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May 11, 2010

Elisabeth Shumaker, Esq.
Clerk, U.S. Court of Appeals
for the Tenth Circuit
Byron White United States Courthouse
1823 Stout Street
Denver, CO 80257

Re: Sala v. United States, Appeals Court Docket No. 08-1333

Response to Government Citation to Supplemental Authorities: *Nevada Partners Fund, LLC v. United States,* No. 06-379 (S.D. Miss. Apr. 30, 2010).

## Dear Ms. Shumaker:

This letter is Appellees' response to the government's second Rule 28(j) letter concerning the Southern District of Mississippi's recent decision in *Nevada Partners Fund, LLC v. United States*.

Nevada Partners found there was no "nexus" between the tax loss generating trades and a later long term investment because the straddle positions generating the tax loss "were not intended to result in a profit," and had the sole purpose of generating tax losses. Slip op. 8, 58. It further held the straddle transaction had no profit potential and was "cash flow negative," which was inconsistent with the second part of the program which the court found did have a profit potential and actually made substantial profits. Slip op. 58. On the other hand, the court in Sala found the trades generating the tax loss had a potential to be hugely profitable, and were part of an anticipated long term program that likewise had large profit potential. Aplt. App. 126-27. The Sala court further found the initial partnership did have a nexus to the long term investment: 1) from the investors' standpoint, it provided them the opportunity to become familiar with Krieger's trading strategies; 2) from Krieger's standpoint, it enhanced his ability to manage the funds long term because investors were locked-in if he made a profit; and 3) each transaction "had

May 11, 2010 Page 2

substantial business purpose other than the creation of losses." Aplt. App. 115, 118, 132-33.

The government makes much about the size of the loss as compared to the size of the investment in *Nevada Partners*. Here, the size of the loss is a function of a rule of law involving the treatment of contingent liabilities. Aplee. Br. at 16-19. In *Helmer v. Comm'r*, 34 T.C.M. (CCH) 727 (1975), the IRS successfully argued for the exclusion of contingent liabilities in the computation of the taxpayer's basis. Accordingly, the *Helmer* taxpayer recognized gain which grossly exceeded his actual profit on the transaction. In this case, application of the same rule vociferously championed by the IRS in *Helmer* results in a loss that exceeds economic investment. As the *Klamath Strategic Inv. Fund*, *LLC v. United States*, 440 F. Supp. 2d 608, 619 (E.D. Tex. 2006), court explained, the proper analysis "will not vary in meaning simply based on whose ox is being gored."

We are forwarding a copy of this letter to counsel for the appellant. We would request that you distribute this letter to the members of the panel assigned to this case.

Very truly yours,

CHICOINE & HALLETT, P.S.

John M. Colvin

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JMC/ct

cc: Arthur Catterall, Esq.