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# The Post-Close Money Trap: Why Earn Out and Escrow Deserves the Same Scrutiny as Purchase Price

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Post-closing disputes are a common feature in business acquisitions. This article addresses two areas that practitioners should consider carefully when negotiating and drafting a private company purchase agreement to avoid surprises and needless litigation after closing: earn-outs, and the loss triggers that govern claims against an indemnification escrow. For each, the outcome of post-closing litigation under Delaware or New York law often turns on the precision of the drafting.

## Earn-Outs

Earn-outs are common in business sales for multiple reasons; they bridge valuation gaps, share risk and align incentives, help retain key employees, and/or reduce the buyer's upfront cash requirement.

Delaware and New York take approach earn-outs similarly, although Delaware has a richer body of case law given the Court of Chancery's expertise in M&A litigation. Delaware courts enforce the contract as written and will not impose obligations beyond those the parties negotiated. The parties should therefore consider express operating covenants that govern the earn-out period, such as commitments to retain key employees and distributors or maintain specified promotional and marketing spend, which give the seller greater security and continuity.


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Absent such covenants, the central question governing the earn-out is whether the buyer's post-closing conduct is governed by an express efforts covenant, the implied covenant of good faith and fair dealing, or only a prohibition on intentional acts to avoid reaching the earn-out threshold before the target date. Agreements often include a non-circumvention clause, and the key drafting choice is whether it prohibits "intent" to frustrate the earn-out or applies to a different standard, such as good faith, "commercially reasonable efforts" or "best efforts."

Where the agreement requires commercially reasonable efforts, Delaware courts apply it rigorously according to its negotiated language including any parameters the parties included to govern that standard. *Johnson & Johnson v. Fortis Advisors LLC*. Where the agreement seeks a heightened standard, such as "commercially best efforts", the parties are best served to define it rather than relying on blunt judicial interpretation. *Menn v. ConMed Corp*.

Where the agreement prohibits only bad faith or intentional circumvention, the buyer has far greater latitude, and the seller bears a heavier burden. In *Lazard Tech. Partners, LLC v. Qinetiq N. Am. Operations LLC,*, the Delaware Supreme Court held that the implied covenant cannot displace the express standard the parties chose, which required the "well-understood concept" of intent to deprive the seller of an earn-out payment. That need not be the buyer's sole intent, but its conduct must be intentional. Nor does the buyer have an implied duty to maximize earn-out payments; it need only refrain from deliberately shifting revenue out of the earn-out period. *Winshall v. Viacom Int'l, Inc.*.

New York offers more generalized guidance but takes a similar approach, implying a covenant of good faith and fair dealing in every contract unless expressly precluded. New York courts are reluctant to find a breach absent evidence that the buyer acted in bad faith or took deliberate steps to prevent the earn-out; mismanagement alone is not enough, and courts will not impose a duty to maximize the earn-out that the contract does not require.

Earn-out disputes also frequently involve projections or assurances given outside the purchase agreement, typically to reassure the seller that the earn-out will easily be met. These give rise to fraudulent inducement claims, in which a party alleges it was induced to enter the agreement by materially false extra-contractual representations. Under Delaware law, two issues predominate: first, whether an anti-reliance provision bars claims based on representations outside the agreement; and second, whether the statement was mere puffery or was known to be materially false when made, for example because the speaker had contemporaneous information showing it was untrue. Parties may disclaim reliance on extra-contractual representations, but only through unambiguous anti-reliance language; a standard integration clause is not enough. *Abry Partners V, L.P. v. F & W Acquisition LLC*, . The Delaware Supreme Court has since held that an exclusive remedy provision, standing alone, cannot operate as an anti-reliance clause, *Johnson & Johnson v. Fortis Advisors LLC*, 352 A.3d 229 (Del. 2026), and that a party cannot invoke an anti-reliance clause obtained by another party for its own benefit. *Paragon Metals Holdings LLC v. Smith,* where the agreement pairs an integration clause with an exclusive representations clause expressly identifying the representations on which the buyer relied, Delaware courts will enforce the combination to bar extra-contractual fraud claims. *Prairie Cap. III, L.P. v. Double E Holding Corp.*.

New York's approach is simpler: a specific disclaimer of reliance will preclude a fraud claim, but a general merger clause will not. *Danann Realty Corp. v. Harris,; Laduzinski v. Alvarez & Marsal Taxand LLC*.

**Loss Triggers in Escrow Agreements**

A second pitfall is the definition of "Loss" in an escrow securing post-closing indemnification claims. Litigation commonly turns on what event suffices to support a claim on the escrow and when that claim is ripe. The central issue is whether the definition requires actual, incurred loss or permits claims for future, potential, contingent exposure. The stakes can be considerable. If a mere potential claim, such as receipt of a customer complaint, suffices, the buyer may tie up the holdback for an extended, indeterminant period far-longer than the original agreed-to holdback. This can be significant depending on the escrow's size relative to the total deal consideration.

The parties should therefore state clearly whether the buyer may claim against the escrow for contingent, unmatured, or anticipated liabilities, which can support claims for nearly anything, or only for actual, incurred, out-of-pocket payments. Delaware and New York will both enforce the bargain struck. Where "Losses" are defined to include liabilities that are "contingent, unknown and unmatured," courts will allow a party to notice and preserve a claim for an obligation not yet quantified or paid, provided the notice identifies the claim with reasonable specificity.

Delaware has a large, disparate body of law on this issue. One court seeks to reconcile it by distinguishing the buyer's *ultimate right to receive an indemnification payment*, which requires an actual defined "loss," from its *ability to assert a claim sufficient to hold escrow funds pending resolution*, which may rest on claims or facts that could give rise to a "Loss." *Rex Medical, L.P. v. Argon Medical Devices, Inc.*.

Notably, in *Rex Medical*, dozens of lawsuits had already been filed that could produce actual Losses. The court distinguished decisions requiring a more exacting showing of Losses, including *Kilcullen v. Spectro Sci., Inc.* and *Hill v. LW Buyer, LLC*.

New York law is similar in its treatment of the definition of Losses, *VXI Lux Holdco S.A.R.L. v. SIC Holdings, LLC*, but emphasizes strict compliance with the contract's notice provisions, including specificity in describing the basis for the claim. *Orbimed Advisors, LLC v. QVT Fund LP*.

**Conclusion**

In both areas, courts in Delaware and New York will hold the parties to the words they chose. Vague efforts standards, boilerplate integration clauses, and loosely defined loss triggers do not resolve disputes; they defer them to the courtroom. Vigilance and precision at the drafting table is the most effective, and least expensive, protection against post-closing litigation.

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