“Stop Wall Street Looting Act” Would Empower Wall Street, Harm Main Street

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Washington policies are often misnamed. Recent legislative proposals labeled “infrastructure” concerned not roads or bridges, but social spending. But sometimes, a bill in Congress would do the exact opposite of what it is titled. Such is the case with the so-called “Stop Wall Street Looting Act,” a bill sponsored by Sen. Elizabeth Warren that is the subject of a Senate Banking Committee hearing this afternoon.

The bill would not touch Wall Street banks or any other big publicly traded companies. In fact, it would give them a competitive advantage. Instead, it would actually loot from—and shackle with regulatory leg irons—private equity funds that have helped rejuvenate numerous businesses on Main Street. The result would likely be devastating losses in jobs and investments for middle class Americans with pensions.

As described recently by Andy Puzder, former CEO of CKE Restaurants, in a *Wall Street Journal* op-ed, “Private-equity firms invest in businesses they see as undervalued or underperforming if they believe they can add value. … The *goal* is always growth and value creation.” A 2019 study by the U.S. Chamber of Commerce, of the economic consequences of Warren’s near identical-bill introduced in the last Congress, points out that private equity funds have provided both the seed capital and strategic plans to foster long-term growth at many of America’s best-know businesses, including Hilton Hotels, Dunkin’ Donuts, and LA Fitness

Pudzer describes how private equity investment was instrumental to CKE going private and rebuilding after the financial crisis 2008. Private equity, he writes, allowed CKE to “de-emphasize quarterly earnings and focus on building the business, something the public market often punishes.” In fact, Warren has criticized the focus of the public market on short-term quarterly earnings.

Yet, Warren’s bill would further enshrine public markets and quarterly earnings by putting private equity at a significant competitive disadvantage. Overriding the nearly two centuries of tradition of the general incorporation laws of U.S. states, Warren's bill would federalize corporate law to place liability for debt directly on private equity shareholders. As Norbert Michel, director of the Cato Institute's Center for Monetary and Financial Alternatives, has written, "These provisions effectively erase the notion of a corporation acting as a separate legal entity."

The bill also prohibits certain capital distributions, such as dividends, from firms that have received a private equity investment; sharply limits tax deductions for interest paid by these firms; and bans many fees private equity fund managers may receive. Again, none of these restrictions would apply to publicly traded companies, no matter how big they are.

In his written testimony for today's hearing, Heritage Foundation Senior Fellow David Burton calls Warren's bill "a major effort to apply the policies which have harmed the public market to the private market." Burton is referring to mandates from laws such as Sarbanes-Oxley and Dodd-Frank that have made it difficult for smaller companies to go public, and for middle class investors to build wealth with by investing in these companies in their early stages.

Burton also cites the threat of broad environmental, social, and governance (ESG) disclosure mandates being placed on private as well as public firms (see this paper by CEI's Richard Morrison on the many problems with ESG mandates). He adds that if these efforts to handcuff private companies are successful, "this will have serious adverse consequences for investors, workers and consumers."

One of the most harmful consequences would likely be more companies going bankrupt, as the bill would disincentivize rescue attempts by private equity funds. As Burton states:

[The bill] would erect a moat and high walls around failing companies so that it would become virtually impossible, and certainly economically unattractive, to take over failing companies and replace their management. While this may be attractive to corporate elites and their lobbyists, it is certainly not in the interests of shareholders, workers or consumers.

The U.S. Chamber study cited above found some devastatingly harmful consequences, including job losses ranging from 6.2 million to 26.3 million jobs across the U.S. and investor losses from $671 million to $3.36 billion per year (about half of which would be lost to pension fund retirees).