

## **New York State Income Tax Treatment of Losses from "*Ponzi-type*" Fraudulent Investment Arrangements**

### **General**

The Internal Revenue Service (IRS) recently issued Revenue Ruling 2009-9, which describes the tax rules that apply to losses from "Ponzi-type" fraudulent investment arrangements. The IRS also issued Revenue Procedure 2009-20, providing an optional "*safe harbor*" procedure for computing and reporting losses for which the discovery year is a taxable year beginning after December 31, 2007. The Department will recognize the federal safe harbor for purposes of computing New York itemized deductions for personal income tax purposes. Accordingly, if the federal theft loss deduction is computed based upon the safe harbor, that amount is to be used in computing the New York itemized deduction. For New York State purposes, itemized deductions are subject to certain limitations, including those described below.

### **New York State limitations on itemized deductions**

Deductions for theft losses attributable to a fraudulent investment arrangement are subject to the limitations of section 615(f) of the Tax Law. Under section 615(f), itemized deductions for a single taxpayer with New York State adjusted gross income (NYAGI) in excess of \$100,000 are reduced by up to 25%. This reduction also applies to married taxpayers filing jointly with NYAGI in excess of \$200,000, and heads of household with NYAGI exceeding \$150,000. For all taxpayers with NYAGI above \$475,000, itemized deductions are reduced by up to an additional 25%.

For the 2009 and subsequent tax years, noncharitable itemized deductions of a taxpayer whose NYAGI is over \$1,000,000 are reduced by an additional 50 percent under section 615(f)(3), bringing them to zero. Accordingly, for taxpayers with NYAGI over \$1,000,000, New York itemized deductions are limited to 50% of federal charitable contributions.

### **Net operating losses**

For federal purposes, theft loss deductions that exceed income can generate net operating losses that can be carried forward or backward to other tax years. For resident taxpayers, any federal net operating loss is also allowed for state purposes. For nonresidents, any federal net operating loss will be allowed in the federal amount column on Form IT-203, Nonresident and Part-Year Resident Income Tax Return. However, in computing New York source income (the New York State amount column on Form IT-203), net operating losses are computed using only New York items of income, gain, loss and deduction. Accordingly, any net operating loss attributable to a theft loss would be allowed only if the loss is attributable to a business, trade, profession, or occupation carried on in New York. The losses from *Ponzi-type* fraudulent investment arrangements generally would not qualify. Also, nonresident individuals may not

carry New York State net operating losses forward or backward to a year in which the individual was a resident of New York State.

### **Filing Procedure**

Taxpayers filing pursuant to the safe harbor rules should complete the "special condition code" space on their New York State income tax return or amended income tax return with the condition code "56." Taxpayers should also attach to their tax return a copy of their federal Form 4684, and a copy of the statement executed pursuant to Revenue Procedure 2009-20.

### **Scope**

The guidelines outlined above will also apply to estates and trusts, shareholders of S-Corporations, partners in partnerships, and members of LLCs, based on the rules for attributing pro rata shares of such losses.

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