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Mergers and Acquisitions—2023

2022 was a tale of two halves for M&A. The beginning of the year was active, as robust dealmaking carried over from the record-breaking levels of 2021 to drive approximately $2.2 trillion worth of global deals through the first half of the year, compared to approximately $2.7 trillion worth of such deals announced over the same time period in the previous year. M&A activity slowed considerably after the first half of 2022, however, as significant dislocation in financing markets, an increasingly volatile stock market, declining share prices, concerns over inflation, rapidly increasing interest rates, war in Europe, supply chain disruption and the possibility of a global recession undermined business and consumer confidence and created hesitancy to agree to major transactions. The year ended with total deal volume of $3.6 trillion globally, down from $5.7 trillion in 2021 but in line with the $3.5 trillion of volume in 2020 as well as with the five-year average (excluding 2021), and in a sense was the inverse of 2020, which saw a precipitous decline in M&A activity in the first half at the outset of the Covid-19 pandemic, followed by a surge in the second half driven by massive liquidity and low interest rates. Transactions involving U.S. targets and acquirors continued to represent a substantial percentage of overall deal volume, with U.S. M&A totaling over $1.5 trillion (approximately 43% of global M&A volume) for the year, as compared to approximately $2.5 trillion (roughly 43% of global M&A volume) in 2021.

Notwithstanding lower overall activity, 2022 witnessed a number of megadeal announcements, including Elon Musk's $44 billion acquisition of Twitter, Broadcom's $61 billion acquisition of VMware, Adobe's $20 billion purchase of Figma, Prologis's $26 billion acquisition of Duke Realty, Microsoft's $68.7 billion acquisition of Activision Blizzard and Kroger's $24.6 billion purchase of Albertsons. The overall number of megadeals decreased, however, with only six $25 billion-plus deals and thirty $10 billion-plus deals announced in 2022, compared to 10 and 53, respectively, during 2021, likely reflecting greater reluctance to pursue large transactions in the current regulatory environment as well as valuation gaps between buyers and sellers and more challenging financing markets than in the previous year. A wide number of companies also announced separations, divestitures, carve-outs and spin-offs across industries over the course of the year, with over thirty $1 billion-plus divestitures and nearly forty spin-offs announced. In addition, both during the first half of 2022 and even during the second half of the year, companies faced unsolicited overtures and takeover bids, public and private, requiring advance preparation and tailored strategies in order to handle such acquisition interest effectively.

As we kick off the new year, we review below some of the key themes that drove M&A activity in 2022 and discuss expectations for 2023.

Technology Transactions

Following a pandemic-driven boom that accelerated years-long trends, the technology industry faced significant headwinds in 2022 as remote work, online shopping and other changes driven in part by the Covid-19 pandemic began to ease or reverse and ongoing interest rate hikes sapped the attractiveness of future growth relative to present earnings. Most notably, the IPO market for tech companies (and generally) ground to an almost complete halt, with the number of tech companies raising at least $1 billion in their IPOs falling from twelve in 2021 to zero in 2022 and major anticipated IPOs, such as those of Instacart and WeTransfer, shelved for the foreseeable future.

Consistent with trends in recent years, technology transactions continued to play a significant role in the M&A story in 2022, with tech deals responsible for approximately 20% and 32% of overall global deal volume and U.S. deal volume, respectively, and with four of the six transactions over $20 billion announced in 2022 being in technology-related sectors. In addition to Elon Musk's acquisition of Twitter, one of the most prominent M&A sagas in recent memory, significant tech transactions included large public company transactions, such as Microsoft's $68.7 billion acquisition of Activision Blizzard, Broadcom's $61 billion acquisition of VMware and Adobe's $20 billion acquisition of Figma, as well as a number of large private equity-backed deals, including the $16.5 billion acquisition of Citrix Systems by affiliates of Vista Equity Partners and Evergreen Coast Capital, Zendesk's $10.2 billion acquisition by a consortium led by Permira and Hellman & Friedman and Thoma Bravo's $10.7 billion acquisition of Anaplan and $8 billion acquisition of Coupa Software.

Technology M&A was not immune from the broader downturn in the technology space, however, and global tech M&A volume declined by approximately 36% year-over-year (from over $1.1 trillion in 2021 to approximately $720 billion in 2022), as dramatically reduced public and private tech valuations, diminished growth prospects, belt tightening in anticipation of a possible recession (including a number of layoff announcements in the tech sector) and intense regulatory and media focus dampened boardroom enthusiasm and contributed to reluctance to engage in acquisitions.

As volatility in valuations eventually declines, interest rates eventually settle and post-pandemic winners and losers become clearer, we expect that tech will continue to be an active area of M&A in 2023. Strategic acquirors that have thoughtfully managed their balance sheets and private equity funds that have ample dry powder may be eager to pursue tech (and other) targets that would have previously been out of reach at the much higher valuations many companies enjoyed in 2021. Further, the trends that support dealmaking—a desire to expand and diversify product offerings, drive growth, enhance efficiency, remain competitive and respond to innovation—remain just as present as ever. Technology will continue to revolutionize the market for products and threaten existing business models, which may create opportunities for M&A and other corporate transactions. For example, in early 2023, Microsoft announced a multi-year, multi-billion dollar investment (reported to total $10 billion) in OpenAI, the developer of pathbreaking artificial intelligence bot ChatGPT. The deal announcement included Microsoft's agreement to deploy OpenAI's models across its consumer and enterprise products and to introduce new categories of digital experiences built on OpenAI's technology. The Microsoft/OpenAI transaction illustrates the potential need for well-established tech leaders to look to bolt-on M&A as a source of product innovation and expansion.

At the same time, the environment for tech companies has only grown more complex, particularly with heightened regulatory, political and public scrutiny (evidenced by, for example, the FTC's announcement that it would be seeking to block Microsoft's acquisition of Activision Blizzard, the introduction of bipartisan legislation in the U.S. Senate and U.S. House of Representatives to ban Chinese-owned social media app TikTok from operating in the United States and widespread attention focused on the crypto industry following the November 2022 implosion of cryptocurrency exchange FTX). All of these developments contribute to a more challenging environment for tech transactions and underscore the importance of early and proactive planning, thorough diligence and collaboration with experienced advisors to identify creative legal and structural opportunities that will maximize the likelihood of successful outcomes.

Healthcare M&A

Although the pace of healthcare M&A was down in 2022, a steady stream of healthcare deals were signed over the course of the year as large pharmaceutical, health insurance and other industry participants turned to acquisitions to drive growth. As overall M&A slowed considerably in the latter half of the year in particular, healthcare remained a bright spot, with the announcements of two transactions over $15 billion (Johnson & Johnson's $16.6 billion acquisition of Abiomed and Amgen's $27.8 billion acquisition of Horizon Therapeutics) and an additional six deals over $3 billion. Pfizer was a major contributor to the level of healthcare M&A, announcing a number of deals, including its $11.6 acquisition of Biohaven Pharmaceuticals, $5.4 billion acquisition of Global Blood Therapeutics and $525 million acquisition of ReViral. Healthcare also overtook technology as the top industry for de-SPAC transactions in 2022, with healthcare targets constituting 24% of de-SPAC targets, while technology companies constituted 21% of de-SPAC targets.

Trends expected to support healthcare M&A in 2023 include (1) the looming patent cliff (in which approximately $230 billion worth of pharmaceutical revenue will lose patent protection before the end of the decade), (2) pharmaceutical and medical device companies with healthy balance sheets and capacity to take on new debt and (3) the continual drive to innovate, evidenced, for example, by forays by retailers and tech companies into the healthcare sector (including CVS Health's $8 billion purchase of Signify Health and Amazon's $3.9 billion acquisition of One Medical). At the same time, indications that regulators are focusing on the effects of healthcare deals, including a June 2022 workshop hosted by the FTC and the DOJ to explore new approaches to regulating pharmaceutical M&A, will put a premium on thoughtful transaction planning in this space.

Financial Institutions M&A

Financial institutions M&A slowed significantly in 2022 relative to the pace of activity in 2021, returning to average levels over the preceding decade. Toronto Dominion's $13.4 billion acquisition of First Horizon, announced in February 2022, was the banking sector's largest transaction by a wide margin and only a small number of other transactions exceeded $1 billion in deal value. Recessionary fears, lower stock valuations and concerns about a highly politicized regulatory environment combined to tamp down merger activity in the sector. This provided a sharp contrast to 2021, when a number of large bank deals were announced, including the Bank of Montreal's $16.3 billion acquisition of Bank of the West and U.S. Bancorp's $8 billion acquisition of MUFG Union Bank. A particularly notable 2022 transaction was TIAA's announcement that it would sell TIAA Bank to an investor group including private equity sponsors with deep experience investing in regulated financial institutions. A steady stream of sub-$500 million deals contributed to the number of deals that were announced in 2022, also declining meaningfully year-over-year but still matching historical averages.

While Fintech activity demonstrated some resilience, it too retreated in the second half of the year, reflecting the realignment of valuations after several years of rapid growth. M&A slowed, venture funding volumes declined and few IPOs were completed. Intercontinental Exchange Inc.'s $13 billion acquisition of Black Knight, Inc. led the field in transaction size. In parallel, digital assets and cryptocurrencies in particular experienced a difficult environment characterised by plummeting prices and the headline-grabbing collapses of major crypto exchanges/intermediaries, including Voyager Digital Holdings, Inc., Celsius Network, LLC, FTX Trading Ltd. and Genesis Global Holdco, LLC.

In the insurance sector, a similar pattern emerged, with overall volumes declining markedly from 2021. Berkshire Hathaway Inc.'s $11.6 billion acquisition of property and casualty reinsurance company Alleghany Corp. far eclipsed in size the few other insurance sector deals that exceeded $1 billion in value.

Cross-Border M&A

Although there was a lower volume of cross-border transactions in 2022 due to economic uncertainty and stock market volatility, such deals remained attractive to dealmakers. Cross-border deals constituted 32% ($1.1 trillion) of global M&A, broadly consistent with the average proportion over the previous ten years (35%). Transaction volume of acquisitions of U.S. companies by non-U.S. acquirors was $217 billion, representing 6% of 2022 global M&A volume and 19% of 2022 cross-border M&A volume. In 2022, Canadian, British, Australian, Singaporean and Japanese buyers accounted for 50% of the volume of cross-border acquisitions of U.S. targets, while acquirors from China, India and other emerging economies accounted for about 8% (up modestly from 2021, where acquirors from China, India and other emerging economies were responsible for approximately 3% of cross-border deal activity).

We expect that cross-border transactions involving U.S. targets will continue to offer compelling opportunities to foreign acquirors in 2023. Conversely, the high valuation of the U.S. dollar relative to the currencies of other major economies means that overseas companies will be especially attractive acquisition targets for U.S. acquirors, which is another trend that is expected to support cross-border deal activity. Parties evaluating cross-border deals will fare better if they are well-prepared for the cultural, political, regulatory and technical complexity inherent in cross-border deals by engaging early and proactively with advisors on these topics.

Private Equity Trends

While private equity M&A in 2022 fell well short of the activity levels of the previous year, PE players displayed ingenuity and adaptability in developing transaction structures to enable dealmaking in a challenging environment. One example was the October purchase by

Blackstone of a majority stake in Emerson Electric's Climate Technologies business in a transaction valuing Climate Technologies at $14 billion, which utilized a number of different financing structures (including $2.6 billion of financing from direct lenders and $2.2 billion of seller financing) as sources of funds. Another avenue PE buyers took in 2022 was to increase their equity commitments—up to and including executing all-equity deals, such as KKR's buyout of April Group—while waiting for better market conditions to refinance some of that equity with new debt. Finally, 2022 saw an impressive number of large PE buyouts, including the $16.5 billion buyout of Citrix Systems by affiliates of Vista Equity Partners and Evergreen Coast Capital, the $10.2 billion acquisition of Zendesk by a consortium led by Permira and Hellman & Friedman, Thoma Bravo's buyouts of Anaplan ($10.7 billion), Coupa Software ($8 billion) and SailPoint Technologies ($6.9 billion) and Blackstone's purchases of American Campus Communities ($12.8 billion) and PS Business Parks ($7.6 billion).

Looking ahead, we expect there will be opportunities for private equity to be an active area of M&A in 2023. PE firms continue to have large amounts of unspent capital available and ready to be deployed. Further, as interest rates rise, companies may seek to raise cash by selling off assets, and PE actors are likely to be in the mix of potential carve-out buyers as they seek to put available cash to work. At the same time, headwinds include availability constraints and significant additional costs associated with leveraged financing that have prevailed in recent months, concerns expressed by both the FTC and the DOJ about private equity's impact on competition, and a slowdown in PE fundraising resulting from investor pessimism in the midst of increasing interest rates, rising inflation and geopolitical instability. These headwinds may present new challenges for PE in the coming year, and should be carefully considered by participants in potential private equity transactions and their advisors.

Antitrust

In a year of relatively robust M&A activity, the U.S. antitrust agencies continued to aggressively investigate and challenge deals large and small, across all industries and sectors, focusing not only on harm from mergers involving competing firms, but also on transactions implicating other theories of harm, including vertical and conglomerate theories, potential and/or nascent competition and monopsony theories (particularly involving labor markets). The hostile enforcement environment was not unexpected, given the Biden administration's expressed desire for more muscular antitrust enforcement as well as strong pronouncements in 2021 from new leadership appointed at the FTC and the DOJ that the agencies would not hesitate to vigorously challenge deals they viewed as anticompetitive. What was not initially clear, however, was whether challenges based on innovative legal theories and more novel theories of harm in this new era of enforcement would be successful.

2022 demonstrated that transacting parties who choose to test nontraditional theories of harm by fighting litigation may ultimately prevail. High-profile litigation losses for the agencies in 2022 included the DOJ's loss in its action seeking to block Booz Allen's proposed acquisition of EverWatch Corp, the DOJ's loss in its civil action seeking to enjoin United States Sugar Corporation's acquisition of Imperial Sugar Company and the dismissal by the presiding administrative law judge of the FTC's antitrust charges in Illumina's acquisition of cancer detection test-maker Grail. Further, the agencies' "just say no" approach to remedy proposals made by merging parties was put to the test in 2022 with parties increasingly opting to "litigate the fix." One successful example of such a challenge was UnitedHealth Group/Change Healthcare, where, in response to regulatory concerns, UnitedHealth announced its intent to divest Change Healthcare's claims-editing business and, prior to the start of the antitrust trial, signed a definitive agreement to sell the business, which the district court accepted as a way to effectively restore competition over the DOJ's objection.

Parties have traditionally accounted for regulatory uncertainty through deal mechanics, including detailed regulatory commitments and reverse breakup fees. In a concerning trend, even negotiated efforts commitments—which are very common in M&A deals—are now being used by the agencies against transacting parties as evidence that the parties themselves had substantive concerns about antitrust risk, and there is increasing concern that merger agreement provisions will be used as a "road map" by the government. This development only underscores the importance of deliberate, advance antitrust analysis and planning—including not only substantive risk allocation but also optics and messaging—in consultation with advisors at the earliest possible stages of a potential transaction. For transactions that raise antitrust concerns, parties should be prepared to deal with the FTC's strong preference for divestitures in lieu of conduct remedies that require ongoing oversight to ensure compliance, as well as both agencies' strong preference for approving acquirors of the divestiture assets prior to closing rather than permitting divestiture acquirors to be identified by the parties and approved by the government after closing.

Antitrust policy at the agency level (including the adoption of new merger guidelines and informal and formal rulemaking such as the FTC's recently proposed controversial rulemaking that would ban most employee non-compete agreements), potential changes to the governing doctrinal framework (including as a result of changes to the antitrust laws through the courts and legislation) and developments in individual litigated challenges (including the outcome of the FTC's challenges to Microsoft's purchase of Activision Blizzard and to Meta Platform's purchase of virtual reality app company Within, among others) will continue to be important areas to watch in 2023. Further, significant increases in the funding allocations for the FTC and the DOJ enacted at the end of 2022 will provide the agencies with additional resources to conduct their investigations and enforcement actions. Transacting parties must carefully consider the possibility of regulatory concerns and have a clear understanding of what remedies they would be willing to offer as well as whether they are prepared to litigate—preferably with a self-imposed fix in place—if the agency's concerns cannot be resolved. Parties should anticipate potentially broader inquiries that may impose significant transaction costs and cause delays in closing timelines, and, in certain sectors such as technology, healthcare and banking, potentially more politicized challenges.

Foreign Investment Review

Regulatory scrutiny of foreign investments has increased in the United States and in jurisdictions around the world in recent years. In the United States, the Committee on Foreign Investment in the U.S. (CFIUS), an interagency committee of the federal government, reviews foreign investments in U.S. businesses and certain real estate transactions for national security implications.

In September 2022, President Biden issued an executive order regarding CFIUS review of potential national security risks associated with inbound foreign investment, representing the first time since CFIUS's establishment in 1975 that an administration provided formal guidance on specific risks that the Committee should take into account when reviewing a transaction. The Executive Order specifically instructs CFIUS to consider the following national security factors: the effect on the resilience of supply chains, potential harm to U.S. technological leadership in areas that impact U.S. national security, the cumulative effects of multiple transactions involving the same or related parties in the same industry or involving similar technologies, potential cybersecurity risks and commercial or other access to sensitive data of U.S. persons. One month later, the U.S. Department of the Treasury, which serves as Chair of CFIUS, for the first time released Enforcement and Penalty Guidelines that detail the process CFIUS will use to assess whether to impose (and the amount of) penalties, and set forth a list of aggravating and mitigating factors that will be considered.

The Executive Order and issuance of the Guidelines indicate that CFIUS will continue to closely scrutinize foreign investments in U.S. companies and businesses, and highlight the importance of thoughtfully analyzing U.S. political and regulatory implications early in the process to determine whether a transaction may attract CFIUS attention or be subject to CFIUS review. Further, governments around the world are expanding the scope of their review of foreign direct investment beyond the traditional national security focus, and are becoming more proactive in analyzing deals even where they do not fall within mandatory notification requirements. The expanding direct investment reviews in foreign jurisdictions may also extend the timeline to closing even when there are no substantive issues. Parties engaging in cross-border transactions with potential foreign investment risk therefore must carefully consider these developments in negotiating the appropriate allocation of risk and time frames, and be prepared to respond to possible (and prolonged) CFIUS and foreign direct investment scrutiny.

SPAC Trends

The special purpose acquisition company (SPAC) phenomenon boomed in 2020 and 2021, and largely busted in 2022. Both SPAC IPOs and de-SPAC M&A fell precipitously—just 85 SPAC IPOs priced in 2022 (with activity declining sharply as the year progressed, as just 16 SPAC IPOs priced during the last six months of 2022 compared to 69 in the first six months of 2022) compared to 613 in 2021, and 196 de-SPAC deals were announced over the course of 2022 compared to 289 in 2021. Further, the number of withdrawn SPAC deals surged in 2022, with a total of 65 de-SPAC M&A deals withdrawn compared to 18 deals withdrawn in 2021. The slower pace of SPAC activity reflected reduced investor interest due to weaker-than-expected performance of post-de-SPAC companies (including relative to projections), heightened regulatory and political scrutiny (illustrated by new proposed SEC rules and increased comments in the SEC review process) and longer time frames to complete transactions.

In March 2022, the SEC unveiled its long-awaited proposed rules governing SPACs. Among other significant changes, the new rules would impose additional disclosure obligations (including regarding SPAC sponsors, conflicts of interest and de-SPAC transactions) and new financial statement requirements (including with respect to financial projections) that, if implemented, would subject SPACs to disclosure requirements that more closely match those applicable in IPOs and make the SPAC process more lengthy, burdensome and complex. The SEC's final rules are expected to be released in early 2023, although the anticipation of the proposed rules and increased SEC scrutiny are among the factors that have contributed to the whiplash in SPAC market conditions over the last two years.

Notwithstanding the likelihood of significant regulatory change and continued scrutiny in 2023, the amount of SPAC dry powder available for acquisitions and the large number of SPACs seeking targets mean that SPACs will continue to be a feature of the M&A landscape in 2023, at least in the short to medium term as existing SPACs approach their deadlines to complete business combinations (or, if they are unable to find a target, decide whether to seek an extension or dissolve, as occurred in record numbers in late 2022 with 85 SPACs liquidating in December alone). After a two-year period in which de-SPAC transactions presented many private companies with a real third alternative to M&A and an IPO, de-SPAC transactions are now more likely to make sense in a more limited set of circumstances.

Delaware Developments

The most closely watched M&A development of 2022 in the Delaware courts (and perhaps the most closely watched M&A dispute of all time) was Elon Musk's attempt to walk away from his $44 billion purchase of Twitter. Musk sought to terminate the deal by alleging, among other things, that Twitter's spam accounts exceeded the number that Twitter had publicly disclosed, which he claimed constituted a material adverse effect (MAE) that should excuse his performance under the merger agreement. Twitter filed suit in the Delaware Court of Chancery seeking to force Musk to close the deal, and following three months of high-profile discovery and pre-trial proceedings, Musk relented and the parties consummated the transaction on the originally agreed terms at the end of October 2022. Following this case and other disputes generated by pandemic-related dislocation, it remains the case that buyers seeking to establish an MAE as a basis for terminating a transaction generally must satisfy a very high bar, consistent with the prevailing philosophy in Delaware that the agreements of transacting parties generally should be respected and enforced. The Musk/Twitter saga also was a powerful reaffirmation of market expectations that the Delaware courts will enforce merger agreements in accordance with their terms.

Acquisition Financing

2022 brought a halt to a nearly unabated 12-year run of booming credit markets and record-low interest rates. Rampant inflation and fears of a recession on the horizon, among other factors, led to a marked contraction in credit availability and a slowdown in dealmaking across sectors and credit profiles. U.S. high-yield bond issuances were down approximately three quarters year-over-year—the lowest volume since 2008—while newly minted leveraged loans fell nearly two-thirds from 2021 levels. Investment-grade bond issuances fared better, but were still down significantly, with new issuances falling roughly 20% year-over-year. By year end, the average interest rate for single-B bonds had risen to 9.2%, up from under 4.7% at the beginning of January, while the average interest rate for BBB bonds more than doubled, from 2.7% to 5.8% over the same period.

Meanwhile, antitrust regulators' aggressive attitudes (described above) led to less predictable (and much longer) timelines between signing and closing of acquisitions. These two factors—a volatile and falling credit market, and the need for longer-duration acquisition financing commitments—had a compounding effect, squeezing availability for commitments of the requisite duration, and making those that were available more expensive.

In the face of these dynamics, debt-fueled M&A activity suffered, as described above. But some M&A acquirors—even those unwilling to pay the higher rates of the day—found creative ways to pursue new deals, including by turning to direct lenders for acquisition financing (who reportedly participated in the financing for six of the year's ten largest announced LBOs), accepting seller financing (as in Rev's and Searchlight's pending purchase of Global Payments' Netspend consumer business), funding their transaction with larger or more creative equity financing solutions (as in VillageMD's $8.9 billion acquisition of Summit Health) and carefully structuring deals to allow targets' existing debt to stay in place post-transaction.

2023, more than any year in recent memory, brings a unique slate of challenges and considerations for players in the acquisition financing markets, and corporate borrowers and sponsors will need to plan rigorously and be creative and flexible in order to thrive in this dynamic and challenging environment.

Tax Developments

The Inflation Reduction Act of 2022, enacted in August 2022, introduced two new taxes effective for tax years beginning after December 31, 2022: (1) a 1% excise tax on repurchases of stock of publicly traded corporations and (2) a 15% corporate alternative minimum tax (CAMT) on the financial statement income of certain large corporations. The 1% excise tax applies to a wide range of transactions well beyond conventional stock buyback programs. For example, under recently issued IRS guidance, the excise tax would apply in all-cash acquisitions to the extent the consideration is paid with cash (including borrowing proceeds) of the public target and would apply in "reorganizations" with respect to consideration received by the public target's shareholders, other than acquiror stock or securities that can be received on a tax-free basis. By introducing a parallel set of tax rules, the CAMT adds significant complexity to U.S. corporate taxation, including in the M&A context. Parties engaging with publicly traded U.S. target corporations will need to carefully consider the potential application of the excise tax, and potential acquirors of U.S. target businesses should carefully model the anticipated tax rate of the combined business, taking into account the potential application of the CAMT.

Activism and M&A

M&A-driven campaigns continued to make up a significant portion of overall activism activity in 2022. "Sell the company" campaigns were a key driver, reflecting an increasing push by activists for companies to explore or pursue transformative M&A as an alternative to perceived "stalled" or "failed" standalone strategies, and activists also commonly pushed for break-ups or divestitures in portfolio-based campaigns. In addition, some activists launched (often unsuccessful) campaigns after a transaction was announced to scuttle or sweeten an announced deal. One notable M&A-focused activism campaign was Light Street Capital's unsolicited recapitalization proposal to Zendesk following Zendesk's announcement that it had reached an agreement to be acquired by a consortium of investors, with Zendesk succeeding in convincing shareholders—and ISS—to support the transaction recommended by the board of directors. Companies and boards across industry sectors were targeted with calls for strategic, business and portfolio reviews and also faced campaigns focused on capital allocation, margin expansion, operational changes and governance reform, including by headline activist funds like Elliott Management, JANA Partners, Carl Icahn, Sachem Head, Starboard Value, ValueAct Capital, Inclusive Capital Partners, D.E. Shaw, Third Point, Trian Partners, Corvex and newcomers such as Voss Capital, among others.

On the regulatory front, potential SEC rulemaking announced in 2022 may impact the activism landscape in the years to come, depending on how the final rules shake out. The SEC's proposed amendments to Regulation 13D-G and a related new proposed rule reaching derivatives were two of the most significant activism-related legal developments of 2022. The proposed rules would modernize the beneficial ownership reporting rules by, among other things, shortening the Schedule 13D filing deadline from ten days to five days, setting an amendment deadline of one business day after a material change, shortening the Schedule 13G filing deadlines, providing that holders of certain cash-settled derivative securities will be deemed beneficial owners of the reference equity securities and requiring expanded disclosure of activity in derivatives. The proposed amendments, which are expected to be finalized early in 2023, would represent the most significant reforms to beneficial ownership reporting requirements since the rules were adopted in 1968 and reflect the SEC's ongoing efforts to enhance transparency to investors and strike a balance among the interests of issuers and other market participants. It also remains to be seen whether proposed rules regarding disclosure of derivatives positions, which were actively opposed by certain major activist hedge funds, will reach the final rulemaking stage.

In addition, the SEC's universal proxy card rules, which would change the legal framework for director election proxy contests by mandating that the company and dissidents use and send to shareholders proxy cards listing the names of all director candidates, regardless of whether the candidates were nominated by the board or by a dissident shareholder, took effect on September 1, 2022. While activism activity had already been increasing, the universal proxy card rules are expected to increase scrutiny (by both shareholders and proxy advisory firms) of individual directors and their roles on boards, alongside an activist's broader economic critique. The upcoming 2023 proxy season will be the first in which use of universal proxy cards is mandatory, and we will begin to see whether and how the new rules impact the success rate for activists who launch campaigns for board seats, as well as the likelihood of lesser known or newer activists (or ESG activists) launching minority slate campaigns "on the cheap" using universal proxy cards. Perhaps the biggest change seen so far is how the proxy advisory firms are now approaching "building a board" across the slates offered by an incumbent board and a dissident running a competing director slate on the universal proxy card.

Looking to the year ahead, we expect that activism activity will continue to be robust and that M&A will continue to be a common campaign thesis for activists, and that the effect of recent SEC developments on activists' behavior and decisionmaking will become clearer. As activists continue to seek board representation (whether via proxy fights or settlements), the coming year will reveal whether the universal proxy card rules have an appreciable impact on activists' inclination to nominate candidates and ability to win proxy contests or result in the typical proponents of Rule 14a-8 shareholder proposals choosing to run director candidates instead to advance their underlying agendas. And as companies and activists acclimate to the new proxy season dynamics over the next few years, another trend to watch will be whether activists who score one or two board seats are, in turn, successful in driving further M&A activity.

ESG

Environmental, social and governance (ESG) issues became more politicized in the United States in 2022 as some politicians and regulators, largely at the state level and divided along party lines, publicly staked out positions on the extent to which ESG should (or should not) affect corporate strategy or otherwise be considered by companies, asset managers and pension funds. Notwithstanding this apparent domestic ESG political backlash in some circles, ESG considerations have remained top strategic and operational priorities that have increasingly influenced the M&A landscape. Senior executives and corporate boards have leveraged M&A to advance ESG strategies and are integrating ESG considerations into due diligence and post-transaction integration processes to generate synergies, advance long-term value creation and reduce risk. Recent examples of transactions in which ESG considerations helped to drive the rationale for M&A include RWE's $6.8 billion purchase of Con Edison's clean energy business, Infrastructure Investment Fund's $8.1 billion acquisition of South Jersey Industries, SSE's $1.8 billion sale of a minority stake in its electricity transmission network to the Ontario Teachers' Pension Plan Board, Alphabet's $5.4 billion acquisition of cybersecurity firm Mandiant, BP's $4.1 billion acquisition of bioenergy firm Archaea and Chevron's $3.1 billion acquisition of Renewable Energy Group.

The influence of ESG considerations on M&A is likely to accelerate as shareholders and regulators continue to exert pressure on companies to make strategic and operational changes to address ESG risks and opportunities, in addition to enhancing board and management oversight of such matters. Notably, in the United States, new SEC rules on climate disclosures, human capital, cybersecurity and board diversity, all of which are expected to be released and/or finalized in the first half of 2023, will increase pressure on issuers to provide accurate and timely disclosures and will incentivize acquirors and targets to carefully diligence these areas to identify potential risks and vulnerabilities. ESG considerations also continue to play a role in post-transaction integration processes, particularly as corporate governance and culture, human capital management and diversity, equity and inclusion remain core investor and stakeholder concerns. Finally, we expect to see activists continue to draw on ESG critiques to strengthen their cases for change, particularly in instances where ESG-related missteps have drawn public attention, drove business crises, or led to internal or external stakeholder divisions. More broadly, it remains critical for boards and management to consider ESG factors and risks (along with all other material and relevant factors and risks) in their decisionmaking processes in order to ensure sustainable value for the company over the long term.

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As 2023 begins, there are reasons to expect that some of the major headwinds that battered M&A activity in the second half of 2022 may soon start to relent. The financing markets are not quite as hermetically sealed as they were in recent months, inflation shows pockets of easing, the impact of energy prices in Europe may not be as severe as initially feared, there is a possibility of a shallow or even no recession in the United States and many observers anticipate that the performance of the equity markets in 2023 will, at the least, be less punishing than in 2022. Nonetheless, the global economy is not out of the woods, and the risks that have depressed M&A activity in recent months are far from fully subsiding. It is difficult to predict how these trends and new developments in economic, financial, regulatory and political conditions will impact M&A in the coming year. In navigating the uncertainty, participants and their advisors should carefully analyze the risks and benefits of potential transactions, anticipate takeover threats and opportunities, proactively address changing shareholder dynamics and emerging regulatory, legislative and other risks, remain flexible and creative in transaction structuring and seek creative solutions to execute on M&A opportunities that are strategically and financially compelling.

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