Baker McKenzie.

Tech Mergers & Acquisitions

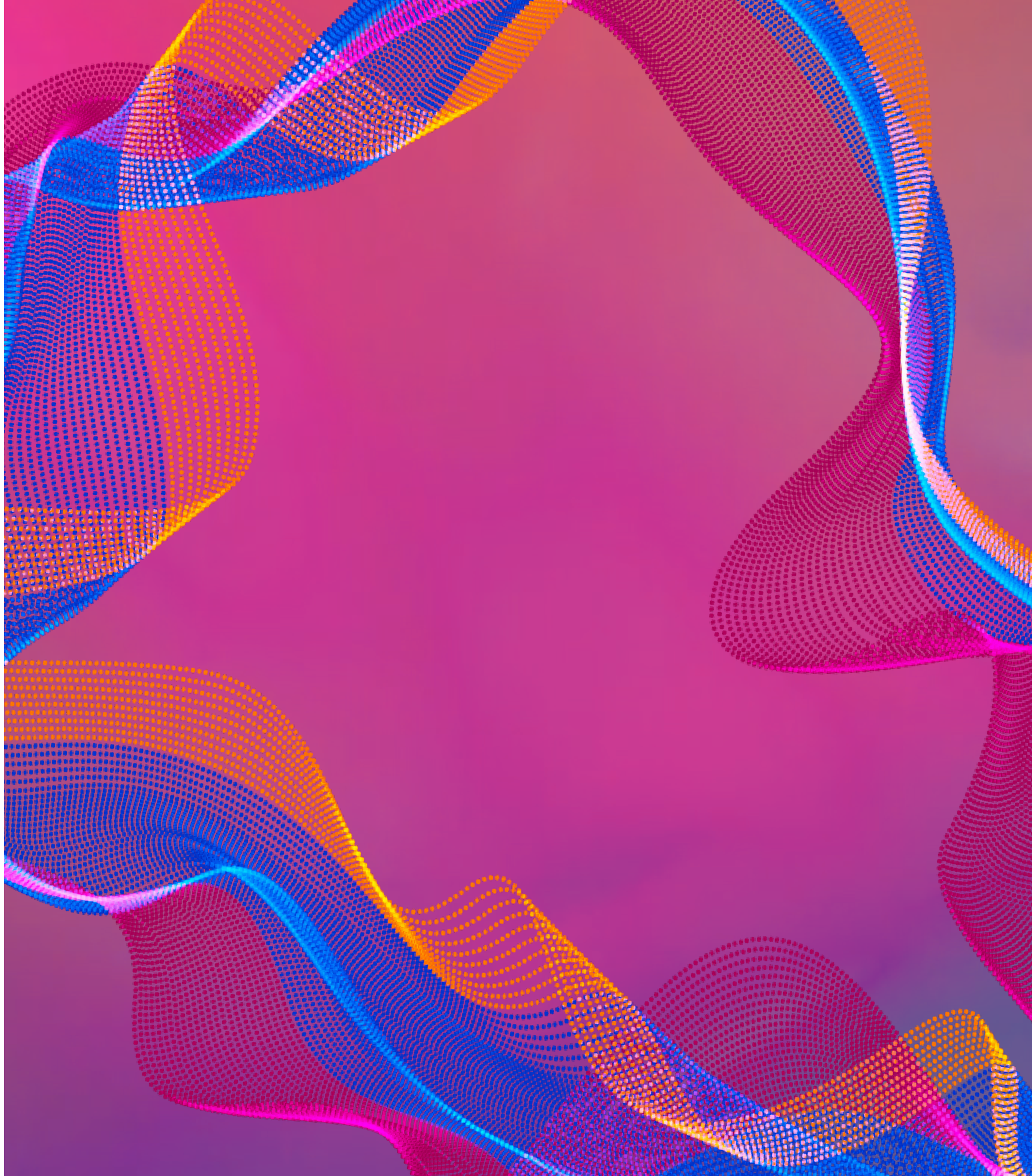
Report 2

TRANSACTIONAL POWERHOUSE

Leading and closing complex deals – every day

TMT Looking Ahead 2022

Contents



Foreword

Technology deals continue to drive global transactions, as evidenced by the growing number and volume of technology, media, and telecommunications (TMT) mergers & acquisitions (M&A) in recent years. This upwards trajectory is expected to continue, albeit in a more complex regulatory environment.

As businesses look to deepen their engagement and investment in the tech space, they should be prepared to understand the opportunities, impacts, and hurdles of emerging M&A trends, IP acquisition as a driver of M&A, the shifting tax landscape, developments in Special Purpose Acquisition Company (SPAC) trajectories, and new Foreign Investment Review (FIR) regimes, keeping in mind that:

Digital transformation remains core to almost all organizations' growth plans as they seek to remain competitive and drive deals to acquire technology and/or talent.

Technologies driving tech M&A include **5G and Internet of Things (IoT) connectivity technology, and artificial intelligence (AI)**. M&A transactions in AI will have to navigate challenges included in current and future IP and privacy laws.

Continued focus on tech transactions by **antitrust and national security** regulators means dealmakers will need to strategize to mitigate regulatory issues or risks.

Upcoming **changes to the international tax landscape** will add important new obligations necessitating additional tax due diligence in transactions.

Raffaele Giarda
Partner, Rome

This report, the second in a five-part series, explores the following key areas:

- What to expect for the M&A landscape in **Section 1**.
- An increasing need to protect and commercially exploit the valuable IP being acquired in tech deals in **Section 2**.
- How the shifting tax landscape will affect due diligence, deal structures and post-acquisition integration planning in **Section 3**.
- SPAC and de-SPAC transaction trajectory nuances across the globe and the impact of regulatory headwinds in **Section 4**.
- Mitigating risks in relation to FIR regimes, particularly for foreign investment in key tech areas in **Section 5**.

1 Tech M&A — What to Expect in 2022 and Beyond

*Authored by **Sze Shing Tan**, Principal, Singapore and **Will Holder**, Partner, London*

The technology sector dominated M&A in 2021, setting records in deal value and volume. Technology M&A in 2021 increased by 71% from 2020 levels, with dealmaking totalling USD 1.1 trillion and accounting for 20% of all global M&A deal value. Deal volume also soared, increasing 34% compared to the previous year's numbers[1]. The expectation is that tech M&A will continue on an upwards trajectory in 2022.

Digital transformation will continue to drive M&A

Digital transformation programs continue to evolve as businesses adapt to the COVID-19 pandemic and position themselves to remain competitive. Companies will look towards acquisitions and investments in tech-enabled assets to pursue their digital transformation strategies. More than two-thirds of respondents to **Baker McKenzie's 2021/2022 Digital Transformation & Cloud Survey** indicated they acquired at least some of their technology needed for digital transformation in 2021. That is expected to intensify in 2022. Despite lofty valuations, buying the necessary talent or technology to enable digital transformation shows no signs of slowing down, as business leaders will continue to search for deals that position them to scale their existing offerings and drive innovation.

Private equity firms will remain key investors in technology companies

Global Private Equity (PE) M&A activity reached record levels in 2021, accounting for 27% of all global M&A value and 9% in volume, with 470 PE investments worth a combined USD 225.7 billion in the technology sector[2]. This level of activity will continue, with PE firms expected to increase investment in technology companies or in acquiring divested technological non-core assets. PE firms have a robust amount of available capacity and are taking advantage of the opportunities posed by organizations' quick adoption of technology to actively become more competitive — they will continue to seize these opportunities in 2022. Further, the enhanced focus by antitrust regulators on tech M&A paves the way for greater opportunities for investment by PE companies, including co-investing alongside strategic players where that is part of the antitrust solution.

Tech M&A will continue to be subject to changing regulatory hurdles

Across the globe, dealmakers active in the TMT sector will face scrutiny from regulators targeting anticompetitive deals and transactions considered to pose a threat to national security. In the United States (US), the Federal Trade Commission and Department of Justice Antitrust Division's recently announced intention to overhaul their merger review processes will impact deals in the technology sector. In the United Kingdom (UK), the Competition and Markets Authority's regulation of big technology M&A is expected to have an impact on tech mergers and acquisitions. On the national security front, continued scrutiny is expected by the Committee on Foreign Investment in the United States (CFIUS) on transactions involving "critical technologies." Additionally, the UK recently passed the National Security and Investment Act, which establishes a national security regime (similar to CFIUS) that will likely also have in its crosshairs technology deals that threaten national security.

[1] *Deal data taken from Refinitiv's Global Mergers & Acquisitions Review for Full Year 2021.*
[2] *Data taken from Dealogic's M&A Highlight: Full Year 2021 article.*

2 IP Acquisition as a Driver for Tech M&A — Be Mindful of Data and Cybersecurity Risks

*Authored by **Adam Aft**, Partner, Chicago & **Isabella Liu**, Partner, Hong Kong*

Digital transformation and the expanded scope and distribution of technology have transformed the M&A landscape and opened new doors for ever-increasing investments. Intellectual Property (IP), and the ability to protect and commercialize it, is fundamental for tech M&A deals and for driving key deal components, including finance/structuring, due diligence, representations and warranties, and post-acquisition integration strategies. IP and data are essential for effectively monetizing digital products and services, and add value to a company through branding, innovative tech patents and databases.

IP affecting M&A deals

5G, and the expansion of related IoT applications and digital infrastructure, continue to drive M&A activity in the technology space. In particular, the increased use of AI, and algorithms powering AI applications, present key opportunities and challenges in tech M&A, including the extent to which data, ideas, and concepts derived from AI can be meaningfully protected by current IP law, as well as the impact of emerging privacy laws on AI's ability to "train" large data sets and make impactful, real-world decisions. Within the IP sphere, 2022 is expected to bring new developments to this rapidly developing area of law.

Trends in data protection and cybersecurity

As companies invest in technologies that collect, store or make use of personal data, compliance with data privacy laws will require continuous attention as evidenced by the increased focus on cross-border data transfer compliance, the implementation of Mainland China's new data protection regime, a number of data privacy bills in US states, and the **EU Data Act** recently proposed by the EU Commission. In an increasingly global marketplace, it is essential that companies stay on top of where their data is stored, how it must be managed, and where it can be sent in accordance with data protection laws. Our **Data Protection Day 2022 publication** provides a country-by-country breakdown of what this year is expected to bring in data protection.

Cybersecurity must also remain top of mind when it comes to tech M&A. Ransomware and significant cybersecurity incidents continue to rise, pose substantial risks, and are an essential area to manage both with respect to diligence and to protecting materials disclosed in the context of corporate transactions.

3 Section 3: The Importance of Tax Planning for Tech Transactions

*Authored by **Erik Christenson**, Partner, San Francisco & **María Antonia Azpeitia**, Partner, Madrid*

The changing international tax landscape will require that additional due diligence be performed to evaluate compliance with a host of new obligations, keeping in mind that penalties for not doing so can be significant. Acquirers will want to understand whether potential targets have fulfilled their reporting and payment obligations with respect to new Digital Service Taxes (DSTs), and keep in mind new rules regarding indirect tax registrations, collections, and substantiation of invoiced transactions as B2B or B2C. Additionally, there is a new generation of tax reporting and registration obligations for marketplaces and marketplace operators, as well as new financing obligations imposed on audio-visual service providers to finance public television services.

International tax changes

Changing international tax rules not only impact tax due diligence but also integration planning. In the US, proposed tax reforms would implement a global minimum tax and would adopt a country-by-country approach in the global intangible low-taxed income (GILTI) regime. In parallel, the OECD is moving forward with its "Two-Pillar Solution" to address the challenges of taxing the digital economy.

- **Pillar One** will create a new taxing right for countries with annual turnover in excess of EUR 20 billion, where a remote seller would otherwise have limited or no taxable nexus.
- **Pillar Two** will apply to any company with annual turnover above EUR 750 million. It will implement a global minimum tax, with the overriding principle that profits in any jurisdiction should be subject to at least a 15% rate of tax in the jurisdiction. Any low tax constituent entities will be picked up by the "income inclusion regime" of the ultimate parent entity or perhaps another group member.
- **Looking Ahead:** With model rules still being drafted, a great deal of uncertainty remains regarding the future global effective tax rate for the acquiring group. Against this uncertain backdrop, important decisions will have to be made with respect to integrating the target group's entities and how to optimize the tax results for the combined group under Pillar Two, including tax and financial consolidation with a special focus on optimizing tax attributes of the combined group (e.g., utilization and preservation of tax and book losses). It remains to be seen whether and how deal models will incorporate the global minimum tax concept.

Importance of the tax audit environment

Companies working through acquisitions should understand the tax audit environment in their targets' jurisdictions. They should also understand whether new approaches are being applied or explored by tax authorities. An emerging trend has seen tax authorities asserting that the licensee has a PE in the market country or perhaps applying new concepts like a "deemed royalty," supporting an assertion that the local entity or market contributed to the creation or enhancement of the group IP and/or that royalties should be attributed to that jurisdiction (and withholding tax applied).

IP holding structures are also being increasingly scrutinized by authorities looking to determine the owner and jurisdiction of the IP for tax purposes. IP integrations are especially contentious, with local tax authorities taking more aggressive positions with regard to IP "exit" transactions or business restructurings. Preparation that includes documenting a business rationale for the transaction and outlining the substance of the new IP owners is more critical than ever.

Digital transformation and tax

More broadly, digital transformation itself creates tax risks. The urgency of technology transactions and the need to integrate different structures and policies quickly make it imperative to identify and mitigate risks before the deal closes. A recent Baker McKenzie survey of 1,200 multinational companies, outlined in **Risk Reshaped: Tax Disputes Outlook 2022-2025**, shows that M&A transactions have been identified as a major source of risk in audits for future years.

4 What to Expect for SPACs & de-SPACs in the TMT Sector

*Authored by **Ivy Wong**, Partner, Hong Kong & **Adam Eastell**, Partner, London*

Since 2020, the number of SPAC listings has risen at an unprecedented rate. A SPAC has no prior business or operating revenue so it raises funds and lists its shares in an initial public offering (IPO) and then seeks a target company to acquire in a so-called "de-SPAC" transaction. As the US Securities and Exchange Commission (SEC) reviews the SPAC regime, companies may see increasing regulatory headwinds. Certain exchanges in Europe are also starting to emerge as alternative listing venues.

Both Hong Kong and Singapore recently launched their own SPAC regimes and these are expected to gain in prominence and further open up the global SPAC market this year. In January 2022, the Singapore Exchange welcomed its first 3 SPAC listings, all with a strong technology theme in the type of target companies they intended to acquire. Since the Hong Kong listing rules came into effect on 1 January 2022, several companies have filed their applications, including SPACs targeting technology companies.

De-SPACs in the TMT Sector

Technology companies offer SPAC sponsors potential for growth in earnings and profitability that they may not find in other sectors. According to data published by Refinitiv, there were 142 business combinations (worth an aggregate of USD 239 billion) involving a SPAC and a target in the High Technology sector announced between 2019 and 18 February 2022. This constitutes 27% of all de-SPAC transactions during this period, making technology companies the number one target for SPAC acquirers. We expect this activity will continue in 2022, with 49% of respondents in a recent Mergermarket study on technology M&A considering a SPAC to acquire a technology company within the next 12 months.[3]

De-SPAC transactions are not without legal and regulatory risk. In addition to intense scrutiny by the SEC in the US, de-SPAC transactions have faced a constant wave of shareholder lawsuits alleging material misstatements or omissions made in connection with the de-SPAC, or claiming that SPAC sponsors have a conflict of interest in rushing into a business combination. Recently, Delaware's Court of Chancery issued its first decision suggesting that, under Delaware law, a SPAC's sponsors and directors can be subject to "well-worn fiduciary principles" in connection with a de-SPAC transaction. Although technology de-SPAC transactions are expected to remain popular, these risks may lead to more deals being terminated before they close.

The rise in SPAC listings has led to oversaturation, with not enough attractive targets. Given the large number of US-listed SPACs now seeking acquisition targets, we expect to see such SPACs increasingly target technology companies in Asia Pacific to complete business combinations as the number of quality targets in the US domestic market may begin to dwindle.

[3] *Fast Forward: How Technology M&A is Reshaping Industry, Mergermarket, 2021.*
https://www.acurisstudios.com/fast-forward-how-technology-ma-reshaping-industry

5 Foreign Investment Review and Tech M&A

*Authored by **Samantha Mobley**, Partner, London & **Rod Hunter**, Partner, Washington DC*

Regulation of foreign investment in strategic sectors of the TMT industry has increased across several markets, driven largely by rising national protectionism and widening national security concerns (including economic security). This trend reflects the growing importance of technology and data to the global economy as well as the resultant vulnerabilities that may exist. COVID-19 has also galvanized the regulation of foreign investment as governments seek to protect strategic assets that may have become more exposed to acquisition. Cross-border tech M&A transactions are thus becoming more complex, especially where multiple jurisdictions are involved, with dealmakers needing to be cognizant of any mandatory requirements to file transactions for review and potentially consider voluntary notifications.

Spotlight on: the NSI Act in the UK

What Is It?
The NSI Act overhauling the UK FIR rules requires businesses and investors to submit mandatory notifications to the UK government's new Investment Security Unit (ISU) for certain investments in 17 key sectors.

What Does It Affect?
Several sectors are technology-focused and include computer hardware, communications and AI, with significant criminal penalties for failure to file. The UK government has broad powers to impose conditions on or prohibit investments that are found to pose a threat to national security, a concept that is not defined for maximum enforcement (more details **here**).

What Else Should Businesses Consider?
In addition to the mandatory notification requirement, the NSI Act enables the ISU to call in transactions for review outside of the 17 key sectors (more details **here**).

Outlook
While it is too early to gauge how the ISU will intervene and assess transactions in practice, we can expect a material volume of notifications as parties and advisors to tech M&A transactions may take a conservative approach to what falls within the scope of the 17 sector definitions and what else should be voluntarily notified. This is given the broad scope of the NSI Act and the stiff penalties for breach of the mandatory notification requirements. Risk mitigation and conditions precedent in transaction documents will continue to evolve as it becomes clearer how the UK government will use its new powers.

Spotlight on: CFIUS in the US

In 2018, the US Congress expanded the authority and resources of the CFIUS, an interagency committee that reviews foreign investments in the US for national security risks.

US Law Now Requires…

- Pre-closing filings where a non-US person acquires certain governance or information rights in US businesses that develop critical technology, a term defined principally by reference to export controls.
- Filings where government affiliated investors acquire 25% or more voting interest in businesses developing critical technology, operating critical infrastructure or collecting sensitive personal data of US citizens (called TID US businesses for Technology, Infrastructure and Data).

CFIUS Jurisdiction Now Encompasses…

- Many investments involving TID US businesses.
- Contacting businesses regarding transactions where the parties did not voluntarily submit a filing pre-closing.
- Note: CFIUS agencies have demonstrated a particular interest in investments that provide non-US entities access to identifiable personal data of US citizens, with CFIUS frequently imposing data security protections as a condition to approval of transactions.

6 Key Takeaways

The TMT deal landscape remains robust, but careful — and ideally front-end — deal planning will be required in anticipation of a raft of important legislative changes, including to privacy regulation and international tax, as well as a tightening of FIR rules in several jurisdictions.

Below are some key takeaways, with practical tips:

Digital Transformation

Digital transformation will continue to drive M&A investment in technology. IP and data will remain essential drivers in any tech M&A deal as they are key to monetizing digital products and services.

IP, Privacy and Cybersecurity

Technologies driving investment include 5G and IoT connectivity technology (and related digital infrastructure) as well as AI.

Important developments in data protection laws and regulatory practice will need to be factored into acquisition strategies. China's new data protection regime, the proposed EU Data Act, and an increased focus by privacy regulators on cross-border data transfer compliance are some of the important trends to watch.

Tax

The shifting international tax landscape will impact not only due diligence and deal structure, but also post-acquisition integration planning.

As the rules are fleshed out in the OECD's Pillar-Two reforms (establishing a global minimum tax rate), TMT companies might want to adjust their integration strategies. It remains to be seen whether and how these changes will be incorporated in deal models.

Acquirers must also understand the tax audit environment where the target may have material tax liability exposure, including whether tax authorities are exploring or adopting new approaches to tax collections in those markets.

SPAC Outlook

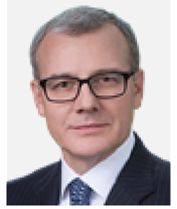
The US remains the largest and most mature market for SPAC listings — and this is likely to continue in 2022. Certain exchanges in Europe are starting to emerge as alternative listing venues, and new listing regimes in Hong Kong and Singapore are likely to open up the global SPAC market.

US-listed SPACs are likely to increasingly target technology companies in Asia Pacific and other regions as the number of quality targets in the domestic markets may dwindle.

Foreign Investment Review

In 2022, regulatory teams must keep up to date on the multitude of FIR regimes likely to be in play in global tech deals and investors must conduct FIR related risk assessments as early as possible with FIR issues treated as systematically and strategically as competition or merger law issues.

7 Key Contacts



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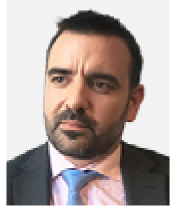

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