Earn-Outs and Reverse Earn-Outs

During the pandemic there was an “increased focus on earn-out provisions as a method to mitigate the risk of a target’s post-closing under-performance and to bridge any valuation gap between the purchaser and seller,” writes Kiri Buchanan in ***Norton Rose Fulbright’s Deal Law Wire***.

In this post they focus on “(i) reverse earn-out provisions and (ii) a review of the use of earn-outs in 2020 M&A deals.”

“…a ‘classic earn-out’ refers to a post-closing increase in the purchase price based on the achieving of certain performance targets, while a ‘reverse earn-out’ refers to a decrease in the purchase price if the performance targets are not achieved. For greater clarity, in a reverse earn-out scenario, the purchaser pays the maximum amount for the target at closing and if the agreed upon performance targets are not met, the vendor must re-pay an agreed portion of the purchase price, reducing the overall price of the target. Reverse earn-outs are used less often because the risk resides with the buyer, rather than the seller.”

Read the post.