CLEARY GOTTLIEB

ALERT MEMORANDUM

Cooperation, Not a Cartel – Why Lender Co-op Agreements Should Generally Withstand Antitrust Scrutiny

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I. Executive Summary

In recent years, as distressed borrowers have used the covenant flexibility in loan documentation to engage in liability management exercises (“LMEs”), often to the detriment of some or all lenders, ad hoc groups of creditors have increasingly responded by entering into cooperation agreements (“Co-ops”). In general terms, Co-ops require participating lenders to cooperate with each other in trying to reach agreements with the borrower on the terms of a restructuring. Co-ops thereby help lenders protect themselves against aggressive actions by a borrower (and possibly other aggressive lenders) and ensure “fair” participation in a potential LME or restructuring. Co-ops also benefit borrowers by, among other things, reducing transaction costs compared to individual lender negotiations and protecting against divergent creditor factions in distressed situations.

Borrowers, however, have complained that Co-ops give lenders too much leverage in negotiations, making it difficult to pursue a “divide and conquer” strategy against creditor factions. Against that backdrop, Optimum Communications, Inc. (f/k/a Altice USA, Inc.) and CSC Holdings, LLC (together, “Optimum”) recently filed a lawsuit challenging a Co-op on antitrust grounds, arguing that lender parties to the Co-op (the “Co-op Lenders”) had formed “a classic illegal cartel” to lock Optimum out of the credit market and prevent Optimum from negotiating with individual lenders.

This client alert examines the claims raised by Optimum in its lawsuit and potential defenses.

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II. Optimum's Antitrust Claims

In its complaint, Optimum alleges a price fixing and group boycott conspiracy among the Co-op Lenders in violation of the Sherman Act, focusing on the following allegations:

— **Price Fixing Allegations** – According to the complaint, the Co-op Lenders sought to reduce the discount that Optimum could receive through negotiations with individual lenders by agreeing that a steering committee will negotiate with Optimum on behalf of the Co-op Lenders.

— **Group Boycott Allegations** – Optimum complains that the Co-op prohibits Optimum's lenders from transacting with Optimum without supermajority approval, preventing Optimum from conducting any substantive debt negotiations with the individual Co-op Lenders.

To remedy the alleged harms, the lawsuit seeks (1) treble damages, (2) attorneys' fees and (3) a declaration that the Co-op is unlawful and void.

III. Overview of Legal Standard

Courts evaluating claims brought under the Sherman Act consider whether (1) the conduct is per se illegal or (2) the plaintiff can show harm to overall competition under the default antitrust framework, the "Rule of Reason."

— **Per Se Illegality** – As the name suggests, when conduct is per se illegal, courts presume that the agreement harmed competition without a further inquiry into the harm caused by the specific facts of the case. For this reason, courts do not apply the per se rule unless (i) courts have "considerable experience" with the type of restraint and (ii) have found the conduct harms competition in all or nearly all cases.[1]

— **Rule of Reason** – The Rule of Reason is the presumptive standard that applies to alleged anti-competitive conduct. To survive a motion to dismiss, a complaint proceeding under the Rule of Reason must include plausible allegations of each of the following:

- a properly defined relevant market;
- anticompetitive conduct;
- net harm to overall competition; and
- antitrust injury to the plaintiff.

IV. Potential Defenses

Applying the relevant standards to the Optimum Co-op (based on publicly available information), the Co-op Lenders can raise the following defenses:

— **The Per Se Rule Does Not Apply**

- There is no per se violation because Co-ops have not been shown to be universally harmful. On the contrary, they encourage similarly situated lenders to work together and efficiently help restructure a company's indebtedness, which can promote the overall value of the company.
- Indeed, the same policy rationale underlying the bankruptcy system applies to Co-ops—i.e., similarly situated creditors can work together to protect against the problems posed by a limited asset pool.[2]

— **Optimum's Claims Fail Under the Rule of Reason**

- The "market" narrowly defined by Optimum implausibly ignores competition from other forms of credit, including the asset-backed loan that Optimum obtained after the Co-op Lenders entered into the Co-op. The alleged market also

[1] *Texaco Inc. v. Dagher*, 547 U.S. 1, 5 (2006) ("Per se liability is reserved for only those agreements that are so plainly anti-competitive that no elaborate study of the industry is needed to establish their illegality.").
[2] The Second Circuit has held that "[j]oint activity by creditors facing a debtor is commonly in the interests of all parties." *Sharon Steel Corp. v. Chase Manhattan Bank*, 691 F.2d 1039, 1052 (2d Cir. 1982) (observing that mutual forbearance by creditors "may be in the interests of both debtors and creditors in that it maximizes repayment and gives the debtor a chance of survival").

fails to account for the relative ease of entry and expansion in leveraged finance.

- Optimum's complaint ignores the substantial amount of capital available to Optimum from third parties who are not party to the Co-op. Although Optimum alleges that the Co-op Lenders comprise 88% of the "Leveraged-Finance Market", this ignores the size/credit needs of Optimum relative to the total available capital in the market.
- As a result, there is no plausible harm to Optimum, much less to competition, if the remaining available capital in the purported market significantly exceeds Optimum's financing needs.

— **Optimum Lacks Antitrust Injury**

- Lenders may be able to provide better lending/workout terms to a borrower when working together to maximize collateral, spread risk and protect a borrower's business as a going concern.
- Co-ops make it easier for borrowers to obtain important benefits, including the ability to garner support from the necessary majority of lenders that can provide waivers/amendments to provisions of the loan documents that would otherwise damage a borrower's ability to operate as a going concern.
- The Second Circuit has recognized that "collective activity reduces . . . the costs of borrowing."[3]

V. Key Takeaways

Optimum argues that the alleged group boycott and price fixing agreements are unlawful under the per se rule and, in the alternative, under the more defense-friendly Rule of Reason.

First, as a general matter, we believe that the Court should not find that Co-ops are per se illegal. Per se illegality only applies to conduct that has been demonstrated to harm competition in all or nearly all cases. Far from harming competition in nearly all cases, Co-ops can be beneficial to both borrowers and creditors. In addition, we are unaware of any evidence (market or otherwise) that demonstrates how Co-ops harm competition on any scale.

Moreover, borrowers benefit from the existence of Co-ops through easier access to credit. Borrowers that have introduced anti-Co-op clauses in their documents have generally failed to clear the market, which shows that lenders would pull back in the absence of the ability to enter into Co-ops or would demand more favorable terms for the same loan.

Co-ops are also effective at directly resolving complex intercreditor issues and reducing transaction costs by facilitating the collective action inherent in debt instruments. These Co-op features enable borrowers and lenders to consider more transaction structures, and reach more favorable deals, than would be possible if the borrower was negotiating with lenders individually. This is especially important in distressed situations, when a borrower may need concessions from its lenders. The group dynamic that forms among Co-op members can also benefit borrowers, as lenders who support a deal can often persuade other lenders in the Co-op group to take less aggressive positions.

The overall effect of any Co-op on competition is ultimately a function of the many benefits to borrowers against the possible harms from the collaboration, so the per se rule is not appropriate.

Second, while an application of the Rule of Reason is a fact-specific inquiry, in general, a borrower will face a very high bar challenging a Co-op under the Rule of Reason. Given the size and evolving nature of the credit markets, the Co-op Lenders can argue that the Co-op affects too small a share of leveraged finance to have meaningfully affected competition in the overall leveraged finance market. Moreover, Optimum's claims focus narrowly on leveraged finance, but the effects on competition become even less significant considering the broader universe of debt financing

[3] *Sharon Steel*, 691 F.2d at 1053.

available to borrowers besides leveraged finance. As discussed above, the Co-op Lenders will also be able to point to offsetting efficiency benefits and better loan terms.

Finally, the Optimum lawsuit appears, in part, to be a litigation tactic to give the company leverage in creditor discussions. It seems more likely that the parties will reach a deal on a restructuring before this lawsuit is fully litigated. A typical antitrust litigation can take years to be finally determined. For example, it can take eight months or more from the filing of the complaint for the court to reach a decision on a motion to dismiss. If an antitrust claim survives such a motion, the timeline for trial and a verdict, particularly in the Southern District of New York where Optimum sued, can be years after the complaint is filed. Given that timeline, if Optimum's lawsuit survives a motion to dismiss, Optimum and the Co-op Lenders may reach a deal on a restructuring prior to trial, leaving the antitrust questions raised by Optimum's lawsuit ultimately unresolved.

For more information on Co-ops and their implementation in your credit facilities, our team at Cleary Gottlieb is available to consult.

This alert is for informational purposes only and does not constitute legal advice.

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