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LEGAL UPDATES

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Michigan Issues Updated Guidance on Successor Liability

Services

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The Michigan Department of Treasury recently issued updated guidance addressing successor liability in response to *Mertz v. Dep't of Treasury* [Dkt. No. 365480 (June 13, 2024)], a recent case before the Michigan Court of Appeals. While the bulk of the case discussed the correct application of the "responsible person" law, the analysis was in the context of successor liability. Specifically, the *Mertz* court held that Michigan requires the Department to have sufficient knowledge of the purchaser's identity to initially assess the purchaser of the business before pursuing a "responsible person."

This case and the updated guidance reaffirm the importance of a purchaser obtaining tax clearances as part of the closing of a transaction. The Department is required to assess the purchaser first. Thus, if a tax clearance certificate is not obtained, a purchaser should separately obtain reimbursement under indemnity clauses from the seller.

Avoiding successor liability

Many states hold purchasers of businesses or parts of businesses liable for taxes owed by the selling business in certain circumstances, under the concept of "successor liability." States often assert "successor liability" against a purchaser to encourage parties to pay any delinquent taxes prior to the sale of the business.

Michigan's successor liability laws allow an assessment of a purchaser, including a purchaser who only purchases some portion of a business's assets. To the extent that a purchaser acquires less than an entire business, that purchaser may only be liable up to the fair market value of the property purchased.

To avoid successor liability, a purchaser should either escrow sufficient money to cover the amount of taxes, interest, and penalties as may be due and unpaid until it receives a receipt from the treasurer showing the taxes due are paid or obtain a certificate from the Department of Treasury stating that taxes are not due (a "tax clearance certificate"). Because successor liability is a derivative liability, the successor is unable to challenge the underlying assessment. Furthermore, successor liability can be assessed for tax liabilities that are both known and unknown at the time of the purchase of the business. As such, liabilities not identified during due diligence and that become known after the close could fall on the unprepared purchaser and such successor liability could be significant.

The Department is statutorily required to assess a successor prior to assessing any corporate officer as a "responsible person" if the Department has information that identifies the successor and determines that assessment of the successor would allow the Department to collect the entire assessment of the business.

What this means to you

Parties negotiating an acquisition of a business or considering such, should obtain tax clearance certificates in applicable jurisdictions, as part of closing the transaction lest it be burdened with unknown tax liabilities of the previous owner. Furthermore, parties should consider indemnification clauses to address these potential successor liability issues.

Contact us

Please reach out to Smitha Chintamaneni, Bill Schenkelberg, or a member of Husch Blackwell's State & Local Taxation (SaLT) team for assistance in understanding successor liability risks and mitigation options.