Debevoise & Plimpton

The Private Equity Report Quarterly

2025 Outlook | Volume 24, Issue 4

From the Editors

The private equity industry enters 2025 amidst numerous positive indicators. Investors are returning to private equity strategies after having been kept on the sidelines by poor macroeconomic conditions in 2022 and 2023. Interest rate cuts by both the Federal Reserve and the European Central Bank are now creating a more favorable liquidity and dealmaking environment. Both capital markets and alternative financing markets are strong. Donald Trump's victory in the U.S. presidential election altered the U.S regulatory outlook overnight, promising a return to a less aggressive and more predictable approach by regulators in a wide range of areas, including antitrust, SEC enforcement, ESG and noncompetes. And the EU introduced a "simplification revolution" with the goal of reducing EU reporting requirements by 25%.

But there are also new complexities with which to contend. Geopolitics is an increasingly concrete concern, with new outbound investment regulations taking effect in the United States, CFIUS scrutinizing private equity transactions and North Korea undertaking a sophisticated campaign to

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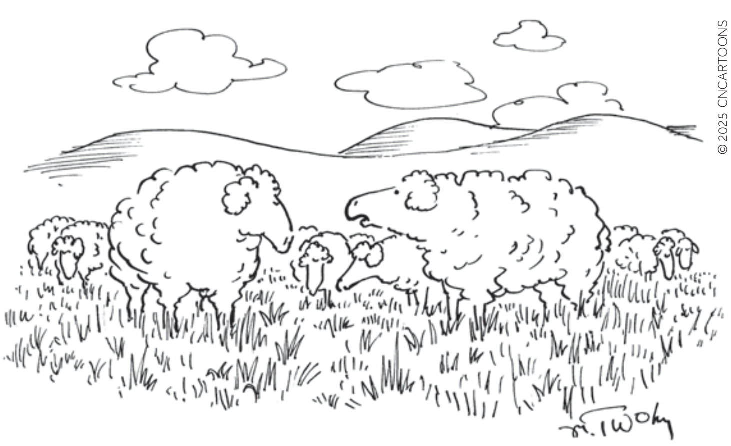

"It's tough sticking to a diet when you're surrounded by temptation."

CELEBRATING 25 YEARS THE PRIVATE EQUITY REPORT

What's Inside

infiltrate the systems of U.S. businesses (while generating revenue for state coffers). A recent U.S. Supreme Court ruling brings new considerations when conducting due diligence of a portfolio company's or target's trademark portfolio. The legal landscape regarding governance rights provisions in stockholder agreements continues to evolve. And if the Trump administration puts ESG on the federal back burner, companies must still navigate a patchwork of ESG regulations across U.S. state jurisdictions, as well as in the UK and the EU.

We hope you find the *2025 Private Equity Outlook* to be a useful summary of both the positive developments and the new challenges shaping the market as you navigate the year ahead.

Chambers CONTRIBUTOR Global Practice Guides 2024 Private Equity

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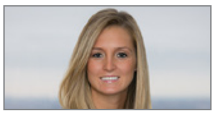

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While the past several years have proven challenging for fundraising, we see reasons for optimism as we head into 2025. Amidst a stabilizing financial environment, investors are demonstrating a growing appetite for private equity investment, and managers are deploying both tried-and-true as well as novel strategies to reach a broader range of participants.

Part of this investor appetite is fueled by an easing of interest rates. After interest rate hikes intended to combat inflation in 2022 and 2023 cast a pall on private equity strategies and outcomes, the second half of 2024 saw the beginnings of a rate-cutting cycle, with both the Federal Reserve and the European Central Bank lowering key rates. The potential for increased dealmaking given these more favorable interest rates serves to bolster investor confidence and suggests better prospects for liquidity in 2025, which we expect will help strengthen the fundraising environment.

While investor interest and optimism may be on the rise, investment managers are still being selected with care and caution. Investors seem keen to align with managers that have historically demonstrated strong performance records, preferring to develop long-term relationships with well-established managers rather than bet on market newcomers. While this has resulted in an increased focus on brand-name mega funds, we are also seeing renewed investor appetite for allocations to small- and mid-market funds, which aligns with our expectations for increased dealmaking and more frequent exit opportunities in the new year.

Much of the investor caution in manager selection stems from challenges of the past few years that are still acutely felt, including a marked increase in fundraise durations and limited exit opportunities. Managers have responded to investor concerns by embracing a variety of solutions, from novel fund structures and parallel vehicles to customized co-investment and separately managed account arrangements. Notably, managers are continuing to cater not only to more traditional institutional investors with large commitments but also to the steadily growing number of private wealth investors, including family offices and even retail investors, across all fund strategy types. While the broadening range of investor needs and bespoke accommodations increases the operational and regulatory complexities for managers, it also presents avenues for growth in the coming year.

While 2024 in many ways represented an extension of the challenging fundraising climate of the prior year, indicators of improving financial conditions and the creative solutions provided by well-positioned managers appear to be boosting investor confidence in the private markets, and we continue to be optimistic for continued improvements in the fundraising environment in the year to come.

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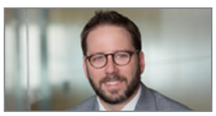

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The fund finance market continued to experience strong growth through 2024, driven by the ability of alternative lending sources with innovative financing products and structures to fill liquidity gaps of fund sponsors, while traditional fund finance lenders remained faced with balance sheet constraints and the aftershocks of the bank collapses of 2023.

Major bank lenders continued to grapple with interest rate increases, regulatory changes in capital treatment and other macroeconomic events, forcing them to be much more selective about credit extensions to fund sponsors. At the same time, the appetite of sponsors for debt financing seemed to be insatiable. The resulting competition for the limited bank balance sheet capacity available to the fund finance market continued to fuel substantial demand for alternative liquidity providers and bespoke financing solutions. With this demand came opportunity, and the growth and expansion of the fund finance lender base and product offerings witnessed in 2023 continued to proliferate throughout 2024.

Subscription facilities remained a staple for many fund sponsors, and demand for capital call-backed credit continued its year-on-year growth. The use of asset-based leverage continued to expand beyond credit and secondaries funds and across a broader range of fund investment strategies, particularly private equity funds. We also witnessed fund sponsors deploy NAV solutions up and down the capital structure of their fund platforms. Sponsors increasingly turned to these asset-based financing products to consummate acquisitions, to purchase portfolio company debt and, with growing scrutiny, to make distributions to limited partners.

The increased use of NAV facilities, particularly when used to fund distributions or to support a struggling portfolio, drew the attention of the investor community and the Institutional Limited Partners Association (ILPA). While ILPA did not publicly criticize NAV facilities as fervently as it had initially criticized subscription credit facilities a few years ago, the group strongly urged fund sponsors to disclose the rationale and key terms of NAV facilities and to engage investors for consent to use NAV facilities when clear authorization is lacking. ILPA also called for sponsors and investors to adopt language in fund documents that sets guardrails around permissible uses of NAV-based facilities going forward.

Sponsors also continue to raise capital from insurance companies and similar investors. While 2024 had seen a slowdown in activity in the face of market conditions and uncertainty over regulatory developments, we expect rated feeder structures and other structured products to continue to evolve and develop in 2025.

Private Funds Transactions


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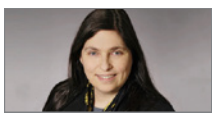
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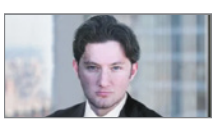
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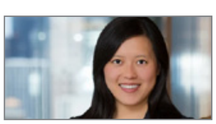
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Global secondaries volume continues to rise year on year, accompanied by the growth of new market entrants, such as evergreen '40 Act funds, raising retail capital for secondaries strategies. In the continuation fund market, several trends have gained headway in 2024 that will continue into 2025.

Purchase Price Deferrals

Historically, many sponsors argued that purchase price deferrals could make LPs presented with liquidity options less inclined to choose to sell. But over the last year, there has been a dramatic uptick in the use of this approach, as fund investors become more familiar with these arrangements and as deferrals emerged as an effective tool to bridge pricing gaps between sponsors looking for a par headline price and lead investors expecting to pay a discount to NAV. Deferral periods are often shorter in the continuation fund market than the traditional LP portfolio market, but deferral periods of a year or more are starting to be seen with some frequency in continuation fund transactions.

NAV Financing

While financing has traditionally been undertaken at the portfolio company or asset level, NAV financing at the continuation fund level is starting to become a more common occurrence. From the sponsor's perspective, NAV financing at the continuation fund level is similar to financing at the asset level insofar as it typically reduces the amount of equity needing to be raised by the sponsor from new investors in order to close a transaction. However, from the (very common) vantage point of a fund of funds lead investor, NAV financing at the continuation fund level will be accretive to the performance that such a lead investor reports to its own investors.

Indeed, the market is starting to see transactions that combine purchase price deferrals with NAV financing (e.g., 50/50 deferral deal with either the initial or back-end payment being NAV financed) in a manner that produces a very attractive return profile for fund of funds lead investors.

To Sell or to Roll Over?

Recent market surveys have confirmed what experienced investors have long known: LPs presented with a sell or roll election for a continuation fund transaction overwhelmingly choose to sell, often due to an inability to commit more capital and/or the desire for liquidity in a distribution-light environment. The inclination to sell is particularly pronounced for continuation fund deals toward the end of a main fund's life. This continues to be the case despite sponsors increasingly offering a status quo option on economics, which has become more common as new sponsors, who may be more conservative than earlier movers, test the continuation fund market.

How to treat co-investors in a continuation fund transaction has become a common issue for sponsors. While sponsors continue to be reluctant to commit upfront in co-investment deal documentation that co-investors will be provided a status quo rollover option that maintains their fee and carry-free economics, in practice, co-investors are

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Private Funds Transactions

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very often afforded this option, which is commonly structured as a choice between selling or "remaining in place." However, there are examples of sponsors determining that the "free ride" should end when the continuation fund transaction is completed, requiring co-investors that want to continue with the asset to agree to the economic deal applicable to the other continuation fund investors.

Leveraged Finance

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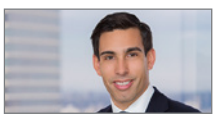

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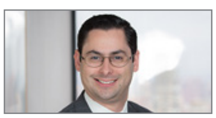

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The financing markets remained robust throughout 2024. Loan market activity reached a record high of $1.4 billion, reflecting a 60% increase from 2021 and a 41% increase from the prior high in 2017, according to PitchBook LCD. Market activity was mainly driven by non-M&A related opportunistic transactions, such as refinancings, repricings and dividend recaps. While only $500 billion of loan market deals involved financing transactions other than repricings, this still represented more than double the corresponding activity levels in 2022 and 2023. The primary beneficiaries of this market environment included well-performing companies that refinanced or repriced higher-cost debt with new, lower-cost debt and companies with near-term maturities that were able to address an upcoming maturity wall by refinancing with new, longer-dated debt.

As we look ahead to 2025, we expect market participants to maintain an opportunistic approach for a number of reasons. First, debt markets continue to be active, with many opportunistic transactions launching after the holidays in early January. M&A activity slowly but steadily increased throughout 2024, and market participants are hopeful this will accelerate in 2025 with the arrival of the Trump administration, allowing for M&A-related new issuances to build on the market momentum seen to date.

Second, rate cuts by the Federal Reserve may lead to lower overall cost of capital. The Fed completed three rate cuts since September 2024, and two additional rate cuts are expected in 2025. This is also expected to be another factor contributing to an increase in M&A activity, as buyers can more easily put in place substantiable capital structures to finance acquisitions.

Third, competition between the syndicated and private credit markets will continue into 2025. Many companies sought financing in the syndicated debt market in 2024 to achieve better pricing and terms than available in the private credit market. Meanwhile, private credit lenders remained active, due to their ability to provide speed and certainty of funding, as well as flexible capital structures with delayed draw facilities and paid-in-kind interest. Further, partnerships with investment firms and insurance companies should provide private credit providers with additional dry powder for new deals in the coming years. We expect that savvy private equity sponsors and borrowers will continue to consider both options as they seek the best available financing terms.

Fourth, liability management transactions will play a key role in financing activity, with highly levered companies and their sponsors looking to take advantage of better market conditions to address their capital structure ahead of upcoming maturities. As a result,

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Leveraged Finance

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lenders for new financings remain focused on negotiating named protections to limit the ability of borrowers and sponsors to implement coercive and non–pro rata transactions.

Finally, macroeconomic uncertainty from anticipated political events, such as the U.S. debt-ceiling debate in Congress and tariffs imposed by the new Trump administration, has the potential to cause short-term cooling of the market at certain times during the upcoming year. As a result, market participants will be less inclined to try to time market windows and instead will take advantage of the first available opportunity to launch debt financing transactions.

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Despite a slowdown in activity levels in Q4 compared to Q3, 2024 saw a recovery in U.S. private equity M&A deal activity, with the year ending up as the third best on record, overshadowed only by 2021 and 2022.

However, not all transaction types fared equally well in 2024. Despite reaching a two-year quarterly high in Q2, take-private activity saw a sharp decline in the second half of the year, bringing 2024's take-private annual activity down slightly below that of 2023, both in terms of deal value and deal count. Some of the drop-off in take-private activity might have been due to potential acquirers taking a wait-and-see approach in the lead-up to the U.S. election, combined with continued strong performance of the public markets. Nevertheless, with expected further interest rates cuts (albeit perhaps at a slower pace, based on the Fed's December meeting) and large sponsors seeking deals that match their desire for larger equity checks, take-private activity is poised for a comeback in the first half of 2025.

Sponsors pursuing take-privates should make sure to engage counsel at the very outset of the pursuit. Although the Delaware Supreme Court reversed the Delaware Court of Chancery's finding in *Mindbody* that Vista aided and abetted Mindbody's CEO in breaches of the duty of disclosure—reinforcing the difficulty of establishing an aiding and abetting claim—the plaintiffs' bar remains focused on finding ways to assert claims against perceived "deep pockets." Take-private transactions are a common target, especially where the transaction presents an arguable conflict of interest for the target's board or where a controlling stockholder is present.

For private deals, while add-ons and carve-outs continue to represent a significant portion of activity, the improved availability of more affordable debt financing appears to be increasing sponsor focus on new platform investments. We expect this trend to continue in 2025, fueled in part by further sponsor-to-sponsor activity as vintage investments are being realized.

While exit activity (including via IPOs) saw a healthy uptick in 2024, exits continued to trail new acquisitions, with sponsors remaining selective in bringing assets to market as they await further improved conditions before ultimately realizing the last few years' inventory buildup. We expect exit activity to further accelerate in 2025 but with continuation funds to remain as an attractive alternative liquidity path for sponsors.

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M&A (U.S.)

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Finally, while much remains to be seen regarding what the Trump administration will bring, we expect to see increased deal activity (at least in the U.S. market) in 2025. This is due in part to a perception of a more predictable antitrust environment, with regulators expected to revert to more traditional models of review and enforcement. Of particular interest for the private equity market is the likely return of structural and behavioral remedies, which have both the ability to de-risk transactions from a regulatory perspective and to be a catalyst for further dealmaking, given that sponsors are prime buyer candidates for structural remedy divestitures.

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Although European private equity M&A activity got off to a slow start during the first half of 2024, the pace picked up in the second half of the year. Compared to 2023, 2024 is estimated to have seen approximately a 28% growth in terms of deal value and a 12% growth in terms of deal count. In 2025, it is likely that activity levels will continue their upwards trajectory.

One key driver of growth going forward will be favorable macroeconomic conditions. Central banks in Europe, including the European Central Bank and the central banks of England, Switzerland and Sweden, lowered interest rates as inflation decreased, with positive effects on portfolio valuations, borrowing capabilities and general market optimism. Lower interest rates have also helped to drive down bid-ask spreads in M&A deals, making it easier for buyers and sellers to agree on key commercial terms. Sponsors also remain sitting on record amounts of dry powder. Partly as a result of these factors, 2024 saw exits to sponsors outnumber exits to strategics for the first time since 2014. On the other hand, consumers are more sensitive to price increases, and any sign that inflation might be returning to elevated levels—such as, in the UK, where inflation jumped from 1.7% in September 2024 to 2.6% two months later—may result in lackluster consumer confidence and lower consumer spending, which could reduce the attractiveness of deals in the consumer sector.

Another factor that may drive growth in 2025 and beyond is the increased focus on private markets by public pension schemes and sovereign wealth funds. A global survey by the Official Monetary and Financial Institutions Forum of 28 pension and sovereign wealth funds published in December 2024 revealed that more than 40% of such funds expect to take a bigger position in private equity. AustralianSuper's 2024 annual report stated that "unlisted assets are expected to outperform listed equivalents over the medium to long term." In the UK, the new Labour government has announced plans to consolidate the UK's fragmented Local Government Pension Scheme (currently managed by 86 different administering authorities, each managing assets between £300 million and £30 billion) into a handful of "megafunds," mirroring the arrangements in Australia and Canada. The UK Government estimates that this will unlock around £80 billion of additional investment, including into private equity.

The increased appetite for megadeals is another trend shaping the European M&A environment. Examples include the £5.4 billion take-private of Hargreaves Lansdown

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M&A (Europe)

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by a consortium of sponsors, Advent International's sale of Evri to Apollo for €3.2 billion and CD&R's acquisition of a 50% controlling stake in Opella from Sanofi for approximately €16 billion. Geographically, UK M&A activity levels are heating up. The final week of November 2024 alone saw four takeover offers announced, worth a total of £5.3 billion. In 2024, UK M&A deal value reached more than $306 billion by December 2024, a 57% increase on the same period in 2023 and significantly more than the $143 billion, $142 billion and $91 billion recorded by Germany, France and Italy, respectively.

Although sponsors are becoming more acquisitive, the market for exits remains muted in Europe, with exit value and deal count dropping in 2024 compared to 2023. This might be attributable to sponsors' preference for companies that have not previously been backed by institutional capital, which may command lower valuations or have less complicated debt structures, or sponsors' greater reluctance to budge on economics. As a result, the market for GP-led secondaries remains busy. The first three quarters of 2024 saw 16 continuation vehicles close in Europe, compared to seven in 2020. We expect this trend to continue in 2025.

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Although several Asia markets were buoyant in 2024, notably Japan (both inbound investments and outbound investments to the United States), India and Australia, a generally challenging liquidity environment and pressures on valuations prompted investors to seek creative exit strategies to adapt to market conditions.

Down Round IPOs

The Hong Kong IPO market had been largely subdued since mid-2022. After enduring one of its most challenging years in 2023, Hong Kong reclaimed its position among the top five global IPO markets in 2024. However, many recent IPOs in Hong Kong, including Horizon Robotics (the second-largest Hong Kong IPO in 2024), are "down rounds," in which the IPO valuation is below the company's latest pre-IPO financing round(s). While investors traditionally prefer to avoid down rounds and explore alternative exit routes, such as trade sales, these recent occurrences indicate that investors are beginning to accept the reality of lower valuation levels and willing to mark down their investments in exchange for quick liquidity.

Exercise of Redemption Rights

For investors lacking the option to exit through an IPO, an increasing number are exercising redemption rights that are typically granted in pre-IPO preference share financings and that require the portfolio company to redeem those preference shares at a pre-agreed price if certain exit events, such as a qualified IPO, do not materialize within an agreed time frame.

Historically, redemption rights have been exercised infrequently, as doing so can negatively affect an investor's reputation within the investment community and diminish their competitiveness for future investment opportunities. However, as exits

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M&A (Asia)

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become more difficult, and venture and growth financing becomes a buyer's market, more investors are contemplating redemption requests. While relatively few investors will actually pursue potentially lengthy and uncertain judicial proceedings for payment if the company does not comply with the redemption requests, many investors are using these requests strategically to gain leverage in restructuring negotiations.

Hybrid Continuation Fund / Strategic Transactions

Continuation funds remained a key strategy in 2024 for assets at the end of their life cycle that did not have a liquidity solution. As previously noted in the *Debevoise 2024 Private Equity Midyear Outlook*, share purchase agreements for transferring underlying assets from existing funds to continuation funds are now adopting terms typically found in traditional arm's-length M&A transactions. As an extension of this trend, recently we have started seeing transactions where a continuation fund and a third-party strategic investor jointly acquire a portfolio company from the existing fund.

Involving a strategic investor offers several advantages: it enhances continuation fund LP confidence regarding fair asset valuation; ensures the underlying assets are managed effectively, benefiting from the strategic investor's industry expertise; and leads to improved deal protections for the continuation fund such as a more robust set of representations and warranties concerning the target's assets and operations. These advantages help GPs secure support from both rollover and new LPs for continuation fund transactions, particularly in a climate of caution among Asian investors.

Preferred Equity as a Liquidity Alternative

The trend in the United States and the EU in the past few years of preferred equity financing by PE funds is now gaining traction as a solution to short- and medium-term liquidity challenges in Asia. Preferred equity provides new investors with priority over the fund's GP and LPs in the distribution waterfall of proceeds until the preferred equity investors achieve a specified rate of return. Preferred equity may be issued by the fund or an SPV below the fund, with the proceeds from the preferred equity financing paid to the LPs to boost the fund's distributions to paid-in ratio.

Preferred equity transactions can be executed within a few weeks—significantly faster than traditional continuation fund transactions, which may take months to close. Moreover, they may not require agreement on the valuation of the underlying assets, as the economics of preferred equity already provide for a minimum return and downside protection. This is especially appealing in a depressed valuation environment and makes preferred equity an effective tool for bridging valuation gaps.

Looking Ahead to 2025

Looking forward, we expect these trends to continue in 2025, with M&A in India and both inbound and outbound M&A in Japan in particular at least somewhat offsetting the slowdown in China, where the implications of the new U.S. administration for growth and transactions in Asia remain uncertain. Further, it will be important to monitor whether China's economic stimulus package is adequate to enhance its domestic consumption and stimulate M&A activities.

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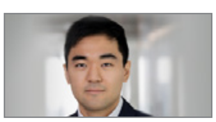

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The IPO Market and Follow-On Transactions

Last year saw a notable recovery of the U.S. equity capital markets on multiple fronts. While initial public offering (IPO) activity has yet to return to the peak of 2021, U.S. equity capital markets activity in 2024 surpassed that of 2022 and 2023, driven by a flurry of follow-on offerings, as sponsors continued to search for liquidity and issuers sought to strengthen their balance sheets during a year of strong market valuations. Additionally, there has been a notable trend towards spin-offs while the IPO market has been quiet.

Following the slowdown in 2022 and 2023, there is now a robust backlog of companies ready to move toward an IPO. Nonetheless, companies considering making that leap should keep in mind several factors including the geopolitical environment and evolving Federal Reserve policy, as a cycle of interest rate cuts is often seen as necessary to support a strong IPO market. Having said that, IPO activity has historically increased in the year after a U.S. presidential election as policies stabilize and market outlook clarifies for the medium term. This trend has held following each of the past four presidential elections, regardless of the political party taking office. Accordingly, we expect 2025 to be a strong year for the IPO market, assuming there are no unforeseen macroeconomic disruptions.

Alternative Capital-Raising Tools

As with public equity issuances, private investment in public equity (PIPE) transactions and convertible bond issuance activity, while not yet back to their 2021 peak, experienced significant increases in 2024.

The market for PIPE transactions has generally aligned with the M&A market because PIPE transactions can be an attractive means to finance M&A activity, especially when traditional financial markets are soft. In addition, PIPE activity has historically been correlated with interest rates, with PIPEs providing an alternative to high-interest debt financing and downside protection for investors during times of market uncertainty. Although 2024 showed signs of recovery in the M&A market, M&A activity has not yet returned to 2021 levels. Nevertheless, PIPE activity saw substantial recovery in 2024, increasing by approximately 21% from 2023.

Similarly, the convertible bond market faced considerable challenges in the past few years, due to the impact of slowing economic growth, volatile public equity markets, decreasing company valuations and high interest rates. However, the market for convertible bonds continued its recovery in 2024, with 97 offerings in 2024 as compared to 74 in 2023 and 50 in 2022.

While 2024 brought reason for optimism, substantial headwinds that have depressed PIPE transactions and convertible bond issuances since 2021, such as interest rates that are still higher than those in previous market cycles, underwhelming corporate earnings and volatile public markets, have not yet fully abated. At the same time, improving market conditions and recent interest rate cuts may contribute to a further recovery in M&A activity, signaling positive investor sentiment and tailwinds for PIPE transactions

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Capital Markets

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(although any increase in PIPE transactions may be slightly tempered by issuers turning back to traditional debt financing in a lower interest rate environment). As more favorable market conditions make their way to mid- and small-cap companies, it is likely that the market for convertible bonds will continue to improve as well.

Please see our full article, Chambers Global Practice Guide: Equity Finance 2024 Trends and Developments, for a detailed analysis of the trends and developments in equity capital markets in 2024 and our expectations for 2025.

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The main UK tax developments likely to affect investment fund sponsors in 2025 stem from announcements made in the UK Government's two primary financial statements (known as "Budgets") in 2024.

In the Spring Budget, the former Conservative government announced that it would abolish the current, long-standing tax rules that benefit certain UK residents for whom the UK is not their permanent home (who are called "non-UK domiciled" or "non-dom"). The two rules in question are the "remittance basis" of UK taxation of non-UK income and gains, and parts of the UK's inheritance tax regime. These rules would be replaced with new rules that would curtail the current tax benefits and would generally only apply during the first four years of an individual's UK residence.

In the Autumn Budget—given by the new Labour government after its victory in the UK's general election—it was announced that the new government intends to (i) largely adopt the Conservatives' replacement of the "non-dom" tax regimes with residence-based regimes, (ii) impose a 1.2% increase to the rate of employer national insurance contributions (NICs) from 13.8% to 15%, and (iii) implement changes to the taxation of carried interest (or "carry"), including changes to the headline tax rate and significant reforms to carry taxing rules. Each of these measures will take effect, to varying degrees, from April 2025.

The increase in employer NICs will result in a much larger windfall to the UK Treasury than the other measures and may have a substantial effect on investment funds' UK offices and UK portfolio companies, while the changes to the "non-dom" tax regimes and the taxation of carry will affect individual private equity professionals who work in the UK according to their particular circumstances. We previously discussed the "non-dom" issues in detail in the Debevoise 2024 Private Equity Midyear Outlook. We summarize below the proposed changes to the taxation of carry, which entail extensive amendments to UK tax law.

Short-Term Changes to Carry Tax Rates

Beginning in April 2025, the higher rate of capital gains tax on carry will increase by 4%, from 28% to 32%. Carry taking the form of dividends (typically taxed at up to 39.35%) and interest (typically taxed at up to 45%) will not be affected by this change.

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Tax (UK)

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Longer-Term Reform to UK Carry Taxation

Starting in April 2026, a wider reform of carry taxation will take effect. The core change under the new rules is that (assuming a partnership structure), rather than being taxed as a partnership profit share arising from *investment* activity, in which profits are taxed based on the underlying form (e.g., capital gains, dividends or interest) in which they arise to the relevant fund, carry will be taxed entirely as profit from an individual *trading* activity. This would, ostensibly, result in carry typically being taxed at 45%, with a further 2% NIC bringing the overall effective rate to 47%. However, "qualifying" (i.e. "good") carry will be eligible for a partial tax exemption, giving it an effective rate of approximately 34.1%.

What constitutes "qualifying" carry is subject to ongoing consultation. Key features in the current consultation papers are:

- The carry must be "qualifying" as determined under the UK's income-based carried interest (IBCI) rules. This mainly requires the fund to hold portfolio investments for a weighted average period of at least 40 months, but special rules apply to certain types of funds.
- The carry recipient or the investment fund sponsor may need to make a minimum co-investment, although this is less certain to be implemented.
- The carry recipient may need to hold their interest in the carry vehicle for a minimum period of time prior to receiving carry distributions, although, again, this is less certain to be implemented.

Further, internationally mobile carry recipients who do some work in the UK but who are not UK resident should take note that there is a possibility that, under the new rules, they may be exposed to a UK tax liability from which they might currently be protected due to current law taxing carry as a profit share from an *investment* partnership. This point, which entails some complicated analysis (including interpretation of various tax treaties), along with finalization of the "qualifying" criteria, should become clearer once draft legislation is published later this year.

Antitrust


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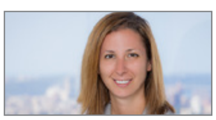
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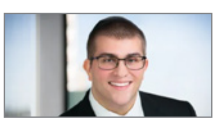
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U.S. antitrust enforcement of private equity deals will see an adjusted focus and new priorities in 2025. While private capital will generally enjoy improved standing with the antitrust agencies, the regulatory landscape will still demand vigilance and mindfulness of the risks associated with problematic transactions or behaviors.

Under the previous Trump administration, private capital transactions often served as a favored remedy for resolving antitrust concerns in mergers and acquisitions. That perspective underwent a polar shift under the Biden administration, where remedies were disfavored and negotiated settlements largely disappeared. In 2025, we anticipate a return to the Trump-era perspective, in which private capital's role in the U.S. economy is regarded more favorably. Antitrust regulators are likely to adopt a more tailored approach, evaluating private capital organizations individually rather than treating them as a monolithic sector.

Merger reviews should benefit from increased transparency and a renewed emphasis on economic principles as a core tenet of antitrust analysis. Traditional theories of harm are likely to predominate, while less-tested and unconventional theories of harm proposed by the Khan- and Kanter-led agencies may be sidelined. Despite this shift, problematic transactions will continue to be scrutinized and challenged where warranted. Document hygiene and preparation will continue to be important to successful merger review.

Healthcare and managed service organization growth will continue to be a focal point of both Congress and antitrust enforcement, as it was during the last Trump administration. Key areas of focus will be pharmacy benefit managers, pharmaceutical distribution, health insurance and hospital transactions involving significant geographic market shares. The largest technology companies will similarly remain targets—after all, the investigations that led to lawsuits against Google, Meta and others originated under the Trump administration. In contrast, energy sector transactions are likely to receive more favorable treatment. Although Congress will continue to examine mergers and acquisitions as well as certain conduct that allegedly impairs competition in this sector, this scrutiny is expected to have less impact than in recent years.

The agencies appear poised to repeal or alter the 2023 Merger Guidelines in favor of more business-friendly positions. Whether the guidelines are repealed or not, certain theories expressed in the guidelines (such as those centered on labor market concerns) may become disfavored or be tacitly set aside (such as those involving lowered structural presumption thresholds). Since the antitrust agencies under the Biden administration revoked most antitrust guidance and did not replace it, increased guidance from the agencies is likely in 2025 and beyond.

However, these changes will not be immediate. The frontline staff at each agency—a good portion of which have embraced some of or all the progressive antitrust agenda—will remain in place for some time. Improved transparency—particularly at the FTC following Chair Khan's departure—will help mitigate these transitional challenges.

However, even if the federal government tempers the progressive antitrust policies, some state attorneys general are expected to carry forward aggressive enforcement.

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Antitrust

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Empowered by the State Venue Act, states have become key players in merger control, complementing federal oversight.

Outside of the United States, 2024 saw heightened regulatory scrutiny of deals, and that trend will continue in 2025. The EU Foreign Subsidies Regulation has been in force for over a year, with almost 150 transactions notified (a significantly higher number than the 30–40 deals a year that were expected to be caught). Similar levels of scrutiny are expected in 2025, and investors should anticipate multiple rounds of questions and disclosure requests. Foreign Direct Investment (FDI) review became even more embedded as a core consideration for transactions during 2024. Several new or reformed FDI screening regimes within the EU came into force last year (including in Luxembourg and Sweden) and, after numerous delays, the Irish regime came into force on January 6, 2025, bringing the number of EU member states with FDI screening mechanisms to 25.

In the realm of merger control, roll-up transactions—whereby a private capital sponsor or its portfolio companies gain scale through making multiple acquisitions of small targets in the same sector—were predictably a frequent focus of regulatory scrutiny in 2024. This is expected to continue into 2025, not least because multiple EU member states have adopted "call-in powers" allowing them to refer a proposed merger to the European Commission for review even if the deal falls below the usual threshold. These call-in powers were largely adopted in response to the ruling in September by the European Court of Justice regarding the *Illumina/GRAIL* merger and are particularly targeted to so-called "killer acquisitions." (Our full case analysis can be viewed here.) Similar powers are coming into force in the UK on January 1, 2025, with the commencement of the UK Digital Markets, Competition and Consumers Act 2024.

National Security

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In 2025, cross-border private equity transactions will likely continue to draw intense national security scrutiny, particularly when they involve a nexus to China. We expect the Trump administration to maintain an aggressive enforcement posture, empowered by recent Biden administration regulations, including new Outbound Investment Regulations and several measures enabling more robust enforcement by the Committee on Foreign Investment in the United States (CFIUS). In addition, the TikTok ban litigation highlights federal distrust of Chinese-owned companies—and courts' willingness to generally defer to the government's national security concerns.

New Outbound Investment Regulations

On October 28, 2024, the U.S. Treasury Department's Office of Investment Security published a final rule, the Outbound Investment Regulations (the "Regulations") establishing new controls on certain technology-related investments by U.S. persons in or related to the People's Republic of China, Hong Kong and Macau. The Regulations became effective on January 2, 2025, and marked a significant expansion of U.S. investment controls.

The Regulations impose either a notification requirement or a prohibition regarding China-related investment activities involving certain sensitive technologies and products

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National Security

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(currently, in the areas of semiconductors and microelectronics, quantum information technologies, and artificial intelligence systems).

The scope of the Regulations is very broad, covering U.S. persons and extending to their controlled foreign entities, which include foreign funds managed by U.S. persons. Covered targets include not only Chinese companies, but any company that evidences certain relationships with Chinese persons.

Further, the initial Continuing Resolution proposed in December 2024 included legislation to create additional requirements and restrictions regarding outbound investment activities. While these provisions did not make it into the final Continuing Resolution, we expect them to become law in the near term.

Private equity firms are starting to develop compliance approaches to navigate the new landscape created by the Regulations. These include implementing new risk-based diligence steps, requiring contractual representations and warranties from third parties, and providing training to U.S. investment professionals and portfolio company directors.

Escalating CFIUS Enforcement

As we noted last year, CFIUS is increasingly scrutinizing private equity transactions as overall enforcement becomes more aggressive. These trends are likely to continue in 2025, so it remains crucial that sponsors closely monitor CFIUS-related regulatory changes and guidance. Transactions will continue to require intensive analyses of complex fund structures to determine whether they are subject to CFIUS review, and the stakes for getting it right will remain high.

Due to broad bipartisan agreement on many national security issues, the personnel changes brought by the Trump administration are unlikely to drastically alter the CFIUS landscape, and the factors used to assess national security risk are likely to remain the same. However, some policy shifts are likely, including a greater emphasis on domestic industry and supply chain risks. Moreover, the protectionist stance of some appointees could lead to greater scrutiny of trade-sensitive industries or even a presumptive block against Chinese investment.

In addition, the Trump administration is armed with more potent CFIUS enforcement tools. A final rule increasing civil and criminal monetary penalties for non-compliance was issued in November 2024. Further, new export controls may increase the scope of items deemed "critical technology," including quantum computing and semiconductor manufacturing technologies.

TikTok Litigation

On January 17, 2025, the U.S. Supreme Court released its decision in *TikTok, Inc. et al. v. Garland*. The ruling upheld the Protecting Americans from Foreign Adversary Controlled Applications Act (PAFACA), which requires ByteDance, Ltd., a Chinese company, to divest its ownership of TikTok or face a ban in the United States effective January 19, 2025.

In upholding the law, the Court ruled that PAFACA's restrictions were justified by the government's interest in preventing the Chinese government from "leveraging its control over ByteDance Ltd. to capture the personal data of U.S. TikTok users." The court reasoned

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National Security

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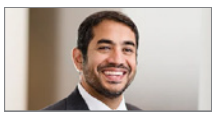
that TikTok's massive scale, its ability to collect "vast amounts" of data on American users, and its susceptibility to Chinese government coercion, justified the government's decision to single out TikTok for prohibition or divestment.

This case illustrates the enforcement risks that firms, including private equity, face in a tense geopolitical climate. In 2025, restrictions on U.S.-China business dealings are likely to become even more stringent, and courts will often defer to the government's national security concerns.

People Solutions



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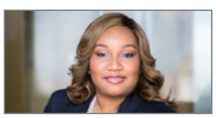

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Employers should anticipate the withdrawal of the Federal Trade Commission's (the "FTC" or "Commission") noncompete ban, which was issued in April 2024 but was set aside by federal district courts in Texas and Florida. While the FTC has appealed these decisions, the Commission is likely to withdraw the noncompete ban before any definitive judicial resolution occurs, given the anticipated changes at the FTC under the new Trump Administration; Mr. Trump has named Andrew Ferguson to replace Lina Khan as FTC Chair. (Ms. Khan, whose term as Chair expired on September 26, 2024, continues to serve as Acting Chair pending her departure or replacement.)

Mr. Ferguson, who was named an FTC commissioner in April 2024 and whose elevation to Chair does not require Senate confirmation, is known for his skepticism of Ms. Khan's regulatory agenda and his opposition to Ms. Khan's rulemaking efforts, including the noncompete ban. Mr. Ferguson, along with the other Republican FTC commissioners, has consistently argued that the FTC lacks statutory authority to impose such a rule—a position explained in a 45-page dissent to the rule's original promulgation. Mr. Trump also selected Mark Meador, a former Senate antitrust aide, to join the FTC, thereby creating a Republican majority on the commission once he is confirmed by the Senate. (Ms. Khan may stay on the commission until Mr. Meador is confirmed.) If the noncompete ban then is rescinded by the FTC, the rule would not take effect, rendering the legal appeals moot.

In the absence of a federal noncompete regime, some state governments are expected to further step up their regulatory efforts. Progressive states, such as California, Massachusetts, Minnesota and Washington, have already enacted stringent restrictions on noncompete clauses, including salary thresholds, duration limitations, job/industry restrictions and, in some instances, outright bans. New York may soon follow suit with a law restricting noncompete agreements for lower-wage workers, as signaled by Governor Kathy Hochul in her December 2023 veto of the state legislature's proposed noncompete ban. Legislative activity and judicial scrutiny at the state level are likely to increase, perpetuating a fragmented regulatory landscape that creates compliance challenges for businesses operating across multiple states. Private equity firms and their portfolio companies may find the following guidelines helpful in the face of this flux:

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People Solutions

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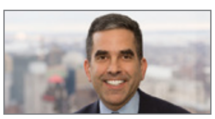
1. **Do Not Become Complacent.** With a Republican-led FTC poised to rescind the noncompete rule, the immediate threat of federal enforcement will likely disappear. However, this development will not alleviate state-level compliance burdens.

2. **Monitor State-Level Trends.** Anticipate heightened regulatory activity in states seeking to impose stricter noncompete limitations and a growing skepticism among courts to enforce noncompetes depending on their breadth and the specific facts and circumstances at issue. Continue to monitor new legislation and judicial decisions that may affect enforceability.

3. **Adapt to a Fragmented Regulatory Environment.** Employers operating in multiple jurisdictions must continue to navigate a complex patchwork of state laws. Developing tailored compliance strategies will be critical to mitigating legal risks.

4. **Stay Attuned to Evolving FTC Policies.** While the FTC's focus on noncompete agreements as a standalone priority may diminish, other areas of the agency's regulatory agenda could retain or even gain prominence. For example, restrictions on worker mobility were a common focus of merger reviews by the FTC, and it is possible that a focus on individual transactions and industry impact could continue, especially with respect to lower-wage workers. Understanding the Commission's shifting priorities under Mr. Ferguson's leadership will be essential for anticipating future enforcement trends.

SEC Enforcement



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On November 22, 2024, the U.S. Securities and Exchange Commission's Division of Enforcement released its enforcement results for fiscal year (FY) 2024. The 583 enforcement actions represented a 26% decline from FY 2023 and the lowest number of enforcement actions during any year of the past decade. This decline may stem partially from the SEC's heavy litigation burden due to factors that decrease the likelihood of settlement, such as the Biden administration's more aggressive settlement demands and focus on crypto cases with novel or existential issues. Last year's results were defined by outgoing Chair Gary Gensler's signature priorities, including recordkeeping violations, digital assets and cybersecurity.

We expect the Trump administration to move away from Chair Gensler's agenda and emphasize "bread and butter" enforcement matters that were in focus during the president's first term. These include offering frauds, investment adviser fraud and violations affecting retail investors. In addition, artificial intelligence is likely to be a continued priority as the technology advances. Below, we highlight notable actions from FY 2024 that are relevant to private equity advisers and serve as a preview of several of the Commission's likely enforcement priorities in FY 2025.

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SEC Enforcement

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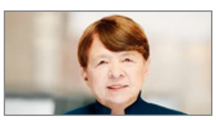

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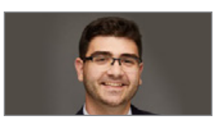

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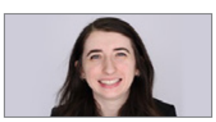

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Market Abuse and Material Nonpublic Information

In FY 2024, the SEC charged 34 insider trading actions, a small increase from the prior year. By historical standards, however, this is a low number, suggesting that the SEC may have de-prioritized insider trading enforcement. Nonetheless, the Commission brought many different types of actions related to material nonpublic information ("MNPI"). The SEC brought or settled charges against investment adviser representatives for a "cherry-picking" scheme and against several investment advisers for failing to implement and enforce policies and procedures to prevent MNPI misuse.

Artificial Intelligence

The SEC continued to scrutinize regulated entities for "AI washing," settling with investment advisers Delphia and Global Predictions after charging them with making false and misleading statements about their use of AI in the investment process. The SEC also charged QZ Asset Management for allegedly falsely asserting that its AI technology could generate exceptional returns while client funds remained "100%" protected.

Marketing Rule

The SEC continued its focus on enforcing compliance with the Marketing Rule, which, in FY 2024, resulted in settlements with more than a dozen investment advisers. Alleged violations related to improper advertisement of hypothetical performance, untrue or unsubstantiated statements of material fact, improper testimonials and endorsements, and misleading performance advertising. Several of these enforcement actions were approved by the Commission over the dissents of one or both Republican commissioners, which suggests that the scope of Marketing Rule enforcement may narrow during the Trump administration.

U.S. Funds Regulatory

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Generally, we believe the change in administration will likely return the SEC's attention to its core mandates of protecting retail investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation. As a result, we expect the significant negative (and at times excessively novel) focus on the private funds industry to slow, enforcement for basic rule missteps without demonstrated harm to lessen, and settlement penalties to decrease from the headline-grabbing sums extracted under Chair Gensler's SEC. Any new regulations that affect private funds are likely to be directed toward modernizing and streamlining existing regulatory frameworks, particularly with respect to capital formation, rather than imposing new obligations.

SEC Rulemaking Agenda

The 30 items on the SEC's Fall 2024 Regulatory Agenda include 13 at the proposed rulemaking stage and 17 at the final rule stage. However, many of the items listed as in the final rule stage were listed as in the final rule stage in previous Regulatory Agendas, with their target dates pushed back one or more times. Further, the Spring 2024 Agenda included the SEC's decision to repropose two rules that were in the final rule stage on the Fall 2023 Agenda: the Safeguarding Rule (a revision of the existing Custody Rule) and the Predictive Data Analytics Rule. Both of these remain on the proposed rule stage list on the Fall 2024 Agenda. The Spring 2025 Agenda, however, will more accurately reflect the new administration's regulatory priorities.

With respect to the three substantive new rulemakings applicable to private fund advisers on the final rule stage list—the proposed Outsourcing Rule, Cybersecurity Risk Management Rule and ESG Rule—we believe the Outsourcing and ESG Rules are unlikely to move forward under the new administration. It is possible, though perhaps not probable, that the Cybersecurity Risk Management Rule could advance in some form.

The to-be-reproposed Safeguarding Rule and the Predictive Data Analytics Rule elicited some of the most vocal objections from the industry, given the practical difficulties that would arise from compliance. The proposals reflected the Gensler SEC's broad distrust of the crypto industry and of the use of artificial intelligence and machine learning in the investment advisory space. Paul Atkins, who has been nominated to succeed Chair Gensler, is known to be a proponent of crypto/digital assets and financial industry innovation more generally. As a result, the perpetually elusive regulatory framework for crypto could finally come to fruition under Atkins' leadership. We could see a version of the Safeguarding Rule that addresses the custody requirements for digital assets and, potentially, the modernization of other aspects of the Custody Rule, such as custody of loan transactions. While we might see a new version of the Predictive Data Analytics Rule that aims to foster the use of innovative technology by advisers, an Atkins-led SEC could instead forego additional rulemaking in favor of applying the existing fiduciary framework to the conflicts that an adviser's use of advanced technology could present.

While changes to the definition of "accredited investor" under Regulation D has lingered on the Gensler SEC's Regulatory Agenda for years, it is possible that an Atkins SEC may look to make updates that would broaden access to private funds by providing additional ways for persons to qualify.

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U.S. Funds Regulatory

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Retail Access to Alternative Investments

Raising capital from retail investors is a key priority for the largest alternative asset managers across the globe. This development is giving rise to innovative new registered fund structures that can permit retail investors to gain exposure to private investment strategies. We expect to see investment advisers, especially the largest investment advisers, designing increasingly creative structures in their attempts to reach this investor segment. It is also possible that the industry may engage in extensive dialogue with an Atkins SEC about how to further facilitate the ability of registered funds to invest in private markets while still maintaining investor protections. We look forward to working with our clients on these innovations and are hopeful that they will receive additional support under a new administration.

Some Uncertainties Remain

While the election provided some relief within the private funds industry about the future regulatory landscape, it also introduced uncertainty around certain market factors that could affect private equity, such as tax rates and credits, inflation, interest rates, tariffs, and restrictions on inbound and outbound investing, as discussed in greater detail in other sections of this report.

European Funds Regulatory

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We anticipate several important developments in the European funds regulatory space during the first half of 2025. These include:

Budapest Declaration

In November 2024, The European Council adopted the Budapest Declaration on the New European Competitiveness Deal, which seeks to increase the competitiveness of European companies through measures that include a “simplification revolution” that aims to reduce EU reporting requirements by at least 25% in the first half of 2025. European Commission President Von der Leyen recently suggested that such steps could include consolidating the EU Taxonomy Regulation, the Corporate Sustainability Directive (CSRD) and the Corporate Sustainability Due Diligence Directive (CSDDD) into a single law. Although it is unclear how this would be achieved in practice (see our update on this topic), the European Commission has recently published a tentative work programme, indicating that it will publish an “Omnibus simplification package” in February 2025, which may be a reference to the simplification programme announced in the Budapest Declaration.

Corporate Sustainability Reporting Directive

The CSRD requires companies in scope to include sustainability information in their annual financial reports. Large listed issuers on EU-regulated exchanges must begin including sustainability information under the CSRD in their annual financial reports

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European Funds Regulatory

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published in 2025, based on data from their 2024 financial years. Asset managers will have to provide information, to the extent they have an EU-listed parent in scope. Large EU private companies or parent companies of large groups will first report sustainability information under the CSRD in 2026, based on data from their 2025 financial years. The detailed reporting requirements under the CSRD are set out in the accompanying European Sustainability Reporting Standards.

To determine the sustainability disclosures required, companies must make a "double materiality" assessment that considers both the financial impact of sustainability-related issues on the company itself, and the impact of the company's own operations and value chain on the environment and society. Additionally, an in-scope company must report on the extent that its activities are environmentally sustainable under the EU Taxonomy. The European Securities and Markets Authority has announced that this reporting obligation is one of its key enforcement priorities (see our update on this topic). Asset managers in scope of the CSRD are considering the extent to which their investee companies form part of their value chains and the type and scale of information they report in relation to their portfolios under the CSRD.

Sustainable Financial Disclosure Regulation

The year 2025 may see further progress towards adopting amendments to the Regulatory Technical Standards (RTS) under the Sustainable Financial Disclosure Regulation (SFDR). The RTS includes the list of principal adverse impact indicators and the templates for pre-contractual disclosure and ongoing reporting under the SFDR. Amendments to the SFDR were originally proposed by the three European Supervisory Authorities in December 2023.

The Commission is also expected to publish a proposal for a more extensive overhaul of the SFDR (known as "SFDR 2.0") in the first half of 2025. The proposal will likely reflect the detailed proposals recently published in December 2024 by the EU Platform on Sustainable Finance, which recommend the adoption of a categorization scheme under the SFDR, with minimum criteria for each category of products. Once published, the Commission's proposal will be subject to further consultation and the usual EU legislative process.

EU Green Bond Standard

As part of the EU's anti-greenwashing efforts, the EU's Green Bond Regulation entered into force in late December 2024. The Regulation establishes requirements for companies that offer bonds to EU investors which are designated as "European Green Bonds" or "EuGBs." Broadly, the proceeds of these bonds must be invested in environmentally sustainable economic activities aligned with the EU Taxonomy, and issuers must meet certain initial and ongoing disclosure requirements. Despite the name, the Regulation is directed at private issues of securities in the field of, for instance, project financing.

Amendments to Alternative Investment Fund Managers Directive

Published in March 2024, the European Commission's proposed amendments to the Alternative Investment Fund Managers Directive (AIFMD II) will continue to take shape in early 2025. Under AIFMD II, for example, the European Securities and Markets

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European Funds Regulatory

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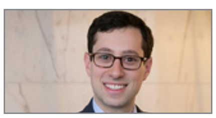
Authority (ESMA) will by April 2025 publish draft standards for open-ended AIFs involved in loan-origination activities. ESMA will also by this date publish finalized standards and guidelines (based on its 2024 consultation) on the use of liquidity management tools by AIFMs to mitigate financial stability risks.

UK Developments

The UK government has signaled its intention to adopt Sustainability Reporting Standards (SRS) based on the ISSB's IFRS S1 and S2 standards, which address general sustainability-related and climate-specific disclosure requirements, respectively. The UK government aims to consult on these draft standards in Q1 2025. Although it appears that these will initially only apply to UK-listed companies, the government has also committed to consult on the possibility of other "economically significant" companies disclosing information under UK SRS.

Separately, the UK government is consulting, through early 2025, on designs for a future UK Taxonomy for sustainable investment activities. The UK Financial Conduct Authority is also considering whether to extend the UK Sustainability Disclosure Requirements regime to UK firms providing portfolio management services, with proposed rules expected to be released in Q2 2025.

Investment Management Litigation (U.S.)



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If there's one thing investors can count on from year to year—and administration to administration—it's commercial litigation. Contractual counterparties and aggrieved investors continually pursue recourse in the courts, bringing claims arising from deals large and small, to enforce terms, secure damages, gain leverage, challenge structures, secure promised compensation, and otherwise vindicate common-law and statutory and contractual rights. Last year was a busy one for litigants across the board, but a few trends stood out as particularly noteworthy and likely to continue into what we expect to be a very litigious 2025:

Aiding and Abetting: The year 2024 closed with two dueling opinions on aiding and abetting liability. In *Mindbody*, the Delaware Supreme Court reversed a finding of such liability while clarifying the "knowing participation" requirement for such a claim. On the same day, the Delaware Chancery Court in *Enhabit* applied the clarified standard to find plaintiffs prevailed on their aiding and abetting claim. A third aiding and abetting claim, *Columbia Pipeline*, is pending before the Delaware Supreme Court with a decision expected in the new year. However these cases are ultimately resolved, they confirm that plaintiffs are focused on finding ways to pursue aiding and abetting claims in order to expand the defendant pool and attempt to plead fact-intensive claims that can be difficult to get dismissed before discovery.

Earnouts/Contingent Consideration: In 2024, in one of the largest judgments ever awarded by the Chancery Court, Johnson & Johnson was required to pay damages exceeding $1 billion on an earnout claim. Indeed, there seems to be a never-ending flow of earnout/contingent consideration litigation, as transactional counterparties continue

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Investment Management Litigation (U.S.)

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to rely on these types of provisions to bridge valuation gaps in order to get deals done. The new year should be no different. Even with parties getting smarter about how to structure and paper earnout provisions, we expect 2025 to see a continued stream of earnout-related litigation.

The Up-C Structure and TRAs: As we have noted, we are seeing an increase in litigation involving companies employing an Up-C structure. That litigation can come from the issuing of dividends while employing the Up-C structure, efforts to unwind the Up-C structure, or transactions that involve the termination or acceleration of the tax-receivable agreements (TRAs). We expect this litigation to continue into 2025 and to grow in significance as plaintiffs focus on transactions involving Up-C structures and TRAs.

Employment Litigation: Litigation and arbitration over terms of employment, carry, retention, and departure are an omnipresent part of the investment management litigation docket, with no sign of letting up. But in 2024, the rapid and varied development of noncompete and DEI rules added a new and growing set of claims and disputes, which we're likely to see more of in 2025.

ESG

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President Trump is expected to reverse various ESG-related policies of the Biden administration. Set forth below are several anticipated changes.

Environmental Regulation and Enforcement. President Trump is expected to repeal or limit various environmental rules and regulations, including those intended to limit emissions of methane and other greenhouse gases (GHG). He announced that he will withdraw the United States from the Paris Climate Agreement and its associated pledges to reduce GHG emissions. He also stated that he intends to accelerate the federal environmental permitting and approval processes for manufacturing, oil, gas, and other chemically intensive operations and to roll back current environmental justice initiatives.

The U.S. Environmental Protection Agency in the new administration is expected to focus more on encouraging alleged violators of environmental permits and emissions standards under the Clean Air Act and Clean Water Act to bring themselves into compliance with such laws and less on pursuing enforcement actions. The possible reduction in federal enforcement may result in more citizen's suits, lawsuits from environmental protection groups, and efforts by state authorities to seek punitive measures under state environmental laws.

Clean Energy. President Trump supports repealing portions of the Inflation Reduction Act (IRA), the 2022 law that encouraged investment in decarbonization and clean energy projects. However, as much of the investment derived from the IRA to date has been in Republican districts, support for repeal among Congressional Republicans may be limited.

Climate Disclosures. The Securities and Exchange Commission (SEC) under the Trump administration likely will rescind, or at least choose not to defend in court, the SEC's climate disclosure rules for public companies. It is also unlikely that the SEC will issue

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ESG

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a final ESG rule for investment advisers or expected human capital disclosure rules. California's climate disclosure laws, however, will remain unaffected by any changes to the SEC's rules. In addition, states such as New York, Illinois, and Minnesota are seeking to implement their own climate disclosure laws. It remains to be seen whether the absence of any federal climate disclosure rules will spur additional states to implement their own rules.

Other ESG Issues. President Trump has criticized corporate diversity, equity, and inclusion (DEI) initiatives and is expected to cut DEI-related programs and initiatives from federal agencies. However, with respect to human trafficking and forced labor, we anticipate the Trump Administration will continue the Biden Administration's increased enforcement of the Uighur Forced Labor Prevention Act.

Looking Ahead. The Trump Administration's anti-ESG stance may spur pro-ESG states, such as California and New York, to pass their own ESG laws. At the same time, anti-ESG states, such as Texas and Florida, may seek to pass additional anti-ESG laws of their own. The polarization in the United States surrounding ESG is likely to present challenges for private equity firms and portfolio companies operating across states, and globally, as ESG continues to be a policy priority and regulatory focus in many countries around the world. Given these challenges, we encourage private equity firms to keep abreast of regulatory requirements, investor expectations, and ongoing developments.

Real Estate

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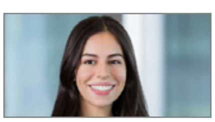

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The year 2025 may offer cautious optimism for the real estate industry. While stubborn inflation, high interest rates and geopolitical tensions have generated unease among investors in various real estate sectors over the last several years, a recent national survey of commercial real estate owners and investors suggests the tide may be turning, with an overwhelming majority of respondents anticipating revenue growth in the coming year and a lower percentage of respondents reporting plans to cut back on spending as compared to the last two years. Ultimately, the state of the market will turn on key external factors, including the scale of wage growth, potential tax cuts and the levels of investment made in the residential, commercial and industrial sectors.

Residential

Activity in the residential real estate market has been hindered over the past several years by high interest rates. The Federal Reserve is anticipating two rate cuts in the coming year, thereby suggesting a modest level of growth for the residential market. Home prices, moreover, are expected to rise. As potential buyers still struggle to afford such high prices, institutional investors and private equity firms will continue to respond by investing in build-to-rent properties to meet the demands of a growing cohort of renters. Forecasts predict a substantial amount of multifamily rental housing coming online (though experts attribute this to long construction lead times stretching

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Real Estate

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projects into 2025 rather than a strong appetite for new construction over the past two years). Because the projected growth in multifamily rental housing stock is forecast to keep pace with the larger pool of renters, the nationwide median asking rent is not expected to deviate significantly from that of 2024. Small improvements in affordability resulting from wage growth and tax cuts, however, may spur greater movement in the rental market. The housing market could also potentially benefit from policies proposed by the incoming Trump administration, including the allocation of federal lands for housing construction and the elimination of regulatory hurdles, such as permitting requirements, that increase the cost of construction, but the ultimate impact such moves would have on the residential housing market remains to be seen.

Commercial

The office market continued to find its footing over the past year. While owners are still feeling the effects of high interest rates and hybrid work policies, leasing volume has increased for sectors requiring in-person attendance, as well as in high-amenity, Class A buildings. On the other hand, Class B and Class C office buildings that lack such amenities continue to suffer from vacancies. Some developers are eyeing struggling properties in these classes (as well as distressed, vacant buildings) for office-to-residential conversion. Such conversions are projected to see an uptick in 2025, as bid-ask spreads are expected to come into alignment. Whether those conversions materialize, however, depends on a myriad of factors, including geography, availability of eligible office stock, local government support and the regulatory landscape.

Industrial

In the industrial sector, the third quarter of 2024 saw a sharp decline in warehouse development. While the prospect of tariffs could reverse this trend due to an increase in onshoring for manufacturers with flexible supply chains, tariffs could also harm the sector—and the commercial real estate industry more generally—if they lead to increases in inflation and interest rates. Industrial development has also seen a shift in focus from storage facilities to data centers over the past year, with demand for data centers currently outpacing the available supply. To meet that supply-demand imbalance, the coming year will likely bring an onslaught of data-center development, subject to the constraints that limit site viability, such as cost of power, weather risk, access to water, local government cooperation and labor force availability. Indeed, the shift towards data centers could prove to be a long-standing trend as artificial intelligence usage increases.

Restructuring

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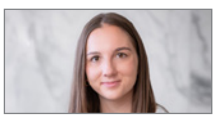

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Out-of-court liability management transactions continue to be predominant in restructurings, and we expect 2025 to bring more of the same. Notably, a significant percentage of liability management transactions—approximately one-third—are follow-on workouts from prior liability management transactions. As of October, the distressed exchange market was on track to hit a record-breaking volume of $50 billion in 2024. These trends are expected to continue, with default rates expected to grow as well.

But if liability management transactions remain common, they are also contentious. To be sure, such transactions have evolved from the binary model—where an initial participating lender group holding a small majority receives all the benefit and the non-participating lenders in the minority receive nothing—to the more refined, current iteration, where non-participating lenders are invited to participate, but on less favorable terms than offered to the majority. The non-participating lenders thus must choose between becoming a consenting—but disfavored—minority lender, remaining a non-participating lender in a worse-off position, or fighting the transaction in litigation. By inducing non-participating lenders to join the transaction, the majority group hopes to minimize litigation risk by shrinking the pool of holdout lenders. How effective this strategy is in practice remains to be seen. Recent court decisions offer mixed guidance and suggest litigation will continue, as courts emphasize that each transaction must be analyzed under the specific terms of the contracts at issue: the Fifth Circuit in *Serta Simmons* and the Southern District of Texas bankruptcy court in *Incora* found that uptier transactions were in breach of the agreements and imposed draconian remedies against the defendants, while a New York appellate court in *Mitel* found that an uptier transaction would be plainly permitted under the terms of that particular credit agreement.

Another notable restructuring trend is the rise of so-called "cooperation agreements"—binding contracts among lenders under which they agree to both present a united front throughout transaction negotiations and to only sell their holdings to other parties to the agreement. Originally developed to defend against the prisoners' dilemma strategy used by borrowers to coerce certain lenders to sign up to transactions, cooperation agreements have evolved into a mechanism for a critical mass of lenders to predetermine prioritization, as well as their recoveries. The initial members of cooperation agreements often condition entry of new group members on their willingness to accept lesser terms; indeed, sometimes subsequent members are expected to agree to terms before knowing in detail what they are. Lenders feel pressure to join these agreements because, once a majority of lenders have signed on, there is no longer a strong market for trading in debt held outside the group. There are some open questions about cooperation agreements—such as potential antitrust liability and characterization as a group under SEC Rules—that have not yet been tested under a Chapter 11 filing or litigation, and it is possible that 2025 is the year in which they will be.

Lastly, we expect courts to continue to clarify the questions raised by the Supreme Court's *Purdue* decision, including whether opt-out or opt-in plan provisions constitute a "consensual" release, exculpation provisions, and whether a plan provides for the "full satisfaction of claims" against a third-party non-debtor.

Data Strategy and Security

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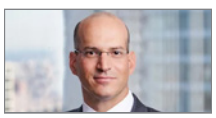

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A growing number of U.S. companies have been affected by the North Korean IT worker scheme, in which North Korea dispatches domestic IT workers to impersonate Western IT workers and then fraudulently apply for remote positions at U.S. companies. Once hired, the North Korean IT workers conceal their true geographic location by having their U.S. employers send company laptops to U.S. addresses that are run by Western-based co-conspirators. The North Korean IT workers remotely connect to these "laptop farms" and from there to their employers, to maintain the guise of being a U.S.-based employee. The long-running scheme, involving thousands of IT workers each drawing salaries as high as $300,000 per year, is intended to generate revenue for the North Korean regime, particularly its weapons of mass destruction and ballistic missile programs.

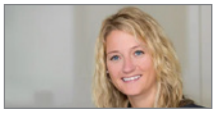
But the challenges to U.S companies have been becoming more complex. In some cases, the North Korean IT workers have planted malware, stolen sensitive data, and extorted companies by threatening to publish stolen data after they were discovered and fired. The scheme also poses legal issues beyond data and system exposure, including sanctions considerations arising from unwitting payments to sanctioned North Korean actors. The U.S. government has been warning about these risks since at least 2022 and issued its latest indictment relating to the scheme in December 2024. Private equity firms and their portfolio companies should consider these mitigation and due diligence measures to increase resilience against this evolving threat:

1. **Policies and Procedures.** Companies should conduct internal reviews of IT and developer hiring practices and procedures. If using third-party staffing firms or outsourcing companies for IT or software development positions, request documentation of their background check processes, consider auditing those processes, and escalating for review by the company potential red flags or discrepancies, especially for positions granting access to sensitive data.

2. **Employment Vetting.** Conduct due diligence checks on all contractors and consider requiring staffing companies to attest to the background diligence conducted on your behalf. When reviewing background check records, avoid relying solely on applicant-provided materials to verify information, and confirm that employment and education references are valid. (North Korea has created shell companies that the IT workers have added to their resumes.) Conduct video interviews to verify a potential worker's identity and require individuals to physically hold identification documents up to the camera. Note instances where individuals have difficulty producing such documents or their behavior is otherwise indicative of possible fraud.

3. **Technical Indicators.** In addition to employee/contractor vetting and reviewing the relevant policies and procedures, special attention should be paid to training the appropriate personnel (including both human resources personnel and employee managers) on spotting the tactics used by North Korean IT workers involved in the scheme. Company laptops issued to remote workers should be monitored for unusual network traffic. Companies should also monitor for, and restrict the use of, remote administration tools and be on the lookout for Voice over Internet Protocol ("VoIP") phone numbers. On-camera spot checks of remote employees are also an effective means to expose identity misrepresentation.

Intellectual Property



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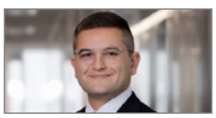

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There were a number of intellectual property decisions over the last year that may have surprise impacts for private equity sponsors and portfolio companies. These cases shed light on certain issues to look for during due diligence, the extent to which infringing conduct abroad may be subject to an injunction from a U.S. court, and how courts view aggressive online advertising strategies using competitors' trademarks as Google AdWords. Private equity sponsors and portfolio companies should also keep an eye on the pending Supreme Court opinion in *Dewberry Group Inc. v. Dewberry Engineers*, which is the subject of a recent article outlining the case's potential to affect businesses' ability to rely on corporate separateness to limit damages and/or litigation discovery.

Increased Risks for Businesses Engaging in "Expressive" Content

Historically, courts have tended to regard "expressive uses" of another's trademarks—such as use in a parody, artwork or even name of a service that provides newsworthy content—as protected by the First Amendment; plaintiffs alleging infringement in such cases faced a high bar for injunctive relief. The Supreme Court's 2023 opinion in *Jack Daniel's Props. v. VIP Prods. LLC*, however, altered the trademark legal landscape by holding that such "expressive" uses of trademarks (in that case, a parody) were not subject to First Amendment protection if the trademark use is "source identifying"—that is, if the infringer is using the mark at issue as its own trademark. This opinion, as well as subsequent lower court rulings in other cases, raises red flags for private equity sponsors considering the acquisition of a company with an intellectual property portfolio including marks or works containing expressive elements that, before *Jack Daniel's*, would have been easily protected by the First Amendment.

For example, in *Punchbowl, Inc. v. AJ Press, LLC*, the Ninth Circuit initially affirmed the district court's ruling that AJ Press's use of "Punchbowl News" for its political news website was protected expression under the First Amendment (given the site's news content) and thus did not constitute infringement of the mark of Punchbowl, Inc., which produces online invitations and greeting cards. Following the *Jack Daniel's* ruling, the Ninth Circuit subsequently withdrew its ruling in *Punchbowl*, determined AJ Press's use to be "source identifying" and therefore ineligible for protection, and remanded the case to the district court to conduct a traditional likelihood of confusion analysis.

The takeaway is that any mark, including marks used on expressive content, which may be construed to be "source identifying", will be subject to traditional principles for analyzing trademark infringement. Because the Supreme Court in *Jack Daniel's* did not define "source identifying," that task falls to the lower courts—a process we expect to be both ongoing and unpredictable. During the due diligence process, private equity sponsors should ensure that any expressive trademarks in the target company's portfolio meet the legal scrutiny of this more stringent standard.

Potential for Injunctions to Reach Foreign Conduct

Hermes Int'l v. Rothschild is the closely watched dispute between Hermes and the artist known as Mason Rothschild, whose "MetaBirkin" non-fungible tokens (NFTs) depict Hermes' iconic Birkin bags covered in fur. The Southern District of New York, in a

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Intellectual Property

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February 2023 jury trial, found that Rothschild infringed on Hermes' trademark rights; the case is now before the Second Circuit on appeal. In the meantime, Rothschild sought clarification from the trial court that its permanent injunction against Rothschild would nonetheless allow Rothschild to permit a Swedish museum to exhibit the infringing MetaBirkins. Rothschild's request raised the interesting question as to whether a U.S. court could enjoin conduct occurring abroad—a possibility that had appeared to be foreclosed following the Supreme Court's decision just months earlier in *Abitron Austria GmbH v. Hetronic Germany GmbH* that the Lanham Act does not have extraterritorial reach.

In its decision regarding Rothschild's request, the court focused on where the authorization would occur (i.e., from within the United States), as opposed to where the ultimate infringing use would occur (i.e., at a museum in Sweden), to construe the court's injunctive powers to reach such conduct, even in light of *Abitron*. This case is significant because it suggests that a U.S. court may be able to prevent infringing conduct occurring abroad if conduct occurring in the United States is furthering, sponsoring or authorizing those foreign activities.

Risks of Online Keyword Advertising

In *1-800 Contacts, Inc. v. JAND, Inc., d/b/a Warby Parker*, the Second Circuit considered whether the purchase and use of a competitor's name and registered trademarks in Google AdWords constituted trademark infringement. The court applied a traditional likelihood of confusion analysis, which looks at several factors (i.e., similarity of the marks being used, strength of the plaintiff's mark, and similarity of the goods or services offered under the marks) to determine if Warby Parker's purchase of "1-800 Contacts" as an AdWord (such that an advertisement for Warby Parker would show up when consumers searched for 1-800 Contacts on Google) gave rise to liability for trademark infringement. Even though the parties were in direct competition, the court found that Warby Parker's advertising practices were not likely to cause consumer confusion (i.e., causing consumers to believe the Warby Parker advertisement is somehow related to, or sponsored by, 1-800 Contacts). The Second Circuit affirmed judgment in Warby Parker's favor. A similar case, *Lerner & Rowe PC v. Brown Engstrand & Shelly LLC*, was brought in the Ninth Circuit, which resulted in a nearly identical outcome, and suggests the analysis will be similar across jurisdictions.

In light of these opinions, private equity sponsors looking to acquire companies conducting extensive online advertising (or firms with portfolio companies already conducting such practices) may take some comfort that the purchase of a competitor's trademark as an AdWord will not give rise to claims for trademark infringement if it does not cause confusion (i.e., so long as the competitor's mark is not used in the displayed ad, the user's own mark remains clearly visible, and the resulting post is clearly labeled as an ad). In fact, these opinions suggest that sponsors looking to strengthen the companies within their portfolio may proactively suggest such competitive practices, assuming it is done in a manner consistent with those in *1-800 Contacts and Lerner & Rowe*.

Life Sciences Regulatory

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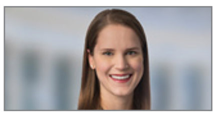

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The second Trump administration is expected to significantly affect FDA policies and priorities, creating potential opportunities for investors in life sciences and consumer product companies. In addition to Robert F. Kennedy Jr.'s nomination to lead the Department of Health and Human Services, Dr. Martin A. Makary, a Johns Hopkins University surgeon, has been tapped for the role of FDA commissioner. Dr. Makary is respected within the medical community and is a proponent of technology-driven, innovative approaches to healthcare, which will be essential as FDA continues to develop policies addressing the use of artificial intelligence in medical devices, drug discovery and manufacturing.

FDA funding and staffing will be hot-button issues in the new administration. President Trump has expressed an intent to shrink the government workforce generally, and Mr. Kennedy is in favor of staffing cuts at FDA. In addition, Mr. Kennedy, a critic of the pharmaceutical industry, has proposed cutting FDA's budget in half and doing away with industry user fees. Although Congress would need to approve budgetary changes, any significant budget cuts could negatively affect product review timelines. Similarly, staffing reductions could slow down approval and other regulatory processes.

We expect President Trump to continue his focus on drug pricing. He previously proposed a "most favored nation" drug-pricing initiative; in addition, the new administration may attempt to reduce drug prices through the existing Inflation Reduction Act negotiation process.

Given Mr. Kennedy's long-standing focus on vaccine safety, we anticipate greater scrutiny in this area, both regarding vaccines under development and those already on the market. Mr. Kennedy's "Make American Healthy Again" agenda—encouraging the distribution of nutritious, unprocessed foods—may also affect FDA regulation of foods and color additives. Both Mr. Kennedy and Dr. Makary are interested in alternative, non-medical treatments, which could lead to a more lenient regulatory environment for dietary supplements and functional foods. It could also result in an emphasis on consumer health, including digital health innovations and over-the-counter drugs that permit greater self-care without physician intervention.

Life sciences companies and investors should be aware of the potential for increased enforcement in certain areas. For example, Mr. Kennedy has expressed a desire to ban direct-to-consumer prescription drug advertisements, and although a ban would be subject to challenge under the First Amendment, FDA's Office of Prescription Drug Promotion may nonetheless increase enforcement of prescription drug advertising. In addition, we anticipate greater scrutiny of foreign suppliers of FDA-regulated products and ingredients, particularly those located in China.

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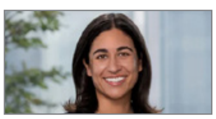

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The legal landscape for controlling stockholders under Delaware corporate law continued to evolve in 2024. In particular, stockholder agreements were put under the microscope following a number of lawsuits challenging the legitimacy of governance rights in such agreements, including in *W. Palm Beach Firefighters' Pension Fund v. Moelis & Co.*

It has been common market practice for controlling stockholders to retain governance rights in a controlled company after an IPO, often through a stockholder agreement. *Moelis* concerned a stockholder agreement between Moelis & Company and its founder, Ken Moelis, which was entered into at the time of the company's IPO. The Delaware Court of Chancery found multiple provisions of the agreement to be facially invalid on the ground that the provisions deprived the company's board of directors of a significant portion of its authority, contravening Sections 141(a) and 141(c) of the Delaware General Corporation Law (the "DGCL"). The decision called into question the enforceability of governance rights in a wide variety of stockholder agreements, including those involving founders, sponsors or stockholder activists.

To better align the DGCL with market practice, following the *Moelis* decision the Delaware legislature amended the DGCL, including by adding new Section 122(18). This amendment authorizes a corporation to enter into contracts with one or more of its stockholders or beneficial owners of its stock and provides a non-exclusive list of provisions that such a contract may include, including provisions relating to restrictions or prohibitions on taking certain actions, requirements for prior approval or consent, and covenants by the company to take or refrain from taking specified actions. However, the amendments expressly provide that any provision that is contrary to the company's certificate of incorporation or the laws of the State of Delaware is not enforceable against the corporation. While the amendments apply retrospectively to agreements entered into prior to August 1, 2024, they do not apply to lawsuits completed or pending on or before August 1, 2024. The law predating the amendments applies to those cases.

Even with the benefit of the recent amendments, parties entering into stockholder agreements still need to be mindful of potential conflicts between those agreements and the DGCL. For example, in *Seavitt v N-able, Inc.*, the Delaware Court of Chancery found that pre-approval requirements relating to change of control transactions violated the DGCL sections applicable to such transactions. While the court applied the law as it stood predating the post-*Moelis* amendments, the court may have well reached the same conclusion under those amendments. The court noted that approving a merger or consolidation or a sale of all or substantially all of the company's assets "requires a two-step process," in which the board of directors must first initiate the process by approving the transaction and recommending the transaction to stockholders, only after which

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Public Company Advisory

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stockholders may vote to approve the transaction. Thus, a stockholder agreement provision that required the prior written approval of the controlling stockholder before the board could approve a change of control transaction impermissibly displaced the statutory process for approving such transactions and caused the board to abdicate its role as a "gatekeeper."

The court also found that the stockholder agreement could not be incorporated by reference into the certificate of incorporation of the company. The court explained that, although DGCL Section 102(d) permits charter provisions to be "made dependent upon facts ascertainable" outside the certificate of incorporation, substantive terms of a private agreement are not "facts" within the meaning of the DGCL—in part because the private agreement could be amended in a way that would have the effect of amending the company's certificate of incorporation without the requisite board and stockholder approvals for a charter amendment. Here, too, the post-*Moelis* amendments are unlikely to have affected the court's ruling. Therefore, any rights that may conflict with the certificate of incorporation should be included directly in the certificate of incorporation, particularly when amending it in connection with an IPO.

How courts will reconcile the post-*Moelis* amendments with existing DGCL provisions remains to be seen. Parties entering into a stockholder agreement should therefore review the governance rights included in the agreement for consistency with those permitted by DGCL Section 122(18) as well as to ensure such rights do not conflict with other sections of the DGCL.

About the Debevoise Private Equity Group

A trusted partner and legal advisor to a majority of the world's largest private equity firms, Debevoise & Plimpton LLP has been a market leader in the Private Equity industry for over 40 years. The firm's Private Equity Group brings together the diverse skills and capabilities of more than 500 lawyers around the world from a multitude of practice areas, working together to advise our clients across the entire private equity life cycle. The Group's strong track record, leading-edge insights, deep bench and commitment to unified, agile teams are why, year after year, clients quoted in *Chambers Global, Chambers USA, The Legal 500* and *PEI* cite Debevoise for our close-knit partnership, breadth of resources and relentless focus on results.

Debevoise & Plimpton LLP is a premier law firm with market-leading practices, a global perspective and strong New York roots. We deliver effective solutions to our clients' most important legal challenges, applying clear commercial judgment and a distinctively collaborative approach.

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