No. 07-1049

# In the Supreme Court of the United States

LAROSA'S INTERNATIONAL FUEL CO., INC., ET AL., PETITIONERS

*v.*

UNITED STATES OF AMERICA

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

**BRIEF FOR THE UNITED STATES IN OPPOSITION**

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## QUESTION PRESENTED

Whether interest accrued on petitioners' tax liabilities under 26 U.S.C. 6601, after the Internal Revenue Service levied upon petitioners' assets, where the levied assets were not applied to petitioners' tax obligations, but were instead placed in escrow pending judicial resolution of petitioners' tax liabilities.

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## OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 2-22) is reported at 499 F.3d 1324. The opinion of the Court of Federal Claims (Pet. App. 23-28) is reported at 56 Fed. Cl. 102.

## JURISDICTION

The judgment of the court of appeals was entered on September 18, 2007. A petition for rehearing was denied on November 15, 2007 (Pet. App. 1). The petition for a writ of certiorari was filed on February 13, 2008. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

**STATEMENT**

1. Petitioner LaRosa's International Fuel Co., Inc. (LaRosa's International), is a Maryland corporation in the business of supplying coal to utility companies. Pet. App. 7. Petitioner Joseph LaRosa is a shareholder of LaRosa's International and his brother, Dominick LaRosa, who is not a party to this litigation, is its president. *Ibid.* In December 1985, the Internal Revenue Service (IRS) made jeopardy assessments against petitioners and Dominick LaRosa (collectively the LaRosas), totaling more than $21 million in taxes, penalties, and interest for the tax years 1981 through 1983. *Ibid.* Immediately thereafter, the IRS served notices of levy under Section 6331 of the Internal Revenue Code, 26 U.S.C. 6331 (1982), on financial institutions holding property belonging to the LaRosas. *Ibid.*

In December 1985 and early January 1986, two payments were remitted to the IRS, in the amounts of $169,955 and $114,098. Those amounts were applied to Joseph LaRosa's tax liabilities and LaRosa's International's tax liabilities, respectively. Pet. App. 8. Before additional assets were collected, liquidated, and applied to the LaRosas' outstanding tax liabilities, however, the IRS consented, as an accommodation to the LaRosas, to enter into an escrow agreement in lieu of applying the levied assets against their tax assessments. Gov't C.A. Br. 5-6; Pet. App. 8.

The escrow agreement, executed in January 1986, provided for the LaRosas' property to be held in escrow pending final judicial resolution of the LaRosas' tax liabilities. Pet. App. 8, 16-17, 25. The escrow agreement stated that "[t]his agreement is entered into solely for the purpose of securing the payment of the taxpayers' tax liability and is not to be considered as payment of

such liability." *Id.* at 20. The agreement provided that all monies deposited under the escrow agreement would be invested in certificates of deposit at a federally insured bank or savings and loan, and it further provided that interest would "accrue to the benefit of [petitioners]" and would be "taxable to them." *Id.* at 16-17. Under the agreement, the IRS could not apply any of the escrowed funds to any tax liabilities without consent or until final determination of those liabilities by a court. *Ibid.* Disbursements from the escrowed funds, however, could be, and were, made to the taxpayers to cover certain personal and business expenses. *Id.* at 17 n.5.

After execution of the escrow agreement, the IRS issued notices of deficiency to the LaRosas, reflecting the tax liabilities that were the subject of the jeopardy assessments, and the LaRosas filed petitions challenging the deficiency determinations in the United States Tax Court. Pet. App. 8.[1] In 1991, the IRS and the LaRosas reached an agreement to settle all the Tax Court litigation. *Ibid.* The stipulated decision in Joseph LaRosa's case determined that he was liable for deficiencies and additions to tax totaling approximately $2.3 million. *Ibid.* The stipulated decision in LaRosa's International's case determined that it was liable for deficiencies and additions to taxes totaling approximately $316,000. *Ibid.* The stipulated decisions reserved the LaRosas' rights to pursue an action contesting the amount of interest claimed by the IRS to be due on the agreed deficiency in tax. *Id.* at 9. The LaRosas paid the stipulated deficiencies out of funds other than the funds held in escrow. *Id.* at 8. The IRS then re-

[1] The LaRosas also attempted, unsuccessfully, to set aside the jeopardy assessments in federal district court. See *LaRosa* v. *United States*, 841 F.2d 544 (4th Cir. 1988).

leased the levies and the escrowed assets, together with the interest that had been earned thereon. *Id.* at 9, 25.

In 1993, the LaRosas filed claims for refund with the IRS claiming that they had made excessive interest payments on their settled tax liabilities. Pet. App. 9. They contended that interest should not have accrued against them on those liabilities after December 1985, when the IRS made its jeopardy assessments and served notices of levy, because, they claimed, after that time the IRS had actual or constructive possession of assets in excess of their tax liabilities. *Ibid.* The LaRosas argued that the IRS should have credited the full value of the assets held in escrow against their tax assessments, thereby suspending accrual of underpayment interest, as of 1985. *Ibid.* The IRS denied the refund claims, and suits for refund followed. *Id.* at 9-11 & n.3.

Dominick LaRosa litigated his refund claim in the United States District Court for the District of Maryland as a counterclaim in a suit the government had brought against him to recover an erroneous refund. Pet. App. 11 n.3; see *United States* v. *LaRosa*, 993 F. Supp. 907, 912-913 (D. Md. 1997), aff'd, No. 97-2782, 1998 WL 393976 (4th Cir. July 10, 1998) (unpublished), cert. denied, 526 U.S. 1004 (1999) (*LaRosa I*). The district court rejected Dominick LaRosa's argument that he was entitled to a refund of underpayment interest. The court held that, because the levied assets were placed in escrow rather than applied to satisfy the outstanding tax liabilities, the IRS was relieved of the duty it ordinarily would have had to promptly liquidate noncash assets and apply the proceeds along with the seized funds to pay the tax. *LaRosa I*, 993 F. Supp. at 916-917. The Fourth Circuit affirmed, adopting the reasoning of the district court. *LaRosa I*, 1998 WL 393976.

2. Petitioners LaRosa's International and Joseph LaRosa litigated their refund claims in the Court of Federal Claims, where their cases were consolidated. Pet. App. 9 & 10 n.2. On cross-motions for summary judgment, the court held that petitioners were not entitled to the refunds they sought and granted partial summary judgment in favor of the government. *Id.* at 23-28.[2] The court concluded that the service of notices of levy and the subsequent placement of the funds at issue in escrow could not be characterized as payment of petitioners' tax liabilities. *Id.* at 10, 27-28. The court explained that, in *Rosenman* v. *United States*, 323 U.S. 658 (1945), this Court held that "tax payment occurs when the IRS actually applies funds to a particular tax liability; it is not enough to place funds into a 'suspense' account, or escrow, which merely functions as a surety against the future payment of said liability." Pet. App. 27 (quoting *Rosenman*, 323 U.S. at 662).

3. The court of appeals affirmed. Pet. App. 2-22. The court of appeals held that neither the levy nor the placing of funds in escrow could be treated as a payment that would stop the accrual of underpayment interest on petitioners' outstanding liabilities. *Id.* at 13. The court explained that a levy is a provisional remedy that "merely bring[s] the property into the Service's legal custody," rather than transferring ownership of the property to the IRS, and is not equivalent to payment of tax liabilities. *Id.* at 14 (quoting *United States* v. *Whiting Pools, Inc.*, 462 U.S. 198, 210-211 (1983)). The court thus concluded that the IRS's levy against petitioners

[2] The Court of Federal Claims ruled for petitioners on the government's counterclaim, which asserted that petitioners owed additional interest on unpaid taxes. See Pet. App. 6-7 & n.1. The government did not appeal from that decision.

did not stop the accrual of interest under 26 U.S.C. 6601(a). Pet. App. 16.

The court of appeals further held that no payment had occurred when petitioners' assets were placed in escrow because the agreement clearly stated that the escrow arrangement did not constitute the payment of taxes, but rather was only a security arrangement. Pet. App. 16-20.

**ARGUMENT**

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Accordingly, further review is not warranted.

1. The court of appeals correctly held that petitioners had not made an overpayment of deficiency interest with respect to their tax liabilities and, consequently, were not entitled to their claimed refunds.

Under Section 6601 of the Internal Revenue Code, interest on a tax underpayment accrues from the time the tax was due to be paid until the date the tax is paid. 26 U.S.C. 6601(a). As the court of appeals correctly concluded (Pet. App. 11-21), petitioners' tax liabilities were not paid for purposes of that provision when the IRS levied upon petitioners' assets, because the IRS did not apply the levied assets to petitioners' taxes; rather, at petitioners' request, the IRS placed the levied assets in escrow, with an express agreement that the placing of the assets in escrow was "not to be considered as payment of such [tax] liability." *Id.* at 20. Under the terms of the escrow agreement, the IRS was prohibited from applying any of the escrowed assets to the asserted deficiencies in petitioners' income taxes until there was a final judicial determination of petitioners' tax liabilities.

The cash assets were placed in interest-bearing accounts for petitioners' benefit, and petitioners received distributions from the escrow account to pay for certain living and business expenses. *Id.* at 16-17 & n.5.

2. Petitioners incorrectly contend (Pet. i, 14-15) that the decision below conflicts with this Court's decision in *United States* v. *National Bank of Commerce*, 472 U.S. 713 (1985), and is inconsistent with the rationale of its decision in *United States* v. *Whiting Pools, Inc.*, 462 U.S. 198 (1983). According to petitioners, those cases establish that, once the IRS has levied upon a taxpayer's assets, "the taxpayer is entitled to the benefit of having the value of the levied property applied against the balance of the tax assessment"—at least where the assets in question are cash or cash equivalents. Pet. 14; see Pet. 15. Petitioners' contention glosses over the fact that, as an accommodation to them, the IRS agreed that the assets would be held in escrow instead of being applied against the balance of their tax assessment. The court of appeals' decision to give effect to the escrow agreement is wholly consistent with this Court's cases.

a. Contrary to petitioners' characterization (Pet. 14), this Court's decision in *National Bank of Commerce* does not "squarely address[] the issues involved" in this case. *National Bank of Commerce* addresses a very different question from the one presented here: Whether a bank may decline to honor an IRS levy on a joint bank account on the ground that the bank is uncertain how much of the funds in the levied account belong to the taxpayer as opposed to co-depositors, when the taxpayer has an absolute right to withdraw funds from the account. 472 U.S. at 714-715, 724. The Court answered that question in the negative. *Id.* at 724. In setting out the statutory background of the case, the Court de-

scribed an IRS levy as "creat[ing] a custodial relationship between the person holding the property and the IRS so that the property comes into the constructive possession of the Government." *Id.* at 720. But contrary to petitioners' suggestion (Pet. 14-15), the Court did not suggest, much less hold, that seizure of the levied property, *ipso facto*, constitutes *payment* of taxes owed. On the contrary, the Court recognized that a levy is only a "provisional remedy" that "does not purport to determine any rights to the property," but rather "protects the Government's interests so that rights to the property may be determined in a postseizure proceeding." 472 U.S. at 731 n.15; see *id.* at 721, 731. The court of appeals' decision is consistent with that recognition.

b. Nor is the decision below inconsistent with the rationale of *Whiting Pools*. In that case, this Court held that equipment and other tangible property the IRS had levied upon prior to the filing of the debtor's bankruptcy petition was property of the bankruptcy estate, and that the IRS was therefore required to turn the levied property over to the estate under Section 542(a) of the Bankruptcy Code (11 U.S.C.). *Whiting Pools*, 462 U.S. at 200, 211-212. The Court explained that a levy is a "provisional remedy" that merely brings property into the IRS's legal custody, and that the Internal Revenue Code does not transfer ownership of such property until the property is sold to a bona fide purchaser at a tax sale. *Id.* at 210-211.

Petitioner contends that the "express language" of *Whiting Pools* "strictly limit[s] [its] holding" to the proposition "that a levy on *nonliquid* assets only results in a delay in crediting the levied nonliquid proceeds to the tax accounts." Pet. i (emphasis added). Petitioner argues that the court of appeals in this case thus erred

in citing *Whiting Pools* for the proposition that levies on *liquid* assets do not themselves effectuate payments of tax liability. *Ibid.*; see Pet. App. 14-15.

Although the levied property at issue in *Whiting Pools* was nonliquid property, no "express language" in that opinion draws the distinction between levies on liquid assets and levies on nonliquid assets that petitioners now urge. And in any event, even if it were appropriate to draw such a distinction in determining whether the IRS must turn over levied assets under Section 542(a) of the Bankruptcy Code, see Pet. 16-17 (discussing *United States* v. *Borock* (*In re Ruggeri Elec. Contracting, Inc.*), 185 B.R. 750 (Bankr. E.D. Mich. 1995)), the court of appeals correctly held that there is no basis for drawing such a distinction in determining whether tax has been paid for purposes of Section 6601(a) of the Internal Revenue Code. Pet. App. 15-16. Although the IRS ordinarily does apply levied assets against the taxpayer's tax liability, see 26 U.S.C. 6342(a)(2), a levy does not in and of itself result in the collection of taxes owed—even where the levied assets are cash or cash equivalents. See Pet. App. 15-16 (citing *Stead* v. *United States*, 419 F.3d 944, 947-948 (9th Cir. 2005)). The IRS may instead agree, as it did here, to refrain from applying seized assets to asserted tax deficiencies pending final determination of the taxpayer's liability. Cf. *LaRosa I*, 993 F. Supp. at 916. The rationale of *Whiting Pools* casts no doubt on the court of appeals' decision in this case.

3. Petitioners claim (Pet. 17-21) that the court of appeals' reliance on the escrow agreement conflicts with the Tax Court's unpublished memorandum in *Stone* v. *Commissioner*, T.C. No. 5311-72 (Mar. 30, 1987). The claimed conflict does not warrant this Court's review, see Sup. Ct. R. 10, and is in any event illusory.

In *Stone*, the Tax Court held that interest on tax liabilities stopped accruing as of the date that the IRS levied on bank accounts and an escrow account, even though the IRS did not receive the funds until much later, because, following the levy, the IRS had constructive possession of the assets and could have demanded payment at any time. *Stone*, *supra*, slip op. at 4-5. As the court of appeals correctly noted, *Stone* "does not help" petitioners for two reasons: First, the Tax Court's decision rested in part on the government's stipulation that interest ceased to run as of the date that the government had constructive possession of the bank account and escrow accounts, and no such stipulation has been made here. Pet. App. 21. Second, and more important, in this case the parties' escrow agreement prevented the IRS from requiring that the assets be delivered to it, and made clear that the placement of monies in the escrow account did not constitute the payment of petitioners' tax liabilities. *Ibid.*

4. Petitioners' assertion that the decision below conflicts with the Fourth Circuit's decision in *United States* v. *Barlow's, Inc.* (*In re Barlow's, Inc.*), 767 F.2d 1098 (1985) (per curiam), is also without merit. *Barlow's* does not hold that "the service of a levy on liquid assets * * * , without more, reduces the levied asset to the dominion and control of the Internal Revenue Service." Pet. 22. Rather, in *Barlow's*, the "IRS went well beyond a mere service of levy," by entering into a payment agreement with the third party against whom the levy had been served "without plaintiff's participation." *Barlows, Inc.* v. *United States (In re Barlows, Inc.)*, 36 B.R. 826, 829 (Bankr. E.D. Va.), aff'd, 53 B.R. 986 (E.D. Va. 1984), aff'd, 767 F.2d 1098 (4th Cir. 1985). The third party subsequently defaulted on its obligations under

that payment agreement, with the result that the IRS's unilateral action in entering into that payment agreement caused the loss of funds that could have satisfied the tax liabilities.

In any event, the Fourth Circuit rejected much the same arguments that petitioners here advance in affirming the decision of the district court in Dominick LaRosa's case. See *LaRosa I*, 1998 WL 393976. That decision demonstrates that there is no disagreement between the Fourth Circuit and the Federal Circuit with respect to the question presented here.

5. Finally, petitioners contend (Pet. 21, 22-23) that they are not only entitled to a refund of the underpayment interest that accrued before their taxes were paid, but also to *overpayment* interest under 26 U.S.C. 6611(a), to the extent that such interest exceeds the interest that their funds earned while in escrow. See Pet. 21 (citing *Berger* v. *United States*, 85-1 U.S. Tax. Cas. (CCH) ¶ 13,618 (S.D.N.Y. 1985)). Petitioners' argument rests on the mistaken premise that their taxes were paid as of the date that the IRS levied upon their assets, and, as such, does not merit this Court's review.

6. This Court has previously declined to review Dominick LaRosa's challenge to the same set of transactions here at issue. *LaRosa I*, 526 U.S. 1004. There is no reason for a different result in this case.

**CONCLUSION**

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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