No. 16–497

In The

# Supreme Court of the United States

MARTIN SMITH

PETITIONER

v.

INTERNAL REVENUE SERVICE

RESPONDENT

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

## REPLY BRIEF OF PETITIONER


Robert L. Goldstein
Law Offices of
Robert L. Goldstein
100 BUSH STREET, #501
San Francisco, CA 94104
(415) 391-8700
rgoldstein@taxexit.com

John A.E. Pottow
*Counsel of Record*
c/o 970A LR
801 Monroe St.
Ann Arbor, MI 48109
(734) 647-3736
pottow@umich.edu

## TABLE OF CONTENTS

## TABLE OF AUTHORITIES

### Cases



### Statutes

**Other Authorities**

## INTRODUCTION

The Brief in Opposition rests entirely on the denial or evasion of not one but both the circuit splits raised by this petition. The IRS concedes that the Eighth Circuit is split from the Ninth on whether timeliness matters under the *Beard* test. Yet it suggests that the split can be dismissed because it will go away if the Eighth Circuit in a future case decides that BAPCPA's hanging paragraph supersedes *Beard*. Yet *that* issue—of BAPCPA's relevance to *Beard*—has itself divided the circuits, with the decision of the court of appeals below conflicting with the First, Fifth, and Tenth Circuits, a split the IRS just ignores. The reliance on one side of a circuit split to assume away the relevance of another circuit split is extraordinary. Rather than resolve either split, the IRS would have this Court retain both.

Beyond split-denial fantasy, there is no opposition to the petition. The IRS does not challenge—nor could it—that this petition presents the best vehicle to resolve the bankruptcy law question of the dischargeability of late-filed tax debts. Nor does the IRS challenge the importance of this question to the consumer bankruptcy system. The Court should resolve the circuit division to bring overdue uniformity to the near-million Americans who find themselves in bankruptcy annually.

## I. The IRS' Denial of Not One, But Two Circuit Splits Is Inexplicable.

The bankruptcy dischargeability of belated tax return debt has deeply divided the circuits. The courts of appeals' differing approaches have arisen from not one, but now two circuit splits. The IRS seeks to deny or assume away both these splits. It does not succeed.

The first split can be called the "*Beard* timeliness split." It pertains to whether the *Beard* test's "honest and reasonable" prong includes a timeliness element. *Beard v. Comm'r,* 82 T.C. 766 (1984), *aff'd* 793 F.2d 139 (6th Cir. 1986). The court of appeals below followed a subjective approach and held that a return filed late without good reason, that comes after the IRS has already issued a notice of assessment, flunks this prong. Thus, an unacceptably belated 1040 is not a "return." Pet. App. 7a. The court of appeals' opinion conflicts with the Eighth Circuit's objective approach in *Colsen*, which holds that the content of the return, not the subjective motivation of the taxpayer, governs this prong of *Beard*. Thus, in the Eighth Circuit, an untimely but duly filed 1040 passes *Beard* and is a return. *Colsen v. United States (In re Colsen)*, 446 F.3d 836, 840 (8th Cir. 2006).

The second circuit split is on the ancillary point of whether BAPCPA's hanging paragraph has any effect on the primary *Beard* split. *See* 11 U.S.C. § 523(a)(*), *enacted by* Bankruptcy Abuse and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 ("BAPCPA"). Thus, what might be called the "BAPCPA relevance split" also divides the circuits. One side holds that BAPCPA's hanging paragraph materially amends the definition of "return" and commands a "one-day-late" rule, thus superseding the *Beard* test altogether. Under this approach *any* late return

(i.e., one day late) becomes reclassified as a non-return under 11 U.S.C. § 523. This one-day-late approach now governs in the First, Fifth, and Tenth Circuits. *See Fahey v. Mass. Dep't of Revenue (In re Fahey)*, 779 F.3d 1, 5 (1st Cir. 2015); *Mallo v. IRS (In re Mallo)*, 774 F.3d 1313, 1321 (10th Cir. 2014), *cert. denied,* 135 S. Ct. 2889 (2015); *McCoy v. Miss. State Tax Comm'n (In re McCoy)*, 666 F.3d 924, 932 (5th Cir. 2012).

As one of these circuits reasons:

> If Congress intended 523 to define a return through application of the *Beard* test or some other substantial compliance doctrine, rather than by a taxpayer's compliance with the applicable [timeliness] filing requirements contained in the Tax Code, Congress could simply have defined a return as one that "satisfies the requirements of applicable nonbankruptcy law," without qualifying the statement with the phrase "including applicable filing requirements."

*Mallo*, 774 F.3d at 1325.

Conversely, the court of appeals' opinion below, after quoting BAPCPA's hanging paragraph, held that the *Beard* test continues to govern. Pet. App. 7a ("We hold that [*Beard*-adopting] *Hatton* applies to the bankruptcy code *as amended*.") (emphasis added). Thus, the hanging paragraph effected no change to the pre-BAPCPA law governing discharge in the court of appeals' view. The IRS itself admits this holding below: "The court of appeals below held that the *Beard* test applies when determining whether a filing satisfies the [hanging paragraph's] requirements of 'applicable nonbankruptcy law (including applicable filing

requirements).'" Br. in Opp. 7. Accordingly, in the Ninth Circuit, *Beard*—complete with its underlying interpretive split—remains the governing law for the dischargeabilty of late-filed tax debt. In the First, Fifth, and Tenth Circuits, however, *Beard* is no longer the test; one-day-late is.

These splits, spanning nearly every circuit, have produced (at least) three outcomes for late-filed tax debt in bankruptcy: (1) categorically excluded from discharge under the one-day-late rule; (2) excluded from discharge under the subjective approach to the *Beard* test if the debtor lacks a good reason for belatedness; or (3) eligible for discharge under the Eighth Circuit's approach to the *Beard* test so long as a facially compliant 1040 is filed.

The IRS remains coy on its ultimate position regarding these splits. It seems either to deny their existence, Br. in Opp. 6 ("The court of appeals' judgment . . . does not implicate any conflict among the courts of appeals . . . ."), or wish away the splits as irrelevant, *id.* at 13 n.5. ("That [circuit] conflict has no prospective importance . . . ."). The IRS' characterizations of these splits are quite frankly remarkable; for example, it describes the circuits on either side of the BAPCPA relevance split as taking "*somewhat different* approach[es]," Br. in Opp. 13 (emphasis added), to *Beard*'s ongoing vitality. Indeed. But the IRS cannot escape the inevitable: these are splits that deeply divide the courts of appeals by subjecting bankrupt debtors to disuniform law.[1]

---

[1] Although necessarily imperfect, a common estimate of the number of annual delinquent taxpayers is seven million. Robert E. McKenzie, *7 Million Taxpayers Fail to File Their Income*

Consider first the IRS' treatment of the *Beard* timeliness split. The IRS concedes, as it must, that the Eighth Circuit is split from the Ninth Circuit below (and the Fourth, Sixth, Seventh, and Eleventh Circuits) on how to treat late-filed tax returns under *Beard*. *See* Br. in Opp. 13 n.5. Recognizing this undeniable split, the IRS assumes it away. Specifically, the IRS argues that the *Beard* split *Colsen* caused can be ignored, because if the Eighth Circuit ever revisits the matter, it might side with the Tenth Circuit over the Ninth on the BAPCPA relevance split and hold that a one-day-late rule commanded by BAPCPA supersedes *Beard*. *See id*. 13. If *Beard* is superseded in the Eighth Circuit by the one-day-late rule, then *Colsen* (and its circuit-splitting effect) becomes moot, and the *Beard* timeliness split vanishes.[2]

The logic underlying this reasoning is flawed (and its sense of *stare decisis* curious). A circuit court's precedent cannot be disregarded by mere hope that the court might subsequently hold it to be superseded by statute—especially so, as here, when there is *circuit division* over the superseding effect of the relevant statute.[3] Indeed, the

---

*Taxes*, FORBES (Aug. 27, 2014), http://www.forbes.com/sites/irswatch/2014/08/27/7-million-tax-payers-fail-to-file-their-income-taxes/#3addd72f45af.

[2] This conclusion is false. Even if the Eighth Circuit did split with the Ninth and join the one-day-late circuits, *Colsen* would remain binding, circuit-splitting precedent on the definition of "return" for non-bankruptcy purposes.

[3] The IRS believes *Colsen* is no longer binding in the Eighth Circuit unless "re-affirmed" post-BAPCPA: "Petitioner urges this

sole premise for the IRS' optimism of spontaneous circuit split dissolution is the unremarkable observation that *some* courts of appeals have held that BAPCPA's hanging paragraph supersedes *Beard* by imposing a new one-day-late rule. Br. in Opp. 12–13. That is true. But it is equally true that *other* courts, such as the court of appeals below, have held the exact opposite: *Beard* survives BAPCPA and has *not* been superseded by a one-day-late rule. Pet. App. 7a (holding that *Beard* applies to the code "as amended"). Hence, the IRS' premise for ignoring a conceded circuit split (the *Beard* timeliness split) rests on ignoring a second, related circuit split (the BAPCPA relevance split).

Moreover, the IRS does not even offer argument for *why* the Eighth Circuit might follow the Tenth rather than the Ninth on the BAPCPA relevance split. On the contrary, it offers many reasons why the Eighth Circuit should not. The IRS agrees with petitioner that *Beard* still controls post-BAPCPA, *see* Br. in Opp. 3, and that the contrary view is rife with textual difficulties, *id.* 10 (rejecting one-

---

Court to adopt a rule of dischargeability that neither the IRS nor any court of appeals has accepted *under the current version of Section 523(a)*." Br. in Opp. 11 (emphasis added). This assumption begs the question: it *presumes* that BAPCPA's hanging paragraph relevantly changed the definition of return, i.e., to supersede the *Beard* test with a one-day-late rule—an issue that has split the circuits. If, as is most plausible given the text and the legislative history, *see* Pet. 31–36, the Ninth Circuit is right and BAPCPA did *not* so relevantly change the definition, then the amendment was unimportant to this petition; pre-BAPCPA and post-BAPCPA precedents alike, like *Colsen*, interpreted the correct "version" of the statute.

day-late approach as IRS policy over concerns of rendering hanging paragraph's text "superfluous"); Pet. 31–36 (raising additional concerns). Given the IRS' well-argued opposition to interpretations of the hanging paragraph that abrogate *Beard*, the claim that *Colsen* can be ignored because the Eighth Circuit may hold the hanging paragraph abrogates *Beard* is self-deprecating and bizarre. Stripped bare, the argument that this Court can ignore the *Beard* timeliness split based on a prediction of the Eighth Circuit's adoption of the one-day-late rule is nothing more than an attempt to alchemize two circuit splits in need of this Court's resolution into zero.[4]

While the IRS' attempt to assume away the *Beard* timeliness split might charitably be characterized as speculative, its assessment of the BAPCPA relevance split in the decision below verges on incomprehensible. The IRS contends that even though the Ninth Circuit affirmed *Beard* as the apposite test (thus creating a circuit split on BAPCPA's relevance), it failed to render a gratuitous, alternative holding that could have avoided the split. Namely, although the Ninth Circuit held that the BAPCPA amendment changes nothing, it also could have added, in the alternative, that the BAPCPA amendment changes everything and *Beard* is no longer the governing test. If the Ninth Circuit had just held differently, the IRS reasons, there might not have been a circuit split. Br. in Opp. 7 (discussing a "possible alternative basis" on which the

---

[4] Of course, the *Beard* split will still apply to non-bankruptcy disputes over the definition of "return." *See supra*, n.2.

court of appeals could have decided the case by adopting the one-day-late rule).

This reasoning is specious. The Ninth Circuit held that *Beard* is still good law, which the IRS not only admits but quotes. *See* Br. in Opp. 3. This holding squarely conflicts with the other courts of appeals that have decided *Beard* has been superseded by BAPCPA and the one-day-late rule now reigns. *See*, *e.g.*, *Mallo*, 774 F.3d at 1325 (holding *Beard* test irreconcilable with hanging paragraph). It is trivial to say that the Ninth Circuit could have adopted, in the "alternate," Br. in Opp. 7, the "somewhat different," *id.* at 13, view that *Beard* is no longer good law and joined the one-day-late crowd to avoid the split. And it borders on sophistry to say that a circuit split, in the alternative, would not have been a circuit split if the circuits had not split.

Moreover, the implicit suggestion that the Ninth Circuit forgot to or did not know it could enter an alternative holding had it wanted is not well taken. At the risk of belaboring the point, consider that the Eleventh Circuit *did* decide its recent appeal implicating the question presented using a hypothetical assumption. In *In re Justice*, it *assumed* that the one-day-late cases are wrong and *Beard* is still good law, conspicuously declining to take sides in the BAPCPA relevance split by leaving the question open. *Justice v. United States (In re Justice)*, 817 F.3d 738, 743 (11th Cir. 2016), *petition for cert. filed* (U.S. Dec. 21, 2016) (No. 16-786). It held that even under *Beard*, however, the debtor would lose given the unacceptable lateness of his return. *Id.* The Ninth Circuit knew about *Justice*—it explicitly cited *Justice* in the opinion below, which contained no such hypothetical hedging. Pet. App. 6a–7a ("We

hold that [*Beard*-adopting] *Hatton* applies to the bankruptcy code as amended."). Thus, the Ninth Circuit is well aware of how to enter an arguendo holding or a holding in the alternative if it wants. It did not want to here.

Accordingly, try as it may, the IRS cannot explain away either of the circuit splits. It does not, and cannot, dispute the stark conflicts of circuit law affecting bankrupt taxpayers today that leaves their discharge fates determined by geography. In the Eighth Circuit, they can discharge post-assessment-return tax debt; in the First, Fifth, and Tenth Circuits, they cannot discharge any late-return tax debt, and in the Fourth, Sixth, Seventh, Ninth, and Eleventh Circuits, they can only discharge late-return tax debt if the IRS has not yet assessed.

## II. The IRS Does Not Dispute This Case Presents the Best Vehicle for Addressing the Belated Tax Returns Discharge Issue.

The IRS puts all its eggs in the basket of denying or downplaying the circuit splits. It does not contest that this case presents the best vehicle for resolving the conundrum besetting the bankruptcy courts on properly filed but late 1040s. This silence is unsurprising.

Recall that the fractured approach to untimely tax returns implicates two separate, but interrelated circuit splits: first, the *Beard* timeliness split on the significance of timeliness to "honest and reasonable" compliance with tax law, and second, the BAPCPA relevance split on the state of *Beard*'s ongoing vitality. This petition presents the Court with the ideal opportunity to resolve both splits in one clean vehicle. More importantly, it presents the only likely posture to come before this Court.

Although the *Beard* split has been percolating through the circuits for decades, the IRS was, until this petition, previously able to tell the Court that every court of appeals to address the issue post-BAPCPA adopted the one-day-late rule. Accordingly, BAPCPA initially raised the prospect that the *Beard* confusion might just go away as superseded by statute. Indeed, the IRS trumpeted this possibility in opposing certiorari in *Mallo*, which was denied. *Mallo v. IRS*, 135 S. Ct. 2889 (2015) (Mem); Br. in Opp. 11, *Mallo* (No. 14-1072) (emphasizing no court of appeals at that time had held that *Beard* survived BAPCPA).

But now *Beard* is back (assuming *arguendo* it was ever gone), and with it the circuit split on its "honest and reasonable" prong. The opinion below quashed any hope that the circuits might unanimously declare *Beard*'s death post-BAPCPA, eviscerating the principal argument of opposition to certiorari in *Mallo*. *Beard* is still the law in the Ninth Circuit after BAPCPA, and so escape from its interpretative split with the Eighth Circuit is impossible. Indeed, the pending certiorari petition from the Eleventh Circuit and the case under submission at the Third make clear that the issue is timely, divisive, and in need of this Court's resolution. (Neither of those cases will provide helpful vehicles for the Court's consideration of the question, as the Eleventh Circuit's opinion (certiorari petition pending) was premised on an arguendo assumption and the Third Circuit (case under submission) was unaided by oral argument. *Justice*, 817 F. 3d at 743; *Giacchi v. United States (In re Giacchi)*, 553 B.R. 36 (E.D. Pa. 2015), *appeal submitted*, No. 15-3761 (3d Cir. June 22, 2016).) There are only two outcomes to this petition. Either this Court will hold that BAPCPA moots *Beard* altogether, or it will dismiss

BAPCPA as a distracting red herring (as even the IRS believes it is) and move onto settling, once and for all, the *Beard* circuit split that continues to subject bankruptcy taxpayers to different law by circuit.

One might ask whether this Court should address these two interrelated splits *seriatim* rather than both together. That is, perhaps the Court could wait for an appeal by a taxpayer who filed his or her 1040 late, but before assessment. Then, and only then, if it rejects the one-day-late rule, it should grant certiorari on a subsequent *Beard* case (however that might find its way to the Court) to resolve the ongoing timeliness circuit split that will persist. There are two reasons this approach will not work. First, by the IRS' own concession it will not object to one-day-late returns, Br. in Opp. 9, and so that issue is unlikely to present itself to this Court for review without being coupled with a *Beard* dispute, as on the facts of this case. Second, and more fundamentally, such delay would be intolerable to the bankruptcy system, which faces disuniform interpretation of Section 523 right here, right now. To wait for at least one and likely two more certiorari grants inflicts an unnecessary burden on the system and its near-million debtors. Nor are there many circuits left to weigh in; only the Second, Third and D.C. Circuits remain. The others have generated three different approaches across the country to belated returns in a marked fracturing of federal law.

The circuits have split. The issues have been well-ventilated. Nobody disputes the propriety of the vehicle or the importance of the question presented. After two decades of only increasing uncertainty, it is time for this Court to provide long-overdue resolution.

## CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

JOHN A.E. POTTOW
ROBERT L. GOLDSTEIN
*Counsel for Petitioner*

JANUARY 2017