DEBT CAPITAL ADVISORS, LLC

Manufacturing Value

When the business of the deal is the business

Summary

A leveraged buyout produces three numbers: the price paid for the company, the cost of financing it, and the value of the business itself. The first two are measured to the dollar and reported every quarter. The third is not measured by anyone who is paid to be at the closing. This article is about the third number.

For the sponsor, the deal is the business. Its product is the return, and it can be indifferent to whether the company makes semiconductors or manure. For the seller, the business is the price. Neither measure says whether the company came out stronger or who bore the burden. That is the question for everyone else: the company's workers, suppliers, and customers; the lenders who financed it; the households whose pensions supplied the money; and the owner deciding whether to sell to a sponsor at all. This article is written for them, and for the lawyers, trustees, and investment committees who act for them. They are not paid at the closing, and they live with its consequences.

Part One follows the returns. Take a company with $100 million of EBITDA sold for $1 billion. The seller leaves with $700 million, the old lenders with $300 million, the advisers with $25 million, and the company owes $500 million it did not owe the day before. The sponsor's return depends on paying that down and selling for more. The controls on what the company may do in the meantime shrink as deals grow. At the small end a bank sets quarterly covenants and takes personal guarantees. At the large end roughly 93 percent of institutional leveraged loans carry no maintenance covenants at all, and recoveries on them are about nine points lower when the borrower defaults.

The sponsor's own reporting shows where the money is. KKR's quarterly management fees now run at about four times the 2019 annual pace, because its fee-paying assets quadrupled over the same period, from $161 billion to $648 billion. The same company sold to a competitor, a management team, or its employees takes on different obligations and a different clock, and the clock decides what the owner invests in and when it sells. The sponsor's exit matters as much as its entry. A strategic sale ends the cycle. A secondary buyout restarts it with new lenders and new fees. An IPO transfers the remaining leverage to public shareholders. A continuation fund makes the sponsor both seller and buyer, and continuation-fund sales accounted for about 19 percent of sponsor exits in the first half of 2025. Bain counts 32,000 unsold portfolio companies worth $3.8 trillion.

The academic evidence is mixed. Buyouts raise productivity and churn jobs. The effects differ by deal type. Prices rise about one percent in consumer products. In nursing homes, residents of acquired facilities went to the emergency room and the hospital more often and cost Medicare more.

Part Two follows the cost when things go wrong. At Red Lobster, sale-leasebacks turned the company's real estate into $1.5 billion of day-one proceeds for the buyer and costly rent for the restaurants every month afterward. Toys "R" Us carried its 2005 buyout debt into the era of online retail, and the debt burden reduced its flexibility to respond. J.Crew moved its trademarks to a subsidiary outside its lenders' collateral and borrowed against them; the lenders sued, and most of their claims were barred by the credit agreement's no-action clause. In a small Long Island bankruptcy, the trustee and his law firm proposed to be paid while unsecured creditors received nothing, and the court refused. And the asset-based lending failures of 2025 and 2026, Tricolor among them, showed lenders the distance between a claimed lien and an actual recovery when the collateral itself is in dispute.

After the 2008 crisis the government collected hundreds of billions in corporate fines and convicted one senior banker. The institutions paid; the people who made the decisions largely did not. A buyout is built the same way. Gains are concentrated at the closing, losses are spread across years and parties, and when the failure comes the accounting asks who recovered what, almost never who was paid at the start.

Part Three is for the investor who can get the documents, and the fiduciary acting for the one who cannot. The household's savings finance these deals and its livelihood depends on the companies they produce. A pension fund supplies part of the equity; the pensioner, or a neighbor, works for or sells to or buys from the company that now carries the debt. The return is paid through the pension. The cost arrives as a layoff or a price increase. No one is positioned to connect the two.

The questions are concrete. Trace the debt to the entity that owes it and the asset that secures it. Test cash, not adjusted EBITDA. Read the documents for what the borrower may do before any default, because in most large loans no maintenance covenant will give early warning. Watch the trend line. Then ask who the lawyers represent. In a syndicated deal counsel is usually there for the borrower, the arranger, or the agent, and a legal opinion says only what a firm will certify under its own standards. Whether independent advice and capital remain available at all is a competition question. Mobility rules that let lawyers, accountants, and brokers move between firms keep the supply of advice open. The antitrust problem is the agreement among competitors and the roll-up that leaves no credible alternative.

The question has to be asked deal by deal: did the capital build something, or did it mainly price and re-price something built by others? The seller's proceeds answer who was paid at closing. They do not answer who ultimately pays.

Introduction

Two families bid on the same house. Their incomes are about the same, but one of them can borrow more, so that family offers more and gets the house. The larger mortgage won the bidding. It did not make the house any better, and it did not add a house to the street. When credit expands against a fixed supply, the extra purchasing power appears as a higher price and a larger debt. Research by Federal Reserve economists on the boom before the 2008 crisis found that looser mortgage credit was a major force behind rising house prices and household debt, and later work found the price effect was largest where new supply could not respond.[1][2]

Most people could not buy a house without a mortgage. But the price of the asset, the cost of financing it, and the value of the thing itself are three different numbers, and any serious account of leveraged buyouts has to keep them apart.

Private equity can bring capital, management, and discipline to a company, and it can fund an expansion or rescue a business that would otherwise fail. It also brings leverage, fees, rent, and a deadline. For the sponsor, the deal is the business. Its product is the return, and for all practical purposes it can be indifferent to whether the company it buys makes semiconductors or manure. For the seller, the business is the price. Those measures cover the first two numbers and leave the third unmeasured: whether the company came out more productive and more resilient, and who carried the burdens. That is the question for everyone else, and this article asks it in three parts: where the returns come from, who bears the cost when things go wrong, and what an individual investor can examine before the losses arrive.

PART ONE: Where the returns come from

The chain

A business starts with an idea and runs through design, sourcing, manufacturing, logistics, distribution, sale, and service. The value is created along that chain, by the people who design, make, ship, sell, and repair the product, and by the capital that pays for all of that before the revenue comes in. Financing can make any link work better. It can pay for a new production line, a better inventory system, or research that will not pay off for years.

Financing also creates claims on future cash. A company that borrows to fund its own acquisition must pay principal and interest. A company that sells its real estate and leases it back must pay rent and live with the lease. A company that transfers its brand or technology to another entity may need a license to keep using what its operations depend on. Those obligations become part of the cost structure, and they shape every decision down the chain.

The purchase math

Take a company with $100 million of annual EBITDA that is sold for an enterprise value of $1 billion, ten times EBITDA. Assume $300 million of existing debt, no excess cash, and a purchase agreement that requires the debt to be repaid at closing. The seller's equity value is $700 million: enterprise value less debt. Enterprise value is the value of the operating business before it is split between lenders and owners, and it differs from the cash the seller receives.

Add $25 million of transaction expenses. Uses at closing are $300 million to repay existing lenders, $700 million to the seller, and $25 million in fees, for a total of $1.025 billion. Sources might be $500 million of new acquisition debt and $525 million of sponsor equity. Real deals are more complicated. Cash, debt-like items, rollover equity, and financing terms all move the numbers, but the structure is the same.

At closing, the seller has $700 million, the old lenders have their $300 million, and the bankers, lawyers, accountants, and financing sources have been paid $25 million. The sponsor has put in $525 million. The post-closing company group carries $500 million of acquisition debt it did not owe the day before. The sponsor's return depends on operating performance, debt paydown, distributions, and the exit price. If the company grows and pays down the debt, the leverage multiplies the sponsor's gain. If it does not, the lenders are paid first and the equity absorbs the loss.

Asset sales can change the picture after closing. The company might sell the buildings it owns and lease them back, raising cash to repay debt, fund investment, or pay a distribution. It gives up the real estate and takes on rent. The same can be done with vehicles, equipment, receivables, or intellectual property. Any of these can make sense. All of them change what the company owes and how much flexibility it has in a downturn.

So the cost of private equity cannot be determined from the purchase price or the sponsor's eventual gain. It has to be traced through the operating company and its supply chain. Does the company grow by serving new customers, or does it lift earnings by raising prices, cutting labor, lowering material quality, deferring maintenance, squeezing suppliers, or narrowing service? If a cost reduction removes waste, customers and workers will never miss it. If it removes capacity, skilled labor, durability, or service, the margin improvement carries a deferred cost. Some PE-owned businesses are run better than they were before. The question is where the pressure fell.

Size and controls

The $1 billion example is a mid-sized deal. The market runs from a $2 million SBA-financed purchase of a local business to buyouts above $10 billion, and the controls that protect lenders and everyone behind them shrink as the deals get bigger. I have worked at both ends of that range, and the difference is not one of degree.

At the small end, a bank or an SBA lender sets maintenance covenants that the company must meet every quarter, limits what the owners can pay themselves, takes a lien on everything, and requires the owners' personal guarantees. The owner of that business reads every covenant, because each one is backed by his personal guarantee. A missed covenant gives the lender the right to act within weeks. At the large end, the same protections have mostly disappeared. Roughly 93 percent of the institutional leveraged loans issued in the United States in 2024 were covenant-lite, with no financial maintenance covenants at all, and about 92 percent of the loans in the U.S. leveraged loan index were covenant-lite as of March 2026. Without a maintenance test there is no recurring early-warning trigger, and the lender's remedies depend on the agreement's other covenants and events of default.[31] The cost appears in recoveries. A Bloomberg analysis of defaults from 2023 to mid-2025 put average recoveries on covenant-lite first-lien loans at about 57 percent, against 66 percent for loans with maintenance covenants.[34]

The documents in those deals let the borrower incur more debt, move assets to unrestricted subsidiaries, pay dividends, and adjust its reported EBITDA, all within baskets negotiated at closing and rarely read again until something goes wrong. The J.Crew litigation shows how much turns on documents of this kind, and the asset-based lending failures of 2025 and 2026 show how long the consequences can remain contested once a company is in distress.

Private credit was for years the exception, and lenders who held a loan to maturity insisted on at least a leverage covenant. That is changing as direct lenders compete for the largest borrowers. Estimates of the covenant-lite share of U.S. direct-lending deals in 2025 run from about 14 to about 21 percent, up from low single digits two years earlier, and the loosening is concentrated among the largest borrowers.[32] The capital, meanwhile, has concentrated in the deals with the fewest controls. Transactions above $1 billion accounted for about 77 percent of global buyout value in 2024 while making up a small share of the deal count.[33]

So the smallest borrowers, with the least sophisticated owners, face the tightest oversight, and the largest borrowers, with the most sophisticated sponsors, face the least. There are reasons for that. A large diversified company with public-style reporting may not need a quarterly covenant test, and a syndicate of several hundred holders cannot negotiate a waiver the way one bank can. But it means the deals large enough to affect a workforce, a supply chain, or a town are the ones in which no lender has an early right to intervene. No one receives a warning. Whoever wants to know what is happening has to read the documents, and most holders never do.

Who is paid at closing

A seller receives a premium, liquidity, and the freedom to pursue other ventures. Executives receive sale bonuses or roll equity into the new company. The sponsor earns a return if the company grows in value or pays distributions. Banks and private lenders earn interest and fees. Bankers, lawyers, accountants, consultants, and insurers are paid for the transaction. If real estate is sold and leased back, a property investor collects rent for the life of the lease.

These parties do not take the same risk, and none of them profits in every deal. The seller gives up control. The sponsor can lose its equity. Lenders can take losses. Most transaction fees are earned at or near closing, on terms set before anyone knows how the company will perform, though some advisers take part of their pay in contingent fees or equity. That timing is the asymmetry worth watching. The fees are fixed on a known date. The company's performance stays uncertain for years.

A second group lives with the result without an equal share of the upside: workers whose jobs or pay may change; suppliers asked to accept lower prices or slower payment; customers who may face higher prices or reduced service; unsecured creditors whose recovery depends on what is left; and the next buyer, who inherits the obligations. Where the business provides essential services, patients, families, and public payers absorb consequences that never appear in an investor's return.

Critics sometimes call this "legal theft." The phrase captures a suspicion that value created by other people is being collected through lawful contracts and financial structures. But it is an accusation, and it blurs distinctions that matter. A freely negotiated sale at a fair price is not theft. A fee, a dividend, an asset sale, or a restructuring is not improper on its face. The useful question is whether a transaction creates productive value, moves existing value from one party to another, or does both, and whether what is left can still invest, compete, and pay its debts.

What the sponsor adds

KKR's third-quarter 2026 results show what the sponsor measures. The firm's chief financial officer reported a second consecutive quarter of record results on its three headline metrics: fee-related earnings, total operating earnings, and adjusted net income per share, each up more than 20 percent per share from a year earlier. Management fees that totaled $1.2 billion for all of 2019 were $1.2 billion in the quarter, an annualized pace about four times the 2019 figure. The firm had returned $31 billion to its fund investors in the year to date and expected to exceed $40 billion for 2026. And it ended the quarter with $75 billion of assets under management not yet paying management fees, which it described as embedded growth and visibility into future earnings.[35]

The investors receiving the $31 billion include the pensions described in Part Three. But none of those measures is a measure of a portfolio company. The companies appear in those results only as assets under management, and fee-related earnings grow when the assets grow, whether or not the companies do. Fee-paying assets were $161 billion at the end of 2019 and $648 billion at September 30, 2026, almost exactly four times, and the annualized fee pace rose in proportion.[36] Those are KKR's figures. The observation they prompt is mine: the fees track the capital, not the companies. A manager's revenue grows with the capital it gathers, whatever happens at the companies that capital buys. KKR describes the $75 billion not yet paying fees as embedded growth because it expects much of it to become fee-paying over time. That is a measure of the manager's future revenue. What value the portfolio companies themselves created is a separate question, and the earnings release does not address it.

Private equity's strongest case has always been expertise rather than access to debt; companies can borrow from banks, private credit funds, the bond market, and asset-based lenders without a sponsor. And expertise is less scarce than it was. A management team can now use data, software, and independent advisers to compare financing, model outcomes, and understand what a contract says, and it can do most of that on its own. Capital and judgment still matter, but the sponsor can no longer assume it knows something the company cannot find out.

The test should be specific. Did the sponsor provide capital when no one else would? Did it help the company build a product, enter a market, fix working capital, repair a broken operating system, recruit a better team, or complete a difficult acquisition? Did the company grow more than it would have under another owner or another financing plan? What did the sponsor charge, what control did it take, and what risk did it leave behind?

The alternative to private equity is not always a patient founder with unlimited money. A company may need a succession plan, rescue financing, or a buyer willing to carry out a hard turnaround, and a sponsor may be the only available buyer. The point is to measure what the sponsor actually did against what else was available: direct financing, an employee or family succession, a strategic buyer, or no transaction at all.

Sales without a sponsor

Most private companies that change hands are not bought by a fund. They go to a competitor, a customer, a supplier, a management team, the next generation, or the employees. I have represented sellers and buyers in each of those, and the questions are the same. The economics are not.

A strategic buyer pays with its balance sheet and its shares. It may borrow to do so, and the target's assets and cash flows may support that borrowing, but the financing is carried within a larger operating business rather than centered on the acquired company alone. It buys because it intends to operate the business, usually for longer than a fund's life, and because it expects to combine it with something it already owns: a sales force, a plant, a distribution network, a product line. Where those combinations are real, the gains are operating gains. Where the buyer is also removing a competitor, the price it can pay includes the value of less competition, and that is where the antitrust questions in Part Three begin. Strategic buyers carry their own risks for the chain: redundant plants close, duplicate functions are eliminated, and the acquired company's suppliers may be dropped for the buyer's. But there is no fund-level fee, no carried interest, and no fund-imposed exit timetable, though a strategic buyer may later divest the business.

A management buyout or a family succession is financed differently. The buyers usually have little capital of their own, so they rely on a bank, a seller note, an earn-out, or an SBA-guaranteed loan, and the debt can be a larger share of the price than in a sponsor deal, depending on how the financing is structured. What they lack in capital they make up in knowledge of the business and in intent: they are buying a livelihood rather than an investment position. In small transactions the lender will ordinarily require the buyers' personal guarantees, which put their own assets behind the company's debt; SBA rules generally require guarantees from owners holding at least a 20 percent stake, and a lender may require them from others depending on the circumstances. In larger deals a personal guaranty would be unexpected unless it secures an equity commitment that has not yet been funded, the credit is weak enough that the lender is relying on the individual rather than the company, the equity cushion is thin, or the guaranty is limited to specific bad acts such as fraud or misapplication of collateral.

An employee stock ownership plan does something similar at the level of the whole workforce, with tax advantages and a trustee who owes duties to the employee-owners. These deals fail too, and I have litigated more than one seller note and earn-out. But the people who carry the operating risk are the same people who hold the equity, and no one is pricing the business for resale.

The same business, sold to a different buyer, takes on a different set of obligations and a different clock. A fund plans to sell after several years, depending on the fund's life and the market. Bain puts the average holding period at exit near seven years, and the funds themselves commonly run ten years or more.[28][12] A strategic buyer's clock runs as long as the combination makes sense. A family's or a management team's runs as long as they can service the debt and wish to keep working. The clock decides what the owner will invest in, what it will cut, and when it will sell.

Exits

A sponsor's return is unrealized until it sells, and the way it sells decides who inherits the company's obligations.

A sale to a strategic buyer is the largest exit channel. Bain's count of global buyout-backed exits in 2021, the peak year, put about $957 billion of exit value at roughly 48 percent to strategic buyers, 24 percent to other sponsors, and 12 percent through public offerings.[27] In 2024, IPOs were about 6 percent of exit value, and in 2025 sales to strategic buyers grew by about two-thirds year over year.[30][28] A strategic sale typically retires the acquisition debt out of the buyer's own resources. The chain gets a new owner with an operating purpose, and the questions become those of the preceding section.

A sale to another sponsor, the secondary buyout, keeps the company inside the model. The second fund pays the first fund's price, borrows against the same cash flows, and starts a new clock. The sellers' investors receive cash and the first sponsor earns its carried interest; the company receives a new set of lenders, new fees, and often more debt than it carried before. A company can pass through three or four sets of owners, each paid at closing, without ever being owned by anyone whose business is the business.

A public offering appears to be the cleanest exit and is usually the most partial. In an IPO the sponsor usually sells only part of its stake, the company issues new shares to repay some debt, and the sponsor sells the rest over the following years as lockups expire. The public shareholders buy the company with whatever leverage remains, and they buy it at a price set in a process the sponsor and its underwriters control. The disclosure is far better than in a private sale, but the public investor is the last buyer in the sequence and knows the least about what the earlier owners took out.

Two routes return cash without a sale at all. A dividend recapitalization has the company borrow more and pay the proceeds to the sponsor as a distribution. The sponsor recovers part or all of its equity and keeps the company; the company keeps the debt.

A continuation fund has the sponsor sell the company from an older fund to a new vehicle that the same sponsor manages, with the old fund's investors given the choice to cash out or roll over. The sponsor acts as both seller and buyer. Jefferies' secondary-market review for the first half of 2025 put continuation-fund exits at a record $41 billion, about 19 percent of all sponsor sales in the period.[29] In a 2025 ILPA and Bain poll of fund investors, who could choose more than one answer, 63 percent selected a conventional sale even at a price below recent marks and 17 percent selected a continuation vehicle.[30] Bain's 2026 report counts about 32,000 unsold portfolio companies worth roughly $3.8 trillion.[28] The model has grown faster than the markets expected to absorb its companies.

For the company and the people who depend on it, the exit matters as much as the entry. A strategic sale ends the cycle, a secondary buyout restarts it, an IPO hands the remaining leverage to shareholders who never negotiated it, a dividend recap adds debt without a change of hands, and a continuation fund extends the holding period while the sponsor is paid as both seller and buyer. Each should be read for what it leaves on the balance sheet and who was paid to arrange it.

The evidence

The research is mixed, and a claim to the contrary rests on a partial reading of it. A large study of U.S. buyouts from 1980 to 2005 found productivity gains at acquired firms alongside lower earnings per worker and heavy job churn; net employment effects were modest once new plants and acquisitions were counted.[3] A follow-up study covering deals through 2011 found the effects depend on the deal type: companies taken private from public markets shed jobs, while sponsor acquisitions of already-private companies added them.[4] Neither study covers sales without a sponsor. A study of consumer products found that acquired firms grew sales through new products and new geographies, raised prices on existing products by about one percent, and gained shelf space at the expense of competitors, who raised their own prices slightly.[5]

In health care the stakes are plainer and the findings are harder to dismiss. A study of 302 nursing homes acquired by private equity found increases in emergency visits, hospitalizations, and Medicare costs relative to other for-profit homes.[6] A systematic review of U.S. nursing home studies found associations with more deficiencies, hospitalizations, and mortality, while reporting some improvements in care processes and noting the limits of the underlying evidence.[7] Financial performance cannot be the only measure when the business is the care of elderly people.

PART TWO: Who bears the cost when things go wrong

Every return is paid by someone. This part follows the money after closing, through four deals, into distress, and to the question of who is held responsible when a company fails.

Four deals

Red Lobster shows how a sponsor can convert a company's assets into day-one proceeds. In 2014, Darden sold Red Lobster to Golden Gate Capital for about $2.1 billion. As part of the financing, the sponsor sold roughly 500 of the restaurant properties to a real estate investor for about $1.5 billion and leased them back on long-term leases.[8] The sale-leasebacks turned real estate the business had owned into $1.5 billion of cash at closing, which funded most of the purchase price. The cost came afterward. The restaurants that had operated rent-free in their own buildings now paid rent on all of them, every month, for the life of the leases, at a level set to give the property investor its return. Whether that burden contributed to Red Lobster's later bankruptcy is a separate question. The trade itself is plain: the proceeds were taken on day one, and the operating company paid for them for years.

Toys "R" Us shows how leverage interacts with an industry shift. A consortium took the retailer private in 2005 for about $6.6 billion, financed largely with debt. By its 2017 bankruptcy the company was carrying a heavy annual interest burden while competing with online and big-box retailers. Its own filing described both the debt service and the competition, and reported that operating changes had saved about $325 million.[9] The debt burden reduced the company's flexibility to reinvest, cut prices, or change its model as the market moved.

J.Crew shows how intellectual property can be moved within a capital structure. In December 2016 the company transferred a majority interest in its U.S. trademarks to an unrestricted subsidiary outside the reach of its term lenders' collateral. In July 2017 it used that intellectual property to secure new notes issued in exchange for $565.7 million of parent-level payment-in-kind notes, while the operating company kept the right to use its own brand under a license. The term lenders sued. The Appellate Division held that the credit agreement's no-action clause barred most of their claims and let certain breach-of-contract claims proceed.[10] The asset at the center of the company's identity was moved, and the value of every creditor's claim moved with it.

The question of who bears the cost also appears when a company fails. In All Island Truck Leasing, a small Chapter 11 case converted to Chapter 7, the trustee's final report proposed no distribution to unsecured creditors while seeking $46,424 for the trustee and $34,725 for his law firm, among other administrative claims. The bankruptcy court found that the assets had been administered without a reasonable likelihood of benefiting unsecured creditors, held the fee applications in abeyance, and found that the trustee had breached his fiduciary duty.[11] The case is small. It is here because it shows, on a small scale, that professional work, asset administration, and creditor recovery can diverge, and that a court sometimes has to ask whether the estate's expenses produced any benefit for the people who were left unpaid.

Distress

A performing loan is judged by yield, covenants, and expected repayment. In distress, the questions become collateral, priority, control rights, and the cost and timing of enforcement. The borrower may seek new money, a priming lien, a maturity extension, an asset sale, or a restructuring. Intercreditor agreements and voting provisions decide which creditors negotiate, which can object, and which are bound by a majority. Bankruptcy adds court-supervised financing, asset sales, administrative expenses, and professional fees ahead of any distribution. A security interest can be valid and still be contested, hard to enforce, or worth less than expected. The collateral may be held by another entity, behind a prior claim, outside the guarantees, or depleted by operating needs. A quoted price, a "senior secured" label, and a final recovery are three different things, and I have watched holders learn the third only after relying on the first two.

The asset-based lending failures of 2025 and 2026 are the current examples. In several of them, borrowers that had financed receivables and inventory through layered facilities failed within weeks of their lenders discovering that the collateral was not what the loan tapes and borrowing-base certificates described. Tricolor, a subprime auto lender and used-car retailer, filed for Chapter 7 in the Northern District of Texas on September 10, 2025, after its warehouse lenders found what they allege was double-pledging of the same loans to more than one lender; federal prosecutors and the SEC have since charged its founder and two executives, and the Chapter 7 trustee is liquidating what remains.[15] Lenders that held first-priority liens on receivables found themselves in litigation with other secured lenders over the same receivables. The record in these cases shows the distance between a claimed lien and an actual recovery, and why liquidity, financing layers, and collateral rights have to be examined before the losses arrive rather than after.

Accountability

Private equity is one part of a wider market that prices and reallocates businesses, and the question of who is held responsible for a failure is older than it. The 2008 financial crisis is the best-documented example. John Sturc's study of the enforcement record found that from 2008 to 2019 the federal government collected hundreds of billions of dollars in corporate fines, while few individuals were held to account and only one senior banker was convicted of a crime. Sturc stresses how hard it was to prove individual responsibility where decisions were diffuse.[26] There were consequences. But the institutions paid them, and the individuals who made the decisions largely did not.

The same divergence is built into a buyout. Gains are concentrated at a closing; losses are spread over years and across many parties. The seller can be paid, the sponsor can earn its return, lenders and advisers can collect their fees, and the company can fail, with no one in the first group accountable to anyone in the second. When the failure comes, the accounting asks what each class of creditor recovered and what the professionals were paid to manage the failure. It almost never asks who was paid at the start.

PART THREE: What an individual investor can examine

Most of the people who fund these deals never see the documents. This part is for the ones who can get them, and for the fiduciaries who act for the ones who cannot.

The household

The money that finances buyouts comes in part from the people who live with the results. A household participates in private equity through a public or private pension, an insurance policy, or a fund whose portfolio includes private equity. The SEC notes that people can be invested in private equity indirectly, through pensions or insurance, without ever buying a fund interest.[12] The same household may also depend on the portfolio company for a paycheck, a contract, a product, or a bond coupon.

So the household's savings finance the deal and its livelihood depends on the company. If the fund performs, the gain is paid through the pension. If the company cuts jobs, raises prices, thins its service, or defaults on its bonds, the cost arrives separately, and the person who bears it has no way to know it is the same deal. The pension or the insurer is several steps away from the portfolio company, and no one along the way is asked to connect them. The risk, the cost, and the benefit should be visible enough for the fiduciaries and the beneficiaries to judge, and most of the time they are not.

How the household can protect itself depends on the route. A pension beneficiary does not pick funds or negotiate credit documents. Oversight rests with plan fiduciaries, trustees, and investment committees. Department of Labor guidance tells fiduciaries weighing private equity in a defined-contribution plan to assess returns net of fees, diversification, manager capability, valuation, liquidity, complexity, and participant needs.[13] GAO has long identified limited liquidity and transparency as the central challenges for pension plans in these assets.[14]

For a family office or an individual investing directly in a private fund or private debt, the questions are immediate. What fees are charged at the fund level and again at the portfolio company? How much debt ranks ahead of the investment, and what secures it? What happens after a covenant breach or a missed payment? How are valuations set, how long is capital locked up, and what conflicts arise from affiliated advisers or transactions among funds? The SEC's investor guidance makes the same points: private equity funds are illiquid, disclose little, carry layered fees and conflicts, and hold capital for a long time.[12]

Questions for an investor

Protection starts with tracing the investment all the way through, from the household's account to the fund, to the portfolio company, to the debt and the assets that are supposed to support the return. What follows are the questions that matter once the trace reaches the company. They are the ones I ask.

Start with the borrower and the capital structure. What is the company's total funded debt, including debt at subsidiaries, asset-based facilities, receivables financing, leases, and guarantees? Which entities owe each obligation, which assets secure it, and where does the investment rank in a liquidation? A "first lien" label is where the review begins. The holder still has to identify the collateral, the obligors, the perfection steps, and the competing claims.

Test cash, not adjusted EBITDA. How much cash remains after interest, taxes, maintenance capital spending, working capital, and required amortization? Which addbacks are recurring costs described as one-time? What happens if revenue falls, customers pay slowly, inventory loses value, or refinancing rates rise? Ask for base, downside, and severe-downside cases and identify the assumptions that drive recovery in each.

Read the documents for flexibility and control. Provisions governing additional debt and liens, asset sales, restricted payments, transfers to unrestricted subsidiaries, EBITDA adjustments, incremental debt, collateral releases, portability, voting thresholds, and amendments decide what the borrower may do before any default, what holders can stop, and what information they receive in time to act. The J.Crew litigation turned on provisions of this kind. The question is never only whether a covenant exists.

Watch the trend line. Weakening cash conversion against stable reported EBITDA, growing reliance on factoring or short-term borrowing, repeated covenant amendments, rising addbacks, deferred maintenance, late financial statements, changes in auditors or senior finance staff, and maturity walls that depend on refinancing are each a signal. No one of them proves distress. Several together call for a new recovery analysis.

Counsel

All of those questions assume the investor can get independent advice. That assumption deserves its own scrutiny.

Ask who represents whom. Identify the client of every counsel and adviser, the scope of the engagement, who selected and pays them, and whether the investor has separate access to advice. In a syndicated facility, designated counsel may serve the borrower, the arrangers, the agent, or a lender group, as the engagement and the documents specify. That is ordinary practice, and it means an individual holder should not assume that anyone in the transaction is looking after its particular investment, because in a syndicated deal usually no one has been engaged to.

Legal opinions illustrate the point, and I have given many of them. The ABA describes an opinion as the opinion giver's professional judgment, prepared and read within customary practice, and surveys show that large firms run opinions through committees and firm-wide policies.[16][17] Those practices improve consistency and prevent careless opinions. They also make the institution's threshold decisive. A requested conclusion is either "opinionable" or it is not, and the firm decides which. If counsel declines to give the opinion, that tells the investor what counsel is prepared to certify under its own standards. A disputed reading of the documents, and the investor's concern, remain open.

The threshold is shaped by repeat business. A market can contain many sponsors and many law firms and still concentrate capital, mandates, and influence among a small set of repeat players. Industry reporting described private-market fundraising in 2023 as more concentrated, with investors favoring established managers and larger funds.[18] A sponsor, arranger, or lender that hires the same advisers deal after deal is a source of future work, and firms compete for the next assignment as well as this one. That shapes judgment without anyone telling anyone to reach a result. Firms debate these questions internally. But the advice the firm delivers reflects the institution's risk tolerance, its client relationships, and its view of what the market will accept, and over time shared precedents and shared model documents narrow what anyone treats as commercially available.

A deal closing, a legal opinion, or an interpretation accepted by the lead parties should not be mistaken for independent advice to every holder. Investors can ask who selected counsel, who the client is, what assumptions and qualifications limit the opinion, and whether a separate review of the documents is worth paying for.

Competition

Whether investors, companies, and workers keep access to independent alternatives is a competition question, and antitrust law exists to ask it.

The framework applies to the deals themselves. U.S. merger guidance treats workers as participants in buyer-side markets, so a merger can be challenged for reducing competition for labor as well as for customers. The agencies may examine a series of acquisitions collectively, which matters for roll-up strategies that remove rivals one small purchase at a time. The Justice Department and the FTC have warned that wage-fixing and no-poach agreements among competing employers can violate the antitrust laws.[19][20] The same tools can reach a transaction that concentrates buyers, lenders, service providers, or employers. The market and the harm have to be shown.

The framework also applies to the advisers, and here two problems that are usually conflated need to be distinguished. The first is an individual restraint: a covenant that limits where one professional may work next. The second is an agreement among competing firms not to recruit one another's people or to hold down pay. The first is a question of contract law and professional ethics. The second is cartel conduct.

Lawyers have a profession-specific rule for the first problem. New York's Rule 5.6 bars a law firm from restricting a lawyer's right to practice after leaving.[21] The rule protects the lawyer's autonomy and the client's freedom to choose counsel. It does not license the misuse of confidential information or the breach of valid partnership obligations, and it does not make lateral hiring suspect. A firm that recruits a rival's partners is competing for talent, and clients gain another choice.

Accountants have no categorical bar. In BDO Seidman, New York's Court of Appeals allowed an accounting firm to enforce a restrictive covenant only to the extent needed to protect client goodwill developed through the firm, and later cases apply the same fact-specific reasonableness test.[22] Financial advisers built their own framework: the Protocol for Broker Recruiting lets a departing representative at a signatory firm take limited client information and solicit those clients at the new firm, and FINRA reminds customers that where their assets go is their choice.[23] London draws the same line. UK courts enforce employment non-competes only where they are reasonable, the government has been weighing reform, and the Competition and Markets Authority treats employer no-poach agreements as cartel conduct.[24][25]

The lesson across all of these professions is the same. Mobility rules keep the supply of independent advice open. The antitrust problem is the agreement among competitors, the merger that removes meaningful rivals, and the serial acquisition that leaves clients, borrowers, or workers with no credible alternative. Enforcement is warranted when the evidence shows fewer credible bidders, cumulative removal of alternatives, coordinated hiring limits, or suppressed pay, and not when the theory rests on firm size or professional mobility alone. Inaction allows concentration to compound. Overbroad intervention blocks efficient combinations, rescue capital, and the movement of talent.

The measure of value

Manufacturing value should mean more than manufacturing a high exit price. The price of the asset, the cost of financing it, and the value of the thing itself are three different numbers. A higher sale price can reflect a better business. It can also reflect more available credit, higher leverage, market optimism, or assets and obligations rearranged among legal entities. The task is to separate improvement in the productive enterprise from an increase in the financial claims on its future.

That means looking at the whole life of the investment: the source and cost of capital, the operating plan, the fees and asset transactions, the treatment of workers, suppliers, and customers, the company's ability to invest and survive a downturn, and who absorbs the losses if it cannot. It also means crediting private equity where it supplies capital and skill that would otherwise be unavailable.

The seller may have received a fair price. The buyer may have made a sound investment. If the company's capacity, workforce, product, or resilience was weakened to produce the financial return, the cost was paid by people who signed nothing at closing. It appears as rent in a restaurant's budget, debt service in a manufacturer's cash flow, a higher price for a consumer, a smaller care team, a supplier's lower margin, or a future lender's weaker collateral.

When the business of the deal is the business, those are the numbers no one in the transaction is paid to watch. The central inquiry is therefore not whether private equity is good or bad in the abstract. It is whether, deal by deal and industry by industry, it creates new productive value or mainly captures and redistributes value created elsewhere in the chain. The seller's proceeds answer who was paid at closing. They do not answer who ultimately pays.

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