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Appeals Court Rules IRS Can't Tax Some Gambling Winnings

Everything is taxed, right? Just about. So when something *isn't*, it seems truly remarkable. When you add that it's *gambling* winnings we're talking about, the idea that *anything* isn't taxed is, well, too good to be true.

The black letter rule is that everything is income for tax purposes. If you manage to find a legal way not to pay, it's remarkable.

And there's no question that gambling winnings are taxed. Yet what about nonresident aliens?

If you're not a U.S. citizen or permanent U.S. resident, can the IRS tax your winnings? This is where the tax rules get complicated. Nonresident aliens pay U.S. tax on their "fixed or determinable annual or periodical gains, profits, and income" from U.S. sources. That phrase is hard to decipher, but it includes gambling winnings.

The flip side is that nonresident aliens can only deduct items effectively connected with the conduct of a trade or business within the U.S. As a result, *gambling losses are not deductible* by a nonresident alien. Is that fair, taxing winnings but not allowing losses?



(Photo credit: Wikipedia)

After all, even domestic gamblers have had to fight with the IRS about how to offset their wins and losses. In 2008, the IRS ruled that U.S. citizens could measure their gains on a per-session basis. In effect, you don't have to compute **each wager separately** to determine if you won or lost and by how much. Just tally your total at the end of your gambling session.

The Tax Court reached the same conclusion in [Shollenberger v. Commissioner](#). As a result, now U.S. citizens (and resident aliens) can measure their gambling wins and losses on a **per-session** basis and don't have to go bet by bet. But should this treatment apply to nonresident aliens who come to the U.S. to gamble? The IRS said no, aliens should pay tax on all gains, period.

But then came Mr. Park, a nonresident alien, who periodically came to the U.S. to gamble. Although he had net gambling **losses**, the IRS determined that he had both gambling gains and gambling losses, because it treated each bet separately. The IRS said he **couldn't** offset them.

The IRS claimed that his wins were "effectively connected" to the U.S., but not his losses! And the U.S. Tax Court agreed. See [136 TC No. 28](#). But Mr. Park appealed, and the D.C. Circuit Court of Appeals reversed. It held that the per-session rule applies to residents and nonresidents alike. See [12-1058 – U.S. Court of Appeals - D.C. Circuit](#).

The Appeals Court said there was nothing in the law to vary the tax rules on gamblers depending on whether they were U.S. citizens. The court pointed out that the IRS itself had said that offsetting wins and losses per session made sense—for citizens. To the court, the IRS opened the door.

If the rule made sense for U.S. citizens, it made sense for nonresidents too. The per-session approach avoids the administrative and practical difficulties of having to track every single win. There is nothing in the law to make this rule any less sensible for nonresidents.

Now, if only we could work out a way to more effectively beat the odds....

You can reach me at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.