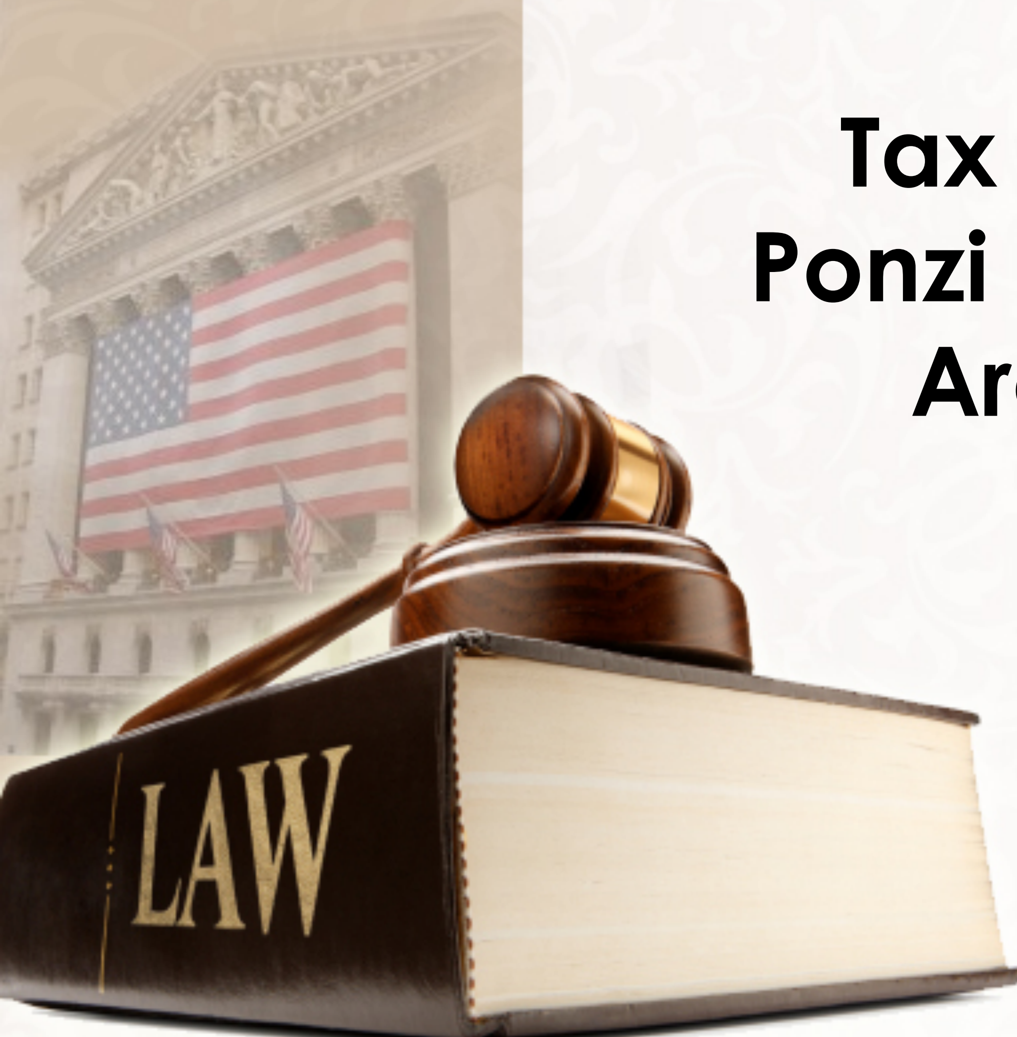
The Ponzi Scheme & TAX LOSS

Tax Refunds from Ponzi Scheme Losses Are Extremely Valuable



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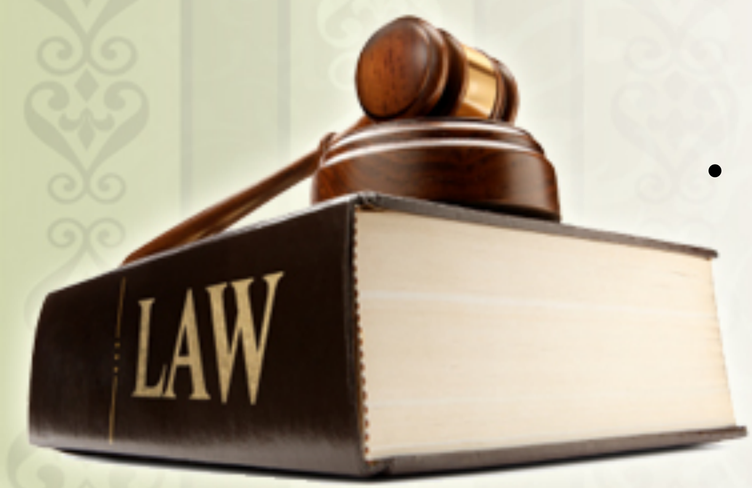
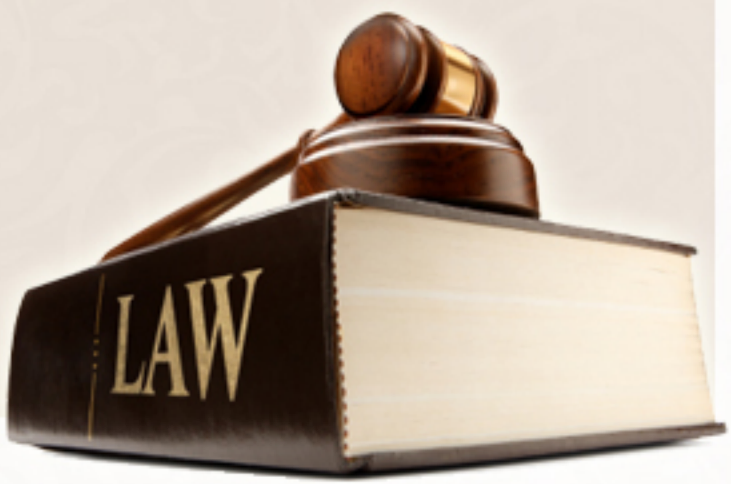
- Masters in Tax Law from New York University Law School
- U.S. Tax Court and Internal Revenue Service experience in Washington D.C.
  - » Served as a law clerk to the Honorable William M. Fay, U.S. Tax Court
  - » Senior Attorney, Interpretative Division, Chief Counsel's Office, Internal Revenue Service, Washington D.C
- The firm regularly works with law firms, accountants, businesses and individuals struggling to find their way through the complexities of the tax law.
- With over 40 years as a tax lawyer in Florida, Lehman has built a boutique tax law firm with a national reputation for being able to handle the toughest tax cases, structure the most sophisticated income tax and estate tax plans, and defend clients before the IRS.



By the end
of this presentation
you will better
understand how
these items relate
to ponzi scheme
tax loss:



THE SAFE HARBOR &

The Internal Revenue Procedure

—

THE LAW &

The Internal Revenue Ruling

—

TAX PLANNING

How the taxpayer will plan and implement his or her Ponzi scheme tax loss for maximum benefits now and in the future.

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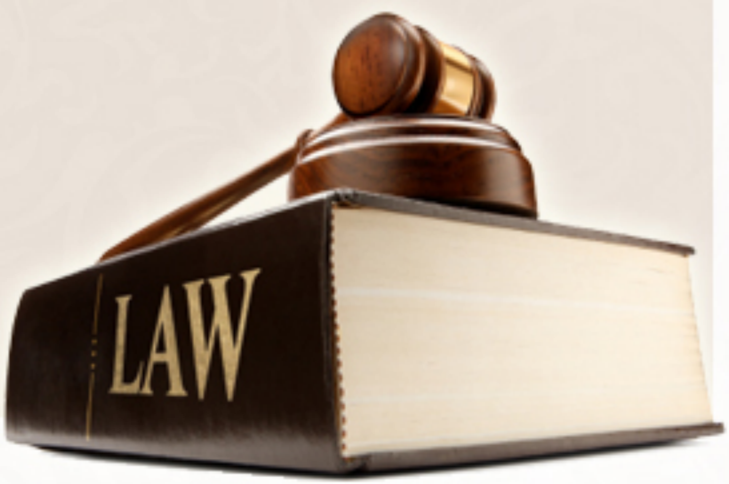

- Ordinary Income Loss can be used against all types of income.
- Loss Carry Backs Eliminated
- Fast Process to Receive Cash – Tax Refund and Amended Returns – No Litigation Costs or Delays
- Most Secure Payer – United States Government
- Can be as High as 37% Return for each Dollar Loss and more for state income tax refunds and due to the absence of deduction limitations
- Can be a lower value in future due to reduced tax rates.
- Unlimited Carry Forward
- Possibility of Receiving Interest on Tax Refunds from Prior Years

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Value Can Be Lost Without Good Professional Advice

PROFESSIONAL

Tax Planning

The final professional product should provide the taxpayer with appropriate projections of the use of the tax losses under differing circumstances that are legally feasible to obtain. The client will be able to understand the financial effect of various options that the tax loss and litigation recoveries may provide for.

The Safe Harbor

The IRS Revenue Procedure

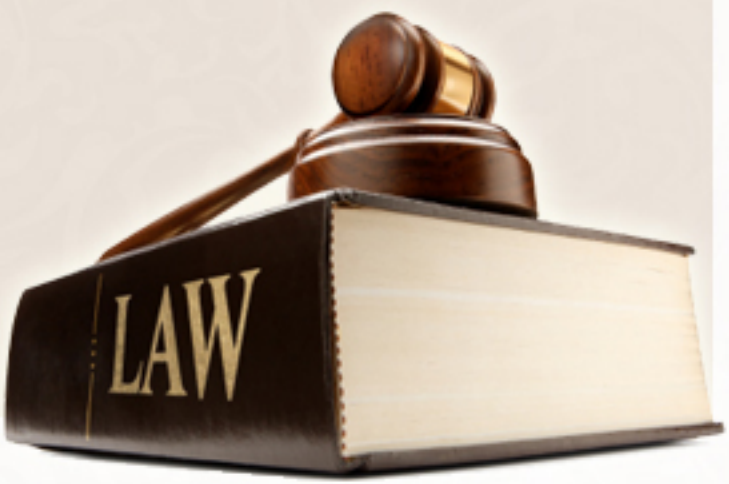
The Safe Harbor

The *Safe Harbor* requires that the Ponzi scheme victims forego the opportunity to file amended returns for those years that are still open by the statute of limitations.

However, by amending a prior return instead of taking a theft loss deduction, a taxpayer can eliminate only the taxpayer's Ponzi scheme "phantom income" from the taxable income in the prior years. This will typically be the high bracket income.

Ponzi Schemes
&
Theft Loss

The Theft Loss allows a deduction for loss sustained during the taxable year and not compensated by insurance or otherwise.



For federal income tax purposes, "theft" is a word of general and broad connotation, covering any criminal appropriation of another's property to the use of the taker, including theft by swindling, false pretenses and any other form of guile.

A taxpayer claiming a theft loss must prove that the loss resulted from a taking of property that was illegal under the law of the jurisdiction in which it occurred and was done with criminal intent. However, a taxpayer need not show a conviction for theft.

Ponzi Schemes & Theft Loss

- The Theft Loss
- Privity of Investor
- Character of Loss
- Limitations on Deductions

II. Ponzi Schemes & Theft Loss

- Amount of the Theft Loss
- Year of Theft Loss Deduction
- Amount of Theft Loss Deduction in Year of Discovery
- Amount of Theft Loss Deduction in Later Years and Recoveries in Excess of Theft Loss Deductions
- The Johnson Cases — A Case Study

The Amount of The Loss (Basis) & Phantom Income

- ***Definition of Phantom Income:***

  The Revenue Ruling and the Revenue Procedure both acknowledge that:

  Theft loss resulting from a Ponzi scheme is generally. . .

  1. The initial amount invested in the arrangement

     plus

  2. Any additional investments upon which taxes have been paid, less amounts withdrawn

The I.R.S. agrees that if an amount is reported to the investor as income in years prior to the **year of discovery** of the theft and the investor includes the amount in gross income; then the amount of the theft loss is increased by the purportedly reinvested amount (the “Phantom Income”).

Year of Discovery

Definition of Taxable Year of Discovery

"…any loss arising from theft shall be treated as sustained during the taxable year in which the taxpayer discovers such loss." A loss is considered to be discovered when a reasonable person in similar circumstances would have realized that he or she had suffered an unrecoverable loss. Although a theft loss must be considered as sustained in the year of its discovery, [The code section] does not indicate that discovery of some false representation (even amounting to theft under applicable law) creates a theft loss as of the date of the discovery of the falsity of the representation. The statue "refers to the year of discovery of the loss, not of the theft."

Year of Discovery

The year of discovery is very important and evidence is critical here to show exactly when and how a taxpayer can pin down this time.

We look to several examples of CASE LAW to help us to define the "year of discovery" of a theft loss.

The Amount & Timing Of The Theft Loss

Reasonable Prospect of Recovery

Definition of "Reasonable Prospect of Recovery"

A reasonable prospect of recovery exists when the taxpayer has a bona fide claim for recoupment from third parties or otherwise, and when there is a substantial possibility that such claims will be decided in the taxpayer's favor. The taxpayer is not, however, required to be an "incorrigible optimist" and claims with only remote or nebulous potential for success will not postpone the deduction.

Reasonable Prospect of Recovery

1. In determining the reasonableness of a taxpayer's belief of loss the courts had to be practical and aware of the individual facts of a case.

2. Circumstances are those that are known or reasonably could be known as of the end of the tax year for which the loss deduction is claimed. The only test is foresight, not hindsight.

3. Both objective and subjective factors must be examined.

Reasonable Prospect of Recovery

The taxpayer's legal rights as of the end of the year of discovery are all important and need to be studied to make a proper decision.

One of the facts and circumstances deserving of consideration is the probability of success on the merits of any claim brought by the taxpayer.

The filing of a lawsuit may give rise to an inference of a reasonable prospect of recovery. However, the inference is not conclusive nor mandatory. The inquiry should be directed to the probability of recovery as opposed to the mere possibility. A "remote possibility" of recovery is not enough; there must be "a reasonable prospect of recovery at the time the deduction was claimed, not later".

Ascertainable Standard

- Once the taxpayer has deducted all that could be deducted in the year of discovery by reducing the loss for all reasonable prospects of recovery the tax in year two, after the discovery year, from this point on will be able to claim continuing theft loss deductions until the loss is recovered in full.

- However, at this point the taxpayer cannot deduct any more of his or her un-deducted theft loss unless the deduction can be "ascertained with a reasonable certainty". This is a higher standard of proof.

Tax Planning

The major principle seen in each of the court's decisions is that victims of the fraud who want to take the theft loss deduction in the year of discovery, must be well advised to separately consider each of their potential sources of recovery.

Value can be lost without good professional advice.

PROFESSIONAL Tax Planning

Tax planning should result in a professional work product that will most likely accompany an amended return or similar type of I.R.S. filing.

The document will most likely be the work product of at least three of the client's advisors:

1. THEIR ACCOUNTANT
2. A TAX ATTORNEY
3. LITIGATION COUNSEL

PROFESSIONAL
Tax Planning

With the professional team in place, the steps generally will be as follows:

1. Records
2. Basis Calculations
3. Sources of Recovery
4. Loss in Year of Discovery
5. Accounting Schedules and Forecasts

These projections will be critical.

The Safe Harbor

The IRS Revenue Procedure

Comparison of Revenue Procedure *vs* Revenue Ruling

The Determination	The Revenue Procedure & THE SAFE HARBOR	VS. THE LAW & The Revenue Ruling
Year of Discovery Deductibility -	Agreement by I.R.S. to a defined set of events	Taxpayer must rely on case law for similar results
Amount of Loss Recognized in Year of Discover	Agreement by I.R.S. to specific percentage amounts	Taxpayer must rely on case law for similar results
Waiver of the Right to File Amended Returns	Potential Tax Benefit Not Available	Potential Tax Benefit Not Available
Claw backs and the Right to Use Code Section 1341	Potential Tax Benefit Waived	Potential Tax Benefit Available
I.R.S. Administrative Issues	Administrative Ease	Increased Proof Requirement Increased Audit Potential

Quantifying the Amount of Theft Loss Deduction in Year of Discovery

The IRS Revenue Procedure **SAFE HARBOR**	**COMPARISON OF LOSS PERMITTED**	The IRS Revenue Ruling **THE LAW**
100%	TOTAL AMOUNT OF QUALIFIED INVESTMENT LOSS	100%
95% Loss Allowed (Loss Reduced by 5%)	"RESPONSIBLE GROUP" RECOVERY SOUGHT	Loss Reduced by any Potential Recovery from the Ponzi Scheme "Responsible Group"
75% Loss Allowed (Loss Reduced by 25%)	THIRD PARTY RECOVERY SOUGHT	Loss Reduced by any Potential Third Party Recovery

Other Reductions to Qualified Investment Loss

SAME FOR SAFE HARBOR OR THE LAW

1. Loss Reduced by Actual Recovery Received in the year of Discovery
2. Loss Reduced by Insurance policies In the name of the Qualified investor
3. Loss Reduced by Contractual arrangements that guarantees or otherwise protects against loss of the qualified investment
4. Loss Reduced by Certain Amounts Payable from the Securities Investor Protection Corporation (SPIC)

Theft Loss
vs
Amended Returns

Amended Returns

A deduction obtained from amending tax returns to eliminate only the Ponzi scheme income may be more valuable than a theft loss deduction.

Clawbacks

Clawbacks and the Right to Use Code Section 1341

Generally in a Ponzi scheme there is a Trustee, usually in bankruptcy. The Trustee has what is called a "clawback" right to recoup funds from Ponzi scheme from investors who have received distributions from Ponzi scheme of funds that belonged to others who had invested in the scheme.

Estates & Trusts
Deductions Available

The income or estate tax deductions available depend on when the loss was incurred and when it was discovered.

There are three common situations:

1. the theft occurs before the decedent dies and is discovered during estate administration;
2. the theft occurs and is discovered during estate administration; and
3. the theft occurs after the accounts have been distributed.

Comparison of Revenue Procedure *vs* Revenue Ruling

The Determination	The Revenue Procedure & THE SAFE HARBOR	vs. THE LAW & The Revenue Ruling
A Ponzi Scheme Loss is a Theft Loss Deductible as an Ordinary Loss	AGREED - Result similar to Revenue Ruling	AGREED - Result similar to Safe Harbor
The Amount of the Loss (Basis) Includes Phantom Income	AGREED - Result similar to Revenue Ruling	AGREED – Result similar to Safe Harbor
The 3 Year Loss Carry Back of Net Operating Losses Applies	AGREED - Result similar to Revenue Ruling	AGREED - Result similar to Safe Harbor
The Deduction is not Reduced by the Application of Certain Percentage or Dollar Limitations	AGREED – Result similar to Revenue Ruling	AGREED – Result similar to Safe harbor
Respect for Pass Through Entities	AGREED -Result similar to Revenue Ruling	AGREED - Result similar to Safe Harbor

Comparison of Revenue Procedure *vs* Revenue Ruling

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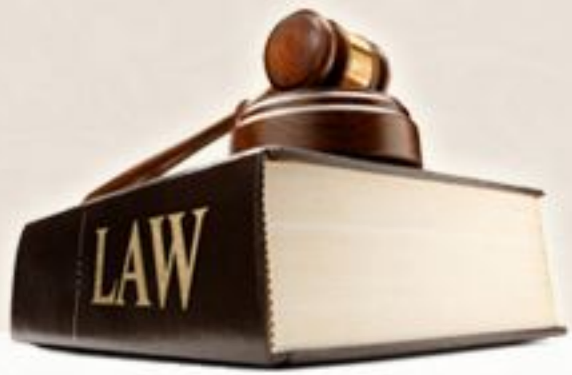

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