

# Earnout Structuring Matrix

Practitioner reference for designing earnouts across LMM M&A; deal scenarios

## Why earnout structure matters

Earnouts in lower middle market M&A; pay materially less than the headline suggests. Per SRS Acquiom analysis, realistic expected value of an LMM earnout is between 30% and 60% of the headline amount. The structure determines which side of that range the seller ends up on. This matrix maps earnout structures to deal characteristics, with the trade-offs each structure carries for both seller and buyer.

**The 30% rule:** If the earnout is more than 30% of total deal consideration, the seller is functionally financing the buyer at zero interest. Maximize base, minimize earnout.

## Matrix 1: Earnout metrics — structure, manipulation risk, and seller protection

| Metric                  | Manipulation risk | Seller-friendly?   | Use case  |
|-------------------------|-------------------|--------------------|---|
| EBITDA target           | HIGH              | Weak               | Common but risky; cost allocation games hurt seller       |
| Revenue target          | MEDIUM            | Better than EBITDA | Harder to manipulate but recognition timing still a lever |
| Customer retention      | LOW               | Strong             | Best for retention-driven businesses (services, SaaS)     |
| Specific milestones     | LOW               | Strong             | Product launches, regulatory approvals, contract awards   |
| Synergy realization     | HIGH              | Weak               | Strategic deals; buyer controls integration tightly       |
| Cumulative gross profit | MEDIUM            | Better than EBITDA | Excludes operating cost allocation issues                 |

## Matrix 2: Recommended earnout structures by deal scenario

| Deal scenario                       | Recommended metric                      | Period   | Rationale   |
|-------------------------------------|---|----------|---|
| PE platform acquisition             | Customer retention or revenue           | 12-24 mo | PE will operate aggressively; EBITDA-based earnouts hurt seller |
| Strategic acquirer (synergy thesis) | Specific milestones tied to commitments | 18-36 mo | Tie buyer's stated synergies to seller's earnout payment        |
| Family office / holding co.         | Smaller earnout or skip                 | 12-24 mo | Patient capital; less need for earnout bridge                   |
| Search fund / individual buyer      | Customer retention + seller financing   | 24-36 mo | Operator-CEO model; retention is the operating thesis           |
| Healthcare services                 | Revenue or payer-mix milestones         | 18-36 mo | Regulatory and reimbursement risk; retention metrics softer     |

|                              |  |          |   |
|------------------------------|--|----------|---|
| <b>SaaS / software</b>       | ARR retention or NRR                     | 12-24 mo | Recurring revenue model rewards retention metric                |
| <b>Manufacturing</b>         | Customer retention or specific contracts | 18-24 mo | Volume commitments and customer relationships matter most       |
| <b>Professional services</b> | Partner retention + revenue              | 24-36 mo | Customer concentration tied to partners; retention drives value |

### Matrix 3: Required seller protections by earnout structure

| Protection                    | EBITDA earnout | Revenue earnout | Customer retention | Milestone     |
|-------------------------------|----------------|-----------------|--------------------|---------------|
| Detailed methodology in PA    | Critical       | Critical        | Important          | Important     |
| Floor structure (partial pay) | Critical       | Critical        | Important          | Optional      |
| Anti-dilution provisions      | Critical       | Important       | Less critical      | Less critical |
| Audit rights for seller       | Critical       | Important       | Important          | Optional      |
| Acceleration on buyer sale    | Critical       | Critical        | Critical           | Critical      |
| Cap on add-back disputes      | Critical       | Less critical   | N/A                | N/A           |
| Cost allocation specification | Critical       | Less critical   | N/A                | N/A           |
| Specific accounting policies  | Critical       | Important       | N/A                | Important     |

### Sell-side negotiation playbook for earnout terms

- 1. Maximize base, minimize earnout.** The 30% rule: keep total earnout under 30% of consideration.
- 2. Choose your metric carefully.** Customer retention > revenue > EBITDA. Milestone earnouts work for strategic deals.
- 3. Lock methodology in the LOI.** Don't accept 'to be determined in purchase agreement' on calculation methodology.
- 4. Demand floor structure.** Earn partial earnout at 80% of plan, full at 100%, super at 110%.
- 5. Negotiate anti-dilution.** Buyer can't shift corporate costs into the acquired business to engineer EBITDA targets.
- 6. Insist on audit rights.** Seller can audit the books during the earnout period to verify calculation.
- 7. Acceleration on buyer sale.** If the buyer sells the business before the earnout ends, full earnout becomes payable.
- 8. Specific cost allocation rules.** Define how parent corporate costs, shared services, and TSA costs are allocated.
- 9. Defined accounting policies.** Specify which accounting policies apply (seller's historical, buyer's, or specified hybrid).
- 10. Reasonable best efforts clause.** Buyer commits to operating the business in good faith to support earnout achievement (limited but useful).

## Notes and references

**The 30%-60% reality:** Per SRS Acquiom analysis, LMM earnouts pay materially less than the headline suggests. Realistic expected value lands between 30% and 60% of headline amount depending on structure. EBITDA-based earnouts skew toward 30-40% paid; customer retention earnouts skew toward 60-80% paid; milestone earnouts vary widely.

**This matrix is a starting point, not deal advice.** Every earnout is a negotiation. Use this matrix to anchor the conversation, not to dictate terms.

### Companion content:

- Earnout structure pillar: [lockroom.com/blog/earnout-structure-lmm-ma](https://lockroom.com/blog/earnout-structure-lmm-ma)
- LMM buyer landscape: [lockroom.com/blog/lmm-buyer-landscape-2026](https://lockroom.com/blog/lmm-buyer-landscape-2026)
- Sell-side QofE (drives earnout EBITDA methodology): [lockroom.com/blog/sell-side-qofe-2026](https://lockroom.com/blog/sell-side-qofe-2026)
- Customer concentration: [lockroom.com/blog/customer-concentration-cim-2026](https://lockroom.com/blog/customer-concentration-cim-2026)
- LMM 2026 outlook: [lockroom.com/blog/lmm-ma-2026-outlook](https://lockroom.com/blog/lmm-ma-2026-outlook)

### External references:

- SRS Acquiom Deal Terms Study (latest edition) — earnout prevalence and outcomes
- ABA M&A; Committee — earnout drafting conventions
- Capstone Partners — practitioner commentary on earnout outcomes