



## Lowenstein Sandler's Insurance Recovery Podcast: Don't Take No For An Answer

**Episode 66:**  
**The Intersection of Emerging Trends in M&A/ Private  
Equity and Reps & Warranty Insurance:  
The Road Remains Bumpy For Dealmakers**

By [Lynda Bennett](#), [Eric Jesse](#), [Marita Makinen](#)  
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- Lynda Bennett:** Welcome to Don't Take No For An Answer. I'm your host, Lynda Bennett, Chair of the Insurance Recovery Practice here at Lowenstein Sandler. And I'm joined by my co-host and partner, Eric Jesse. Good to see you again, Eric.
- Eric Jesse:** Glad to be here.
- Lynda Bennett:** All right. And today it's All Home Week for Lowenstein Sandler. We're very pleased to invite to the show Marita Makinen, who is Chair of our M&A practice. So Marita, thanks for joining us today.
- Marita Makinen:** Hi everyone. Glad to be here.
- Lynda Bennett:** All right. So today we wanted to invite Marita on the show because there's been a lot of volatility in the M&A and private equity deal space, and there's an equal amount of volatility in the reps and warranty insurance space. So we want to talk about where the issues are in both of those spaces and how they're intersecting. And what we see is we're just about to drop this episode in early June, what the second half of 2023 is going to look like for us. So Marita, let me kick it over to you to start us off here today and talk about what's the current state of play with respect to deal flow? What's it been up to this point in the year?
- Marita Makinen:** Well, I think the first half of 2023, we've all been kind of trudging through the desert, looking for the oasis, looking for water somewhere. And I think it's been a common issue across a lot of different sectors. I think the middle market has been faring a little bit better than the large cap market. Basically, any deal that needs financing in any form has been slow to come together. But I think as we're rounding the corner on mid-year, we can see the end of the desert on the horizon. And there's some glimmers of hope. People are starting to talk more about deals. We're seeing more term sheets, more LOIs, and I think people are seeing where there might be some opportunities as the

economy is stabilizing to do deals maybe if not right this minute, then in the near future. And I think we're definitely seeing probably an end to the dry spell, I'm hoping by the end of the year.

**Lynda Bennett:** That's great to hear. And you touched on a little bit, some of the drivers behind why flow was a bit slower. For those deals that have gone forward in 2023, what are you seeing in terms of deal value? And again, keeping the point of reference of the last couple of years before this dry spell came along, it was pretty much a go-go market. What are you seeing in terms of deal values now?

**Marita Makinen:** Well, I think lack of stability in the markets has made it harder for people to make big bets. Without the stability it's harder to reach alignment on valuations, particularly for sellers who are really expecting a lot. So I think, again, the middle market has been stronger. Areas like equity investing have been a little bit stronger and any deals that don't need financing have been a little bit stronger. So I don't know if I would characterize it exactly that the larger deals aren't getting done, but the smaller deals are because both of those categories of deals can get done if there's financing available. But again, bigger bets are harder in a volatile market. And so you do see more of an emphasis on the middle market.

**Eric Jesse:** Marita, your point on valuation or the instability and the impact on valuation is well taken. So are you seeing a lot more deals or is the market seeing a lot more deals where the purchase price or there's a contingent payment or an earn-out, has that crept up?

**Marita Makinen:** I think that's a phenomenon we've seen over the last probably three to five years, people maybe a little bit more frequently reaching for earn-outs. And I think that was because it was such a hot market. I think a lot of buyers were hesitant about valuations and so wanted to back-end some of that in an earnout. I think you see kind of some of the same reactions if you're dealing with a volatile market or an environment with uncertainty. So, I'm not sure that it's really trended up or trended down, but it's still a factor.

**Lynda Bennett:** So that's one potential change. Are you seeing any lessons learned on current deals that are in the market as a result of that incredibly hot market? I mean, I still remember all of us being up into the wee hours of the night because every deal needed to close seemingly within 48 hours. Are there any lessons that are coming out of that very white-hot market and what's in the market right now?

**Marita Makinen:** Well, look, I think when valuations are super high, where people feel like they're super high, people really want to make sure they're getting what they're paying for and that there are no unexpected surprises. And so I think the high valuations led to a couple of things, which I think are continuing and we'll see if they get adjusted as a result of what the market is going to be going forward.

One thing is that sellers were really insisting on limited recourse or no recourse deals at the same time that they were insisting on high valuations. And this put a lot of pressure on due diligence throughout that kind of white-

hot market period because people knew that they were signing up for a limited recourse deal. They knew they were paying a really fulsome valuation and they didn't want to get burned. And then I think in addition, the fact that you had rep and warranty insurers most often now also participating in the diligence process, that created further incentives for careful diligence. And so I think in terms of lessons learned, I think people are very focused on diligence, even buyers that maybe in the past were only focused on a couple of different areas of diligence are now I think focused on a larger number of areas and a larger number of issues. And I think that will continue and we'll see what happens to limited recourse. If the market softens up, we'll see how that continues, but I think people are going to continue to hound for the limited recourse deals.

**Eric Jesse:** I was going to say on the diligence front, are there any major diligence areas that are coming up that you're seeing any areas that buyers are probing much harder than they used to?

**Marita Makinen:** Well, I think financial and accounting diligence has always been a hot topic. I think that's continuing. I think cyber and privacy has been an area of focus for a number of years now, so I'm not sure if it's new, but it's certainly continuing to be an area where there's a high level of focus. I think sanctions compliance and having good compliance policies at a target company has been a big area of focus because the world is getting more and more complicated in terms of international relations. And I think that's something that people are very focused on and want to make sure that everyone who should be in compliance is in compliance.

**Lynda Bennett:** So Marita, are there any particular sectors, as I mentioned at the top, we're just about to start the second half of 2023. Are there any particular sectors that you think will be hot in the second half of the year?

**Marita Makinen:** Well, everyone's talking about AI. We'll see how that bears out in deal activity, but I would assume that you're going to see a lot of people investing, at least in AI, continuing to. I suspect that although I hear we're in a crypto winter, I suspect that crypto will see a resurgence of sorts as the year goes along. And then I think there's some industries that you're going to see maybe consolidation or opportunistic deal making just given what's happening in the market. Financial services, retail are a couple of sectors that come to mind. And then cross border deals. People are talking a lot about what areas of the world, maybe hot areas to invest in, in the coming years. India is coming into focus a little bit more. China I think is still very important to people, but I think India is growing and so that'll be an interesting one to kind of watch for the future.

**Eric Jesse:** Are there any types of transactions that have or are gaining strength or becoming more prominent in the current market, in the desert, whether it's minority deals or GP secondaries? I know you said mid-market deals that don't require financing are going along. What are you seeing there?

**Marita Makinen:** I think in terms of thinking about what types of deals are more resilient in bad markets, we've talked about middle market, that's certainly a more resilient sector usually. I think same thing with maybe late stage minority investing.

That, I think, is potentially a resilient market, although there's been a little bit of desert in that as well. And then in terms of buyer types, strategics are generally more resilient in this type of market. They may have been waiting a little bit while the valuations were so high and maybe we'll see more opportunities in the upcoming year or so. Those are all things that we're watching.

**Lynda Bennett:** Marita, you mentioned before, cyber and privacy, and basically just keeping track of your data becoming an area that's getting greater diligence. Are you also seeing just a greater focus on the wording of the representations with respect to that kind of issue?

**Marita Makinen:** That's always evolving, and it seems like our reps and warranties always keep getting longer and more detailed because people want to make sure they're covering everything, that it's kind of clear that they're covering everything that they want to be covering. So I don't know that there's anything too new on that, but I think sellers are focusing on exclusions and materiality qualifiers and things like that. But I think that's kind of a continuation of what we've seen in the past.

**Lynda Bennett:** And I have the same question with respect to another seemingly very hot issue right now generally, which is ESG. So is that an area that's also getting greater diligence and greater attention with respect to the words on the page for any representations being made with respect to ESG issues?

**Marita Makinen:** Well, I think a target company's policies and practices are very important, and you are seeing more representations about those policies being in place. I think it's particularly important in deals where you have strategics because a lot of the strategics have their own environmental standards, human rights policies, supply chain policies, and they want to make sure that the company that they're buying isn't out of line with their own policies. So I think that has been an area of more emphasis, to a lesser degree in most cases, I think when you're looking at just pure financial investors, although I do think that that market will continue to evolve and ESG questions are going to become more common over time.

**Eric Jesse:** So Marita, what are you seeing with respect to reps and warranty policies? Is that still an important term in the bidding process? Are sellers still expecting them? Are buyers willing to accept them? Are you seeing any pushback? What are you seeing there?

**Marita Makinen:** Well, look, I think in competitive auction processes, and particularly, the larger deals in the larger cap markets, it's even more standard. But rep and warranty insurance has become standard in deals of a wide size range today, and I don't think that's going to change even if the market is a little softer for the sellers. I think sellers need to continue to make it clear that when they start a process, it's kind of in their process letter to say that they're expecting a limited recourse deal and they're expecting buyers to come to the table in their bid with a policy or with an indication of a policy.

And I think on the buyer's side, buyers need to make it clear that they're expecting coverage, indemnification coverage, like good old traditional, put

some money in an escrow coverage for matters that aren't covered by a rep and warranty policy. Because I'm sure as you've seen, the insurers, once you find a problem, it's going to be excluded from the policy. And I think from a buyer perspective, you want to make sure you're going to get some coverage for that, even though the policy's not going to cover it because it's a known issue. And if there's a softening in the market, I think you're going to see maybe a little more set aside in those traditional, old-fashioned, put the money in an escrow type pots of money. But those, I still think it'll be limited to things that the rep and warranty policy is not covering, and I don't see rep and warranty insurance going away really.

**Lynda Bennett:** Well, we hope not Marita, that's for sure. But really appreciate you sharing your insights today because I think you've laid the groundwork for us beautifully to pick up this discussion next time because as you mentioned, there was a lot of activity for a couple of years, things cooled off over the last year or so. And it seems as though certainly the M&A and PE stakeholders have taken a breath and started to maybe modify their process a little bit. We're expecting that the insurers are going to do the same kind of thing, and we're certainly encouraging them to do that. Right, Eric? So this has really been a terrific discussion and provided a wonderful overview of what's to come in the second half of 2023. We'll look forward to having you back in January, Marita, to see if all of your predictions have come true. But thanks for joining us today.

**Marita Makinen:** Thanks for having me. Good to talk to you.

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