



DID YOU KNOW?

Did you know that you should include a “push out election” when you buy a LLC?

Generally, pre-closing income tax liabilities are not a big concern for the buyer of LLC interests, since the income of LLCs (taxed as partnerships) is not a liability of the LLC but its selling partners. Under the “new” (effective 2018) partnership audit procedures, any tax liability arising from an audit of a partnership (LLC) must be paid by the LLC itself unless it makes a “push out” election causing the selling members to pay the tax. Therefore, an audit of a pre-closing tax year could result in tax on the partnership itself.

Membership interest purchase agreements (MIPAs) typically provide that a seller cannot settle an audit without the buyer’s consent. However, the settlement merely establishes the amount of income and tax. MIPAs also typically provide that the buyer cannot make tax elections with respect to pre-closing tax years (without sellers’ consent), so the buyer is prohibited from making the push out election for the audited year. A buyer may be able to bring an indemnity claim for the tax due, but the alternative of making a push out election and letting the IRS pursue and collect the tax directly from the sellers is vastly more desirable.

In this era of transaction rep and warranty insurance, this issue may be less critical to the buyer in an insured deal. As seller’s counsel, it would certainly make sense to take the position that the buyer does not need the right to make a push out election because any LLC tax liability resulting from an audit would be covered by insurance. This may be true, although a prudent buyer will check the terms of its rep and warranty insurance policy before agreeing on that point.

Bottom Line: Buyers of LLCs will want to negotiate the right to make a push out election for taxes relating to pre-closing tax years (unless perhaps there is rep and warranty insurance to cover it). If you have any questions, please contact the author or one of Taft’s Tax attorneys.



[Jim Duffy](#) / (612) 977-8626 / jduffy@taftlaw.com

All overnight success takes about 10 years. – Jeff Bezos