and leads later to a lower resale price. A higher IRR does not always mean higher returns to pension funds and other investors.

annual outperformance just over 2.4%. A PME of 1.03 implies a cumulative outperformance of 3% over 10 years, or less than 0.3% a year.

The finding by finance economists that buyout funds beat the stock market before 2006, but since then, their performance has just matched that of the stock market means that the PME of buyout funds has hovered close to 1. We can see this in the figure below, which shows cumulative performance of the median fund launched in each year (its vintage year) from date of launch to the fourth quarter of 2016. [27]

PE KS-PME Benchmark by Vintage



PME calculated using Morningstar Small Growth Total Return Index
Source: PitchBook

2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013

When using a KS-PME, a value greater than 1.0 implies outperformance of the public index (net of all fees). For example, the current 1.03 value for 2005 vintage PE funds means investors in a typical vehicle from that year would be 3% better off having invested in PE than if they had invested in public equities over the same period.

Source and notes: Adapted from PitchBook (2019).

But, as we have seen, PE funds have gone on a selling spree, with funds of many vintages exiting companies in their portfolios at high rates and at high prices in the four quarters to the end of September 2021. This may have raised the median performance of some fund vintages, but it is too early to do an analysis. When all the data are in and finance professionals crunch the numbers, we may see some improvement in performance. Will it be sufficient to outperform the stock market by a

[27] PitchBook. 2017. *PE and VC Fund Performance*. Data through Q4 2016.

meaningful margin? Will it return a premium above the stock market returns sufficient to compensate for the risks involved in investing in private equity?[28] PE investors will surely welcome the windfall that 2021 provides. But questions will remain. How will this windfall affect the way private equity firms value the unsold companies still in their fund portfolios? This calculation is largely a subjective guesstimate by the PE firm, leaving investors and creditors with no opportunity to peer under the hood to see if the portfolio company is worth what the general partner says it is. PE firms are raising larger funds and raising them faster on the assumption that 2021 returns are the new normal after 15 years of substandard performance, and that their ability to do IPOs that value the companies at astounding multiples of earnings is more than a blip. How will investors interests be protected if this ability to exit investments at such high multiples turns out to be more hype than fact? Limited partner investors do not have access to information that will let them assess the likely future path and profitability of the funds they are investing in.

Your proposal is more necessary now than when it was first introduced two years ago. It prevents private equity funds from taking advantage of their asymmetric access to information in their negotiations with potential investors. This legislation will empower investors by increasing transparency around the true return of private equity investments so that investment professionals can make accurate assessments and comparisons across funds. The legislation includes new annual reporting requirements, which require private equity funds to make public information about the amount of debt held by portfolio companies and information about the fees charged and actual return on investment. It would also require marketing materials for new funds to include information about historic performance, past bankruptcies of portfolio companies, workers hired and laid off by those companies, and past exit strategies from portfolio companies, which will allow investors like pension funds to determine whether those investments are consistent with their values. Finally, the legislation will end the increasingly prominent practice among the private investment firms of forcing limited

[28] Risks specific to private equity include: *leverage risk* (potential for default and bankruptcy of portfolio company); *business risk* (some portfolio companies may face special risks as when Energy Future Holdings' PE investors bet on price of natural gas rising and instead it collapsed); *liquidity risk* (investments by LPs are typically for a 10-year period and cannot be withdrawn if economic conditions change); *commitment risk* (uncertain timing of capital calls and distributions means that LPs may face difficulties if capital is called on short notice or distributions they are counting on are delayed); *structural risk* (potential for misalignment of GP and LP interests as when GP collects monitoring fees from a portfolio company that later reduces resale price of the company).

partners to waive the fiduciary duties that require the investment firms to work in the best interest of their investors.

Conclusion

Companies owned by private funds touch millions of workers, tenants, students, patients, borrowers, consumers, and families all across the country — and their reach is growing. In their quest to make money, many private equity firms have employed exploitive practices that not only hobble their portfolio companies, but also hurt the people who rely on them. The Stop Wall Street Looting Act will, for the first time, create sensible rules for the private equity industry that will allow productive investment to continue while halting the kinds of abusive practices that wipe out jobs and cripple strong companies.

Sincerely,

Eileen Appelbaum, PhD
Co-Director and Senior Economist
appelbaum@CEPR.net
202-293-5380 x 116