**Tax Tips**

**Deduction for Losses from Ponzi Schemes (Part 2of 2)**

As you may recall, in last month’s Tax Tips we began a discussion concerning the IRS rules applicable deducting investment losses that you may sustained from Ponzi and similar fraudulent schemes. In this article, we’ll wrap up our discussion of the IRS rules concerning the deductibility of losses you may sustained from Ponzi and similar fraudulent schemes.

**Net operating losses.** Under the general rules for net operating losses (NOLs), the losses can be carried back two years and forward 20 years. The interaction of the NOL rules with the rules for other deductions and credits is complex; if you had a potential NOL, you should seek tax advice before choosing a carryback period.

**Safe-harbor relief.** Some investors will qualify for elective relief under Rev. Proc. 2009-20, 2009-14 IRB 735. The amount of the investment that qualifies for relief under the revenue procedure is the same as it is under the rules described above. But the amount to be deducted is 95% of the qualified investment if the investor doesn't pursue any potential third party recovery or 75% of the qualified investment if the investor is pursuing or intends to pursue a third party recovery. These amounts must be reduced by any actual recovery or potential SIPC recovery. The biggest advantage of this method is that the deduction isn't further reduced by a potential direct or third party recovery (although further deductions or income from losses or recoveries occurring in later years are covered by the rules above). It is important to note that the safe harbor can be elected only by investors who invested in Ponzi schemes similar to the one perpetrated by Bernard Madoff.

To qualify for relief under Rev. Proc. 2009-20, investors must file Form 4684, Casualties and Thefts, marked “Revenue Procedure 2009-20,” with the tax return for the year in which the theft was discovered. Appendix A of Rev. Proc. 2009-20 contains a worksheet for calculating the amount of the theft loss and a statement that must be signed by the investor and submitted with Form 4684.

If you have any questions concerning deducting losses generated from Ponzi and similar fraudulent schemes, please do not hesitate to call me at (562) 698-9891.

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