

THE GENERAL ASSEMBLY OF PENNSYLVANIA

HOUSE BILL

No. 2153 Session of  
2009

INTRODUCED BY ADOLPH, DENLINGER, McGEEHAN, DALLY, GILLESPIE,  
BAKER, BELFANTI, CARROLL, CASORIO, J. EVANS, FAIRCHILD,  
GABLER, GEIST, HALUSKA, HENNESSEY, HORNAMAN, KILLION, KORTZ,  
KOTIK, LONGIETTI, MANN, MILLER, O'NEILL, PICKETT, PRESTON,  
READSHAW, REICHLEY, ROSS, SANTONI, SCAVELLO, SIPTROTH,  
SOLOBAY, STEVENSON, SWANGER, TALLMAN, VULAKOVICH, WATSON,  
YOUNGBLOOD AND MARSICO, DECEMBER 8, 2009

REFERRED TO COMMITTEE ON FINANCE, DECEMBER 8, 2009

AN ACT

1 Amending the act of March 4, 1971 (P.L.6, No.2), entitled "An  
2 act relating to tax reform and State taxation by codifying  
3 and enumerating certain subjects of taxation and imposing  
4 taxes thereon; providing procedures for the payment,  
5 collection, administration and enforcement thereof; providing  
6 for tax credits in certain cases; conferring powers and  
7 imposing duties upon the Department of Revenue, certain  
8 employers, fiduciaries, individuals, persons, corporations  
9 and other entities; prescribing crimes, offenses and  
10 penalties," in personal income tax, further providing for  
11 classes of income.

12 The General Assembly of the Commonwealth of Pennsylvania  
13 hereby enacts as follows:

14 Section 1. Section 303 of the act of March 4, 1971 (P.L.6,  
15 No.2), known as the Tax Reform Code of 1971, is amended by  
16 adding a subsection to read:

17 Section 303. Classes of Income.--\* \* \*

18 (a.8) (1) A taxpayer is entitled to claim a loss from a  
19 fraudulent investment arrangement for which the taxpayer is  
20 permitted a deduction under section 165 of the Internal Revenue

1 Code of 1986, as amended.

2 (2) (i) A "fraudulent investment arrangement" shall include  
3 an arrangement in which a party:

4 (A) receives cash or property from investors;

5 (B) purports to earn income for the investors;

6 (C) reports income amounts to the investors that are  
7 partially or wholly fictitious;

8 (D) makes payments, if any, of purported income or principal  
9 to some investors from amounts that other investors invested in  
10 the fraudulent arrangement; and

11 (E) appropriates some or all of the cash or property of  
12 investors.

13 (ii) A fraudulent investment arrangement shall not include a  
14 tax shelter as defined in section 6662(d)(2)(C) of the Internal  
15 Revenue Code of 1986, as amended, or any other investment  
16 arrangement, if a significant purpose of that investment  
17 arrangement is the avoidance or evasion of the tax imposed under  
18 this article.

19 (3) (i) Except as provided in subparagraph (iii), a loss  
20 from a fraudulent investment arrangement shall be recognized in  
21 the taxable year in which the taxpayer discovers the loss. The  
22 year in which the taxpayer discovers the loss shall be  
23 determined in accordance with section 165(e) of the Internal  
24 Revenue Code of 1986, as amended.

25 (ii) If during the year of discovery there exists a claim  
26 for reimbursement with respect to which there is a reasonable  
27 prospect of recovery, a taxpayer shall not recognize any portion  
28 of the loss for which reimbursement may be received until the  
29 taxable year in which it can be ascertained with reasonable  
30 certainty whether reimbursement will be received. Whether a

reasonable prospect of recovery exists is a question of fact to be determined upon examination of all facts and circumstances.

(iii) Subject to subparagraph (ii), a taxpayer may make an irrevocable election to recognize a loss or portion of a loss, whichever is applicable, in the taxable year in which the taxpayer included the amount claimed as a loss or portion of a loss in income if:

(A) the taxpayer actually paid tax under this article on that income; and

(B) the taxpayer files either an amended return within three years from the due date, including any extension, of the original return in which the income giving rise to the loss was included, or a petition for refund with the department within the applicable statute of limitations provided in section 3003.1.

(iv) A taxpayer shall make the irrevocable election with the timely filing of either the amended return or the petition for refund.

(v) A taxpayer is only permitted to claim a loss or portion of a loss, whichever is applicable, in a prior taxable year through the filing of a petition for refund in circumstances where the amount or class of income to which the loss relates is the subject of an administrative or judicial appeal.

(4) (i) The amount of a loss that a taxpayer is entitled to recognize from a fraudulent investment arrangement shall equal the amount of the taxpayer's investment in the arrangement, including any additional investments, less all withdrawals, distributions, reimbursements or other recoveries and the amount of all claims to which there is a reasonable prospect of recovery. Additional investments shall include an amount

1 reported to a taxpayer as income in years prior to the year of  
2 discovery of the loss if the taxpayer:

3 (A) included the amount in income;

4 (B) paid tax under this article on that income; and

5 (C) reinvested the amount in the fraudulent investment  
6 arrangement.

7 (ii) A taxpayer may not claim a loss for amounts invested in  
8 a fraudulent investment arrangement that were borrowed from any  
9 individual or entity that was involved in the conduct of the  
10 fraudulent investment arrangement to the extent that the  
11 borrowed funds were not repaid at the time the loss was  
12 discovered.

13 (5) (i) A loss attributable to income upon which a taxpayer  
14 previously paid tax under this article shall be included in the  
15 same class or classes of income as the income to which the loss  
16 relates.

17 (ii) A loss not attributable to income upon which a taxpayer  
18 previously paid tax under this article shall be included in the  
19 appropriate class or classes of income.

20 (iii) To the extent that a taxpayer is unable to trace a  
21 loss to a specific class of income, the loss must be allocated  
22 to the applicable classes of income in a reasonable manner.

23 (iv) A taxpayer may not source the same loss or the same  
24 portion of a loss, whichever is applicable, to more than one  
25 class of income.

26 (6) (i) (A) If a taxpayer recovers an amount in a later  
27 taxable year for which the taxpayer recognized a loss in an  
28 earlier taxable year, the taxpayer shall recognize the amount  
29 recovered in the later taxable year to the extent that the  
30 recognized loss to which the recovery relates reduced the

1 taxable income of the taxpayer in the earlier taxable year.

2 (B) The amount recovered must be included in the same class  
3 or classes of income that the related loss reduced taxable  
4 income in the earlier taxable year. In the event that the amount  
5 recovered relates to more than one class of income, the amount  
6 recovered must be allocated between or among the applicable  
7 classes of income in a reasonable manner to the extent that the  
8 taxpayer is unable to trace the amount recovered to a specific  
9 class of income.

10 (C) The taxpayer shall not report the recovery on an amended  
11 return for the earlier taxable year whether or not the statute  
12 of limitations has expired.

13 (ii) (A) If a taxpayer recovers less than an amount covered  
14 by a claim for reimbursement with respect to which there is a  
15 reasonable prospect of recovery that reduced a deduction in an  
16 earlier taxable year, the taxpayer shall recognize the  
17 difference as a loss in the tax year in which the amount of  
18 recovery is ascertained with reasonable certainty.

19 (B) In the event that the additional loss relates to more  
20 than one class of income, the taxpayer must allocate the amount  
21 of the recovery between or among the applicable classes of  
22 income in a reasonable manner to the extent that the additional  
23 loss is unable to be traced to a specific class of income.

24 (7) A taxpayer may not carry back or carry over any unused  
25 losses to another taxable year.

26 (8) The taxpayer has the burden of proving the entitlement  
27 and amount of any loss recognized from a fraudulent investment  
28 arrangement. The department shall not deny a loss from a  
29 fraudulent investment arrangement claimed on an original return,  
30 amended return or petition for refund merely because the

1 transaction is not reported on an original or corrected Federal  
2 Form 1099, Federal Schedule K-1, PA-20S/PA-65 RK-1, PA-20S/PA-65  
3 NRK-1 or similar document.

4       Section 2. The addition of section 303(a.8) of the act shall  
5 apply to losses from fraudulent investment arrangements  
6 discovered on or after January 1, 2007.

7       Section 3. This act shall take effect in 60 days.