No. 02-1389

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

ABEL COSMO GALLETTI AND SARAH GALLETTI;
FRANCESCO BRIGUGLIO AND ANGELA BRIGUGLIO

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

REPLY BRIEF FOR THE PETITIONER

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1. This case was brought by the United States in bankruptcy court to enforce the derivative liability of the individual partners for the tax debt of their partnership. Because respondents had filed for bankruptcy, the United States was barred by the automatic stay from bringing suit outside of bankruptcy court to enforce this derivative liability. 11 U.S.C. 362(a)(1). When the government asserted its claims in the bankruptcy proceedings (11 U.S.C. 501(a)), respondents exercised their right to object to the allowance of the claims (11 U.S.C. 502(a)). After such objections are filed, the bankruptcy court is to determine the validity and amount of the government's claim "after notice and a hearing." 11 U.S.C. 502(b). The adjudication and determination of a disputed claim in a bankruptcy case constitutes a judgment with res judicata effect. See,

e.g., *Siegel* v. *Federal Home Loan Mortgage Corp.*, 143 F.3d 525, 528-529 (9th Cir. 1998); *In re Baudoin*, 981 F.2d 736, 742 (5th Cir. 1993).

Such proceedings in bankruptcy court obviously comport with the requirement of California law that there be a "judgment against the partner" before the liability of a partnership may be collected "from a partner's assets" (Cal. Corp. Code § 16307(c) (West Supp. 2003)). Respondents' strained assertion that a bankruptcy case may not proceed against the partners because California law requires that "a judgment against the individual partner" be obtained before collection of the partnership debt occurs (Br. in Opp. 4) is transparently circular and manifestly incorrect. The extraordinary breadth of respondents' contention is noteworthy. If respondents new argument were accepted, the derivative liability of a partner for *any* type of partnership debt could never be enforced for, on respondents' theory, the partner could simply commence a bankruptcy case and thereby preclude the entry of any judgment in a pending suit or any recovery on the claim thereafter filed in bankruptcy. There is obviously no support for that broad proposition, and respondents cite none for it.

The question presented in the petition is whether, in order to enforce the derivative liability of partners for the tax debts of their partnership, the United States must, as a matter of federal law, make a separate assessment of the taxes owed by the partnership against each of the partners directly. As is explained in the petition (Pet. 15-16), the California statutes cited by respondents do not address or purport to govern that question of federal tax administration.

2. Respondents also err in their asserted reliance (Br. in Opp. 7-8) on *Jersey Shore State Bank* v. *United*

States, 479 U.S. 442 (1987). That case addressed a narrow question under Section 3505 of the Internal Revenue Code, which creates a liability for lenders who (i) pay wages to the employees of borrowers and (ii) do not withhold required amounts of federal employment taxes from the wages paid. 26 U.S.C. 3505(a). That liability is created by federal statute, and it does not rest on general principles of derivative liability. The question addressed in *Jersey Shore* was whether, as a prerequisite to enforcing this statutory liability of the lender, the United States must provide *the lender* with a notice of the assessment for employment taxes that was *issued to the employer*. The Court held that notice of the assessment issued to the employer need not be sent to the lender as a condition of enforcing the separate statutory tax liability of the lender. 479 U.S. at 447-449.

Nothing in that decision supports respondents' assertion that assessment is "generally required" to enforce a "derivative liability" (Br. in Opp. 7). To the contrary, the decisions of this Court and of other courts of appeals have consistently held that the derivative liability of a third party may be enforced based on the assessment of the primarily liable party and "without assessment" of the tax against the party whose liability was only derivative. *Leighton* v. *United States*, 289 U.S. 506, 508 (1933); see cases cited Pet. 11-16.

3. Respondents nonetheless assert that the conflict among the courts of appeals that is created by the decision in this case is only "illusory" (Br. in Opp. 9). In making that contention, respondents simply fail to acknowledge that the decision in this case directly conflicts with the longstanding holding of the Federal Circuit that a separate assessment is *not* required to collect a tax from a party who is derivatively liable for

it. *Anderson* v. *United States*, 15 F. Supp. 216, 225 (Ct. Cl. 1936), cert. denied, 300 U.S. 675 (1937); see Pet. 11-13.

For the reasons set forth in detail in the petition (Pet. 12-17), respondents also err in their effort to minimize the conflict with other circuit decisions. For example, respondents incorrectly state that the record in *United States* v. *Wright*, 868 F. Supp. 1070 (S.D. Ind. 1994), rev'd, 57 F.3d 561 (7th Cir. 1995), showed that "assessments were made against the partners as well as the partnership" (Br. in Opp. 11). On the contrary, the government maintained in *Wright* "that the assessments were levied against the partnership only and not against any of the partners individually." 868 F. Supp. at 1071 n.1. The district court in *Wright* stated that whether an assessment was made against the partners was "not material" to its resolution of the case. *Ibid*. And, as noted in the petition (Pet. 16 n.9), the Seventh Circuit in *Wright*, in a holding that directly conflicts with the decision in this case, expressly held that "suits against persons derivatively liable for taxes are timely, or not, according to the rules for timeliness of suits against taxpayers." 57 F.3d at 564.

Respondents also completely miss the point of *United States* v. *Botefuhr*, 309 F.3d 1263 (10th Cir. 2002). The decision in that case did not turn on the fact that the liability of the donee under 26 U.S.C. 6324(b) was limited to the value of the gift. Instead, it turned on a straightforward application of the legal principle that a "suit [that] would be timely [if] brought against the" primarily liable taxpayer is also "considered timely against the [derivatively liable] donee or transferee." 309 F.3d at 1277.

4. Respondents do not dispute that the conflict that now exists among the circuits will cause improper "ine-

qualities in the administration of the revenue laws." *Commissioner* v. *Sunnen*, 333 U.S. 591, 599 (1948). Partners who happen to reside in different circuits will receive different treatment based solely on the location of their residence. Resolution of the conflict among the circuits created by the decision in this case is thus warranted by the importance, in a national system of taxation, of "ensur[ing] as far as possible that similarly situated taxpayers pay the same tax." *Thor Power Tool Co.* v. *Commissioner*, 439 U.S. 522, 544 (1979).

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For the reasons stated above and in the petition, the petition for a writ of certiorari should be granted.

THEODORE B. OLSON
Solicitor General

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