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Successor Liability Can Snare the Unsuspecting Purchaser of Assets

Many businesses are finding that the current economic climate presents favorable opportunities for business acquisitions. State sales and use tax liabilities are a frequently overlooked, but critical, element of any acquisition.

A primary motive for choosing an asset purchase rather than a stock acquisition is to avoid succeeding to the liabilities of the target. However, state tax statutes typically make a buyer of assets liable for the seller's liability for unpaid sales and use taxes, and sometimes corporate tax liabilities, unless the buyer satisfies the requirements set forth in the particular state's successor liability statute. The only limitation is the full purchase price.

Connecticut, Massachusetts, New York, and Rhode Island have specific statutes governing the liability of a buyer for a seller's unpaid sales and use taxes. While each state has its own unique requirements, the uniform premise is that a buyer is liable for all of the seller's past sales tax liabilities unless a tax clearance letter or escrow letter is obtained. Unless and until the applicable state revenue authority acknowledges that there are no outstanding liabilities, the buyer remains on the hook for the seller's unpaid taxes.

Successor liability statutes differ in the designation of the party required to obtain the certificate, the specific method of making a request, the length of time required by the revenue authority to issue a tax clearance letter or certificate, and the types of taxes covered.

In Connecticut, for example, the purchaser of the assets of a business is liable for the seller's unpaid sales and use tax liabilities unless the purchaser has obtained a tax clearance certificate from the Connecticut Department of Revenue Services (DRS) indicating that the seller owes no sales and use taxes.¹ A purchaser that does not obtain a certificate from the DRS is liable for any of the seller's sales and use tax liabilities up to the full purchase price of the assets unless it withholds a sufficient amount from the purchase price to cover these liabilities.

The Massachusetts successor liability statute operates in much the same manner as Connecticut's but includes as liabilities both the corporate excise tax and the sales and use taxes. New York and Rhode Island also apply successor liability to both corporate tax and the sales and use taxes.

¹ The purchaser may also have to obtain a comparable clearance letter from the Connecticut Department of Labor stating that the seller has also satisfied its unemployment compensation obligations.

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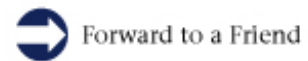
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