

RECENT CHANGES IN TAX LAW CREATE OPPORTUNITIES TO BETTER SERVE INTERNATIONAL SLOT MACHINE PLAYERS

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I. INTRODUCTION

Business opportunities do not often come in the form of compliance with Federal tax law.¹ In fact, preparing filings and maintaining compliance throughout the ordinary course of day-to-day business and throughout the year carries a heavy burden for businesses in both time and money.² However, recent developments in case law and related proposed rules issued by the Internal Revenue Service (IRS), have changed the standard of withholding income from slot machine play and offer considerable benefits to casino

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Thank you to Dean Hamilton, Dean of the William S. Boyd School of Law for your support and guidance throughout my law school career. To Professor of Law, Francine J. Lipman, thank you for your passion for tax law, support, and counsel in the editing process. To Associate Dean for Academic Affairs and Professor of Law Jeanne F. Price, thank you for all you have done to help prepare me and guide me through law school. My sincere thanks goes to my fellow classmates at the law school who offered guidance and support throughout the writing process. To the generous sponsors, advisory board members, and journal staff who make the *UNLV Gaming Law Journal* possible this note could not have been done without you. It is my hope that this note will help bring value to the gaming industry. I am grateful to the gaming industry as it has played a crucial role in developing the town I grew up in. This industry has also made it possible for me to attend law school locally. Thank you to all.

Last, counsel should always be on the lookout for opportunities present in the ever changing legal environment. It is not often that law review articles offer a path to increased profits. I would like to see more of them. The reason I selected the above prerequisite for my note was I felt strongly about giving back to the industry that founded and continues to support the William S. Boyd School of Law.

¹ See generally Joshua D. McCaherty, *The Cost of Tax Compliance*, TAX FOUNDATION (Sept. 11, 2014), <http://taxfoundation.org/blog/cost-tax-compliance>; Jason J. Fichtner & Jacob Feldman, *The Hidden Costs of Tax Compliance*, MERCATUS CTR. (May 20, 2013), <http://mercatus.org/publication/hidden-costs-tax-compliance> (noting, “Americans spend more than 6 billion hours (2011) complying with the tax code.”).

² McCaherty, *supra* note 1; Fichtner, *supra* note 1.

properties who serve certain international slot machine players. The benefit of this change translates to more money left in the hands of the gambler for a longer period of time rather than withheld, and a greater opportunity than ever before for the casinos to win money back.

This article will describe the change from a per-bet determination of income to a per-session-based determination for non-resident, non-professional gamblers who engage in slot machine play. Subsection A within Part I begins with a discussion of U.S. Casinos and their relationship with international gamblers, thereby providing a foundation for why the amounts at issue are so substantial.

Part II will consist of several definitions and classifications relevant to the tax analysis. For those not familiar with slot machines, Part II subsection A, will provide a brief discussion explaining how the machines work and how the IRS defines them. Subsection B will explain how non-resident taxpayers are classified under the Internal Revenue Code (IRC or Code). Because the determination of a professional gambler versus a casual gambler is an important step in applying the Code, subsection C will outline the factors courts consider in classifying players as casual gamblers or professional gamblers.

Part III examines what gross income is in general and then discusses two models of calculating gross income from slot machine play through a series of illustrations in subsection A and B. Although the current case law describes which model is appropriate for non-resident taxpayers, some of the IRS's offered guidance on the issue remains unclear.

Part IV describes the transition in case law from the per-bet basis to the per-session-basis of accounting for withholding on earnings from international slot machine players. This section will include an analysis of Chief Counsel Advisory Memorandum AM2008-011, the cases *Schollenberger*³ and *Park*,⁴ and propose how casinos can increase revenues through session-based tracking because of the court's decisions.

Part V highlights how IRS's guidance conflicts with the holding in *Park* and statutory authority in §871 and §1441(a). Part VI identifies some of the counter arguments suggested by attorneys in the tax field. Finally, Part VII explains the benefits for casinos seeking to take advantage of case law that, if applied correctly, will decrease withholding requirements for their non-resident players leaving more money in play.

A. The Romance Between U.S. Casinos and the Non-Resident Gambler

The relationship between international gamblers and U.S casinos is important because international gamblers from countries whose withholding requirements are not governed by various treaties are in the best position to

³ *Schollenberger v. Comm'r*, 2009 T.C.M. LEXIS 310 (2009).

⁴ *Park v. Comm'r*, 722 F.3d 384 (D.C. Cir. 2013).

benefit from the new interpretation of the withholding requirement. Las Vegas, Nevada, in particular has been a model of building connections with international travelers. One of the most visited destinations in the United States by international travelers, Las Vegas has a prime market to benefit from the court's recent interpretation of the withholding standard for foreign gamblers.⁵ The slot machine is "America's favorite casino game and one of the most widely recognized symbols of commercial gaming."⁶ Without gaming revenue, Las Vegas as we know it would likely not exist.⁷ The land occupied by billions of dollars of investments in gambling facilities catering to international travelers on the Strip provides jobs and serves as the leading powerhouse of Nevada's economy.⁸ Because of the gambling opportunities, people from all corners of the earth come to Las Vegas and other parts of the United States to try their luck and attempt to cash in.⁹ These gamblers often lose due to the design of the gambling contract offered to them because the odds of profiting from the wagering activity favor the casino.¹⁰ The fact the odds favor the house is particularly true for slot machines.¹¹ Because slot machines function based on random events, which without exception, will over time, favor the casino,

⁵ William N. Thompson, *Gambling Taxes: The Philosophy, the Constitution and Horizontal Equity*, 17 JEFFREY S. MOORAD SPORTS L.J. 389, 396 (2010) ("Casinos work for the Las Vegas economy because ninety percent of the play is from visitors"); see also *The 10 Most Visited States in the United States by Foreign Travelers* (2013), TRAVELER'S DIGEST (Aug. 30, 2014), <http://www.travelersdigest.com/7516-10-most-visited-states-in-the-united-states-by-foreign-travelers-in-2013/2/>.

⁶ *Taking the Mystery Out of the Machine: A Guide to Understanding Slot Machines*, AM. GAMING ASS'N, http://www.oapcg.org/pdfs/taking_the_mystery_out_of_the_machine_brochure.pdf (last visited Sept. 26, 2016).

⁷ See M.A. Smith, *Top 5 Industries in Nevada: Which Parts of the Economy are Strongest?*, NEWSMAX (Apr. 14, 2015, 3:16 AM), <http://www.newsmax.com/FastFeatures/industries-nevada-economy/2015/04/14/id/638269/> (asserting that Nevada's number one economic driver is tourism and gaming).

⁸ See *How Gaming Benefits Nevada*, NEV. RESORT ASS'N, <http://nevadaresorts.org/benefits/taxes.php> (last visited Sept. 26, 2016). See generally Stephanie Grimes, *Knowing Vegas: What's the Most Expensive Hotel on the Strip?*, L.V. REV.-J. (Mar. 18, 2014, 2:22 PM), <http://www.reviewjournal.com/news/knowning-vegas-what-s-most-expensive-hotel-strip> (amounts adjusted for inflation: Cosmopolitan costing \$4.18 billion, Wynn Las Vegas costing \$3.26 billion, Bellagio Hotel costing \$2.3 billion, The Palazzo costing \$2.05 billion, MGM Grand costing \$1.62 billion).

⁹ See TRAVELER'S DIGEST, *supra* note 3.

¹⁰ Anthony Cabot & Robert Hannum, *Advantage Play and Commercial Casinos*, 74 MISS. L.J. 681, 684 (2005).

¹¹ Pete Knutson, *Best Casino Odds: Blackjack, Craps, Roulette? Which Games Give You the Best Shot at Winning*, KRJH (May 8, 2013, 1:29 PM), <http://www.kjrh.com/news/local-news/best-casino-odds-blackjack-craps-roulette-which-games-give-you-the-best-shot-at-winning> (stating slot machines are not one of the games that give players an edge in winning).

players often lose.¹² This means one thing for casinos and it is paramount—profits.

Recently, Asian gamblers have come to represent a gold mine for many Las Vegas casino properties.¹³ “By 2019, about 180 million Chinese—and \$275 billion in travel spend[ing]—are expected to flow outside of China.”¹⁴ Casinos are hoping to get a chunk of the change the non-resident players are willing to spend during their stay.¹⁵ The number of mainland Chinese and Hong Kong tourists to Las Vegas is growing and has increased almost 80 percent, likely due to catering to the Asian market.¹⁶ The special attention given to these gamblers is done for good reason; many of the Asian players coming to Las Vegas bet big, spending millions of dollars in a single night in one of the private gaming rooms.¹⁷

One difference between domestic and Asian guests is that the Asian guests spend more time gambling as opposed to spending time shopping or going to shows.¹⁸ Because of these customer characteristics, every casino’s dream is to catch high rolling gamblers, known as whales.¹⁹ Casinos try to bait these whales with free flights on Gulfstream jets, lavish hotel suites or villas, and other plush incentives known in the casino industry as “comps.”²⁰ But casinos are not picky; they do not cater to only a few whales.²¹ In fact, it is not just the whales that are bringing in the money to casinos, China’s increasingly wealthy middle class is attracted to Vegas more than ever.²² Not only are the Asian

¹² Cabot & Hannum, *supra* note 10, at 684; *see also* *Congratulations, You’ve Lost! How Slot Machines Disguise Losses as Wins*, FREAKONOMICS (Sept. 1, 2011, 2:09 PM), <http://freakonomics.com/2011/09/01/congratulations-youve-lost-how-slot-machines-disguise-loses-as-wins/>.

¹³ Alexandra Berzon ET AL., *Vegas Bet on Chinese VIPs Raises Red Flags with Feds*, WALL STREET J. (Dec. 18, 2012, 2:18 PM), <http://www.wsj.com/articles/SB10000872396390444017504577648160626366488>.

¹⁴ Ann Friedman, *Chinese Tourists Spell Opportunity for Vegas*, L.V. BUS. PRESS (Oct. 24, 2015, 1:44 PM), <http://businesspress.vegas/gaming-hospitality/chinese-tourists-spell-opportunity-vegas>.

¹⁵ *See generally id.*

¹⁶ Berzon, *supra* note 13.

¹⁷ Donald Frazier, *Chinese Players Find Good Fortune in Las Vegas*, FORBES (Mar. 28, 2012, 6:00 PM), <http://www.forbes.com/global/2012/0409/feature-visitors-mgm-grand-find-good-fortune-in-las-vegas.html>.

¹⁸ Gary Rivlin, *Las Vegas Caters to Asia’s High Rollers*, N.Y. TIMES (June 13, 2007), <http://www.nytimes.com/2007/06/13/business/13vegas.html>.

¹⁹ John Gapper, *The Risky Game of Whale-Hunting*, FIN. TIMES (Sept. 10, 2006, 11:05 AM), <http://www.ft.com/intl/cms/s/0/eca3e42c-4131-11db-827f-0000779e2340.html#axzz40xp5Vj8u>.

²⁰ *Id.*

²¹ Mark Hanrahan, *VIP Gambling: As High Rollers Desert Macau, Can Other Asian Destinations Win Big?*, INT’L BUS. TIMES (Apr. 5, 2015, 11:58 AM), <http://www.ibtimes.com/vip-gambling-high-rollers-desert-macau-can-other-asian-destinations-win-big-1868820>.

²² Michelle Florcruz, *Chinese Money Brings New Life to Las Vegas, but Macau’s*

gamblers attracted to U.S. Casinos, they are also becoming more and more attracted to slot machine play.²³ Reflecting this fact, floor space in casinos has steadily transitioned from table games to thousands of slot machines because of the gaming market's heavy reliance on slot revenues.²⁴

II. DEFINITIONS AND CLASSIFICATIONS

A. Slot Machines—A Foundation

The familiarity and growing popularity of slot machines is relevant to this note because the interpretation of the withholding requirement applies only to slot machine winnings and not to other games offered in the casino. For the purposes of the following discussion, the IRS defines slot machine as “a device that, by application of the element of chance, may deliver, or entitle the person playing or operating the device to receive cash, premiums, merchandise, or tokens whether or not the device is operated by insertion of a coin, token, or similar object.”²⁵ The fact that Las Vegas style slots are now offered in twenty-two states is a testament to their popularity and societal acceptance of the gaming industry.²⁶ In Las Vegas alone, slot machines generate more than \$7 billion annually, which is about double the revenue of that taken in by table games.²⁷ With the development of new technology, particularly the microprocessor, slot and video poker machines and other electronic gaming devices offer bigger jackpots, are more sophisticated and are more appealing

Casinos Are Suffering, INT'L BUS. TIMES (May 12, 2014, 4:55 PM), <http://www.ibtimes.com/chinese-money-brings-new-life-las-vegas-macaus-casinos-are-suffering-1583222>.

²³ Interview with Kelvin Chiu of Asia Gaming, *Kelvin Chiu Explains Slot Machines' Popularity in Asia*, CALVIN AYRE (Apr. 20, 2016), <http://calvinayre.com/2016/04/20/casino/chiu-explains-slot-machines-popularity-in-asia-bl-video/>.

²⁴ Kasra Christopher Ghaharian, *A Mathematical Approach for Optimizing the Casino Slot Floor: A Linear Programming Application 1–2* (Dec. 2010) (unpublished B.A. thesis, University of Nevada, Las Vegas), <http://digitalscholarship.unlv.edu/cgi/viewcontent.cgi?article=1717&context=theses-dissertations> (“For the fiscal year ending July 31, 2010, Nevada statewide slot machine win was \$6.6 billion, compared to the \$3.5 billion in table games win (Nevada Gaming Control Board, 2010). In 2009, 88% of Illinois’ and 90 % of Iowa’s total casino win came from slot machines (Illinois Gaming Control Board, 2009; Iowa Racing & Gaming Commission, 2009)”); see Gapper, *supra* note 19.

²⁵ I.R.S. Notice 2015-21, 2015-12 I.R.B. 765, <https://www.irs.gov/pub/irs-irbs/irb15-12.pdf> [hereinafter I.R.S. Notice 2015-21].

²⁶ David Stewart, *Demystifying Slot Machines and Their Impact in the United States*, AM. GAMING ASSOC. 5, <http://docplayer.net/2859075-Demystifying-slot-machines-and-their-impact-in-the-united-states.html> (last visited Sept. 21, 2016).

²⁷ Matt Richtel, *From the Back Office, a Casino Can Change the Slot Machine in Seconds*, N.Y. TIMES (Apr. 12, 2006), http://www.nytimes.com/2006/04/12/technology/12casino.html?pagewanted=all&_r=0.

than ever before to players.²⁸ “[A] new generation of gamblers . . . that were less interested in the traditional table games are more intrigued by the machines.”²⁹ There is little reason to believe that this trend will not hold true for non-resident gamblers, due to the efforts of Macau’s slot hall operators educating Chinese gamblers about the slots and the influx of slot machine devices designed with the culture and generation of the player in mind.³⁰

B. Defining the Non-Resident Taxpayer

The IRS generally treats non-resident taxpayer gambling winnings on slot machine play differently from those who are U.S. citizens or resident taxpayers under the federal income tax system.³¹ Although the Code and some case law refers to non-resident taxpayers as “non-resident aliens,” any reference to “non-resident aliens” will hereinafter be referred to as non-resident taxpayer or non-resident individuals.

Non-resident taxpayers are defined as “a nonresident alien individual, foreign corporation, foreign partnership, foreign trust, a foreign estate, and any other person that is not a U.S. person.”³² If a non-U.S. citizen is not a U.S. resident under the Code, he or she will be characterized as a non-resident individual.³³ If a person receives the non-resident status classification, “[he or] she will generally only be subject to federal income tax on [his or] her U.S.-source income, e.g., wages for services performed in the United States, rents from U.S. real property, and income effectively connected with a U.S. trade or business.”³⁴ The relevance of this definition is that non-resident gamblers not

²⁸ *Id.*; see also Andrew Thompson, *Engineers of Addiction: Slot Machines Perfected Addictive Gaming. Now, Tech Wants Their Tricks*, THE VERGE <http://www.theverge.com/2015/5/6/8544303/casino-slot-machine-gambling-addiction-psychology-mobile-games> (last visited Sept. 21, 2016); see generally *Types of Slot Machines*, CASINO NEWS DAILY, <http://www.casinonewsdaily.com/slots-guide/types-slot-machines/> (last visited Sept. 21, 2016).

²⁹ Anthony N. Cabot & Louis V. Csoka, *The Games People Play: Is it Time for a New Legal Approach to Prize Games?*, 4 NEV. L.J. 197, 213 (2004).

³⁰ Kareem Jalal, *A New Slot: Table Game Crazy Macau Casino Patrons Becoming More Interested in Slot Machines*, HIGH BEAM RES. (Feb. 1, 2008) <https://www.highbeam.com/doc/1G1-180066431.html>.

³¹ Park, 722 F.3d at 385.

³² *Foreign Persons*, I.R.S., <https://www.irs.gov/Individuals/International-Taxpayers/Foreign-Persons> (last visited Oct. 24, 2016).

³³ See Francine J. Lipman, *Taxing Undocumented Immigrants: Separate, Unequal, and Without Representation*, 9 HARV. LATINO L. REV. 1, 18-19 (2006); see also 26 U.S.C. § 7701(b)(1)(B) (2012).

³⁴ Lipman, *supra* note 33, at 18-19; see also Thomas St. G. Bissell, *Portfolio 907-3rd: U.S. Income Taxation of Nonresident Alien Individuals, Detailed Analysis, II. Historical Background*, BNA, <https://www.bloomberglaw.com/p/a8e56c4a18bd40a104b87ec6975386c9/document/2648460840> (recounting the history of taxation of resident aliens and U.S. citizens on one hand, and nonresidents on the other hand, since at least 1913) (last visited Sept. 23, 2016).

governed by treaty may have to pay income tax on gambling income. In contrast, an individual classified as a “resident [individual]” for tax classification purposes meets the qualifications under any of two residency tests: “the lawful permanent resident test” or the “substantial presence test.”³⁵

The first test, the “lawful permanent resident test,” classifies any individual that is a lawful permanent resident of the United States at any time during the calendar year as a resident [individual].³⁶ “An individual is a ‘lawful permanent resident’ under the Code if he or she has been granted permanent residence status under the immigration laws that has not been revoked or abandoned.”³⁷

The second test to determine an individual’s classification under the Code is the “substantial presence test.”³⁸ Under the “substantial presence test,” “if an individual is physically present in the United States for at least [thirty-one] days during the current year, and at least 183 days during the current year and prior two years, she will be classified as a resident [individual].”³⁹ The days of physical presence for the current tax year is calculated by counting all days present in the current year, one-third of the days present in the prior year, and one sixth of the days present in the second preceding year.⁴⁰ If an individual does not satisfy the requirements of either the “lawful permanent resident test” or the “substantial presence test,” or is not able to qualify for an exception to these tests, she will be classified as a non-resident individual and therefore eligible under the court’s interpretation of the withholding change for international slot machine players.⁴¹

Adding more confusion to the classification of the non-resident, many non-resident taxpayers are already exempt from withholding on slot machine winnings under certain treaties. Provided that non-resident taxpayers possess an individual taxpayer identification number⁴² issued by the IRS, slot machine winnings are exempt from the withholding of tax on non-resident taxpayers under treaties with the following countries and therefore cannot take advantage of the court’s interpretation of withholding if the gambler is from: Austria, Belgium, Bulgaria, Czech Republic, Denmark, Finland, France, Germany, Hungary, Iceland, Ireland, Italy, Japan, Latvia, Lithuania, Luxembourg,

³⁵ 26 U.S.C. § 7701(b)(1)(A) (2012).

³⁶ *Id.* § 7701(b)(1)(A)(i).

³⁷ Lipman, *supra* note 33, at 19; *see also* 26 U.S.C. § 7701(b)(6).

³⁸ Lipman, *supra* note 33, at 19; *see also* 26 U.S.C. §§ 7701(b)(1)(A)(ii), (b)(3)(A) (setting forth the substantial presence test).

³⁹ Lipman, *supra* note 33, at 19; *see also* 26 U.S.C. §§ 7701(b)(3)(A)(i)–(ii) (describing the mechanics of the test).

⁴⁰ Lipman, *supra* note 33, at 18; *see also* 26 U.S.C. § 7701(b)(3)(A)(ii).

⁴¹ Lipman, *supra* note 33, at 19; *see also* 26 U.S.C. § 7701(b)(1)(B).

⁴² Lipman, *supra* note 33, at 22 (“[T]he ITIN is a 9-digit number resembling a SSN, but starting with the number “9” and having the number “7” or “8” as the fourth digit.”); *see* Paula N. Singer & Linda Dodd-Major, *Identification Numbers and U.S. Government Compliance Initiatives*, 104 TAX NOTES 1429, 1433 (Sept. 20, 2004).

Netherlands, Russia, Slovak Republic, Slovenia, South Africa, Spain, Sweden, Tunisia, Turkey, Ukraine, and the United Kingdom.⁴³ When not governed by the country's treaty with the United States, the standard protocol for enforcing the collection tax for non-residents on their U.S.-source-nonbusiness-income is governed by section 1441(a).⁴⁴

C. Casual Gambler versus the Professional Gambler Classification

Although this note will deal solely with the treatment of casual gamblers, a casino seeking to take advantage of the change in the withholding requirement must make not only a resident classification but also a classification of the gambler's status as a player or a professional because "[t]he Code mandates . . . that casual gamblers be treated differently from taxpayers who are in the trade or business of gambling" for profit.⁴⁵ There is little specific legislative or regulatory guidance on whether an individual is a professional engaged in the trade or business of gambling.⁴⁶ However, in *Groetzinger*, the Supreme Court recognized several factors that should be considered when determining whether a gambler is a casual or professional gambler engaged in a trade or business.⁴⁷ These factors are sensitive to the facts and circumstances of each individual and include whether the taxpayer engages in gambling full-time—not simply as a hobby—and gambles with the primary purpose of making income for a livelihood.⁴⁸ Title 26 of the Code of Federal Regulations Section 1.183-2(b) also provides a list of nine factors which should normally be taken into account when determining whether an activity is engaged in for profit.⁴⁹ The nine factors are:

- (1) Manner in which the taxpayer carries on the activity;
- (2) The expertise of the taxpayer or his advisors;
- (3) The time and effort expended by the taxpayer in carrying on the activity;
- (4) Expectation that assets used in activity may appreciate in value;
- (5) The success of the taxpayer in carrying on other similar or dissimilar activities;
- (6) The taxpayer's history of income or losses with respect to the activity;
- (7) The amount of occasional profits, if any, which are earned;
- (8) The financial status of the taxpayer; and
- (9) Elements of personal pleasure or recreation.⁵⁰

⁴³ Treas. Reg. § 31.3402(q)-1(c) (2016); Denis McDevitt ET AL., *Mr. Park Goes to D.C.: Federal Taxation of NonResident Aliens' Wagering Gains from Slot Machines and the Per-Session Rule*, 48 CREIGHTON L. REV. 65, 112 n. 26 (2014).

⁴⁴ McDevitt, *supra* note 43 at 106 n. 155 (summarizing the holding in *Barba* ("stating the purpose of enacting withholding on gross income is to "increase" revenue and make administration of laws easier"); see *Barba v. United States*, 2 Cl. Ct. 674, 677 (1983).

⁴⁵ *Shollenberger*, 2009 T.C.M. LEXIS 310, at *5.

⁴⁶ See *Free-Pacheco v. United States*, 117 Fed. Cl. 228, 259 (2014).

⁴⁷ *Comm'r v. Groetzinger*, 480 U.S. 23, 35-36 (1987).

⁴⁸ See *Free-Pacheco*, 117 Fed. Cl. at 258-59.

⁴⁹ Treas. Reg. §§ 1.183-2(b)(1)-(9) (as amended in 1972).

⁵⁰ *Id.*

Although the general rule is the burden of proving professional gambler status is on the taxpayer and not the casino, this determination should be made by the casinos first before taking advantage of the new withholding requirement because the new withholding requirement does not apply to professional gamblers.⁵¹ Once the determination is made that a player is not a professional by applying the factors above on a case-by-case basis, IRS classifies all non-professional gamblers as casual players.⁵²

III. INCOME IN GENERAL

Title 26 U.S.C. Section 61 provides that gross income means all income from whatever source derived.⁵³

In general, non-resident taxpayers are required to pay tax on all income generated in the United States. Reg. Section 1.871-1 provides that income can be divided into three categories: income connected with a U.S. trade or business; income not effectively connected with a U.S. trade or business; and income that is exempt from U.S. tax.⁵⁴

And “[g]ains from wagering transactions are included in gross income” through 26 U.S.C. Section 61.⁵⁵

A. *The Determination of a Casual Gambler’s Gross Income from Slot Machine Play*

There are two opposing methods for determining income from a casual gambler’s slot machine play. One method is the per-bet method and the other is the per-session method.

1. *The Per-Bet Illustration—The Old Method*

Before 2008, IRS and the courts calculated gambling income on a per-bet basis for non-resident taxpayers.⁵⁶ Under the per-bet method, when a non-resident gambler won money from a casino, the casino would have to track and withhold 30% and give the player the 70% winnings each time that player won per transaction (e.g. each pull of the slot machine).⁵⁷ A simplified example of the per-bet analysis is: a tourist from China walks into a casino in the United States and plays the Wheel of Fortune slot machine.⁵⁸ The first bet, the player

⁵¹ *Free-Pacheco*, 117 Fed. Cl. at 259.

⁵² *See Groetzinger*, 480 U.S. at 987.

⁵³ 26 U.S.C. § 61(a) (2012).

⁵⁴ *See* Jason Borkes, *Nonresident Alien Gamblers Get Similar Treatment as U.S. Gamblers*, TAX ADVISER (Oct. 31, 2013), <http://www.thetaxadviser.com/issues/2013/nov/clinic-story-04.html>.

⁵⁵ I.R.S. Notice 2015-21, *supra* note 25.

⁵⁶ *See Barba*, 2 Cl. Ct. at 675-78.

⁵⁷ Borkes, *supra* note 54.

⁵⁸ *Id.*

wins \$1,500, but on the second and final bet, he loses \$1,500.⁵⁹ Under the per-bet analysis, on the first bet, the casino would have interrupted the gambler, withheld \$450 from him, and the player would have to report \$1,500 in income on his 1042-S tax return.⁶⁰ Neither the casino nor the player is happy with this scenario. The casino is unhappy because the withholding removes the \$450 dollars that could have been kept in play by the gambler and creates a lost opportunity to win the \$450 back from the gambler. Further, withholding on every win interrupts the gambler's entertainment and experience with paperwork.

Casinos currently following the per-bet method report winnings on slot play in excess of \$1,200 or more because \$1,200 is the threshold required to file a Form W-2G.⁶¹ When non-resident gamblers visit the United States and play slot machines, the same threshold is used as a matter of custom. For each win of \$1,200 or more, casinos currently following the old per-bet method file a Form 1042-S and withhold at a thirty percent rate, unless accepted by treaty on wagering gains.⁶² Thus, under the per-bet practice, when a single slot spin results in a payout of \$1,200 or more, regardless of the amount bet, the slot machine is set to lock up; a slot attendant is called for a hand pay and issues a tax form to comply with federal rules for withholding or information reporting.⁶³

If a jackpot requiring either a Form W-2G or Form 1040-S occurs, the casino will ask the player for a taxpayer identification number and picture ID before paying the jackpot.⁶⁴ "The player will be issued one or more copies of the Form W-2G or Form 1042-S, which shows date, time, amount of gross winnings, and tax withheld, if any."⁶⁵

2. The Per-Session Illustration

After 2008, the courts and the IRS in its Office of Chief Counsel Memorandum AM2008-011 found "a casual gambler, . . . who plays the slot machines" should no longer use the per-bet bases and instead recognize his or her wagering gains or losses at the time she redeems her winnings.⁶⁶ The

⁵⁹ *Id.*

⁶⁰ *See id.*

⁶¹ INTERNAL REVENUE SERVICE, *2016 Instructions and Forms W-2G and 5754* (2016).

⁶² 26 U.S.C. § 871(a)(1)(A) (2012).

⁶³ McDevitt, *supra* note 43, at 68-69; *see also* Treas. Reg. § 7.6041-1(b)(2) (1977) (providing that the amount reported on either Form W-2G or Form 1040-S as gross winnings from slots is not reduced by the amount of the winning bet).

⁶⁴ McDevitt, *supra* note 43, at 69 & n.11 (stating that "[s]ome states such as Iowa, also automatically withhold state tax").

⁶⁵ McDevitt, *supra* note 43, at 69.

⁶⁶ *See Shollenberger*, 2009 T.C.M. LEXIS 310, at *2-3; *see also Park*, 722 F.3d at 387; *see generally* Memorandum from George J. Blaine, Associate Chief Counsel,

relevant case law and memorandum will be discussed at length in Part IV. This method is hereinafter referred to as the per-session-basis. Under the per-session-basis, play is not interrupted at each win like the per-bet method. Instead, income is determined at the time the player redeems his or her ticket from the slot machine.⁶⁷

In calculating gross income under the per-session-basis, wagering losses are allowed to the extent of wagering gains under §165(d) from such transactions.⁶⁸ In interpreting this limitation, the significance of the term “transactions” is paramount to define what gambling winnings and what gambling losses are.⁶⁹ Section 165(d) “uses the plural term ‘transactions’ implying that gain or loss may be calculated over a series of separate plays or wagers.”⁷⁰

To illustrate this new rule in a simplified way, and how it effects a non-resident taxpayer and the casino, visualize a player sitting down at a slot machine. On her first bet, she wins \$1,500.⁷¹ The player is not interrupted by any paperwork or withholding; instead, she is able to gamble longer and with more money. On her second and last bet for the session, the player loses the entire \$1,500.⁷² Under the per-session approach, the casino gained \$1,500 instead of the \$1,050 the casino would have made under the per-bet method, which would have required withholding of \$450. As a result, the player does not have any income to report because her gain or loss was measured over the session of her play at the slot machine.⁷³ This session results in zero gambling income for the player to report and allows the casino to realize more gains in gambling revenue instead of losing those gains due to old withholding requirements.

This change in the method for determining income from casual gambling slot play has major implications with respect to reporting gambling winnings and non-resident taxpayer withholdings. The important takeaway is that if no gambling income occurs then it would follow that no withholding would be required. Simply put, if there is zero income then any percentage of withholding on income would be zero, meaning more money is left in play for a longer period of time.

I.R.S., to Roland Barral, Area Counsel 4 (Dec. 12, 2008) (on file with the IRS) [hereinafter “I.R.S. Memo AM2008-011”]; *see also infra* Part IV.

⁶⁷ McDevitt, *supra* note 43 at 93-94.

⁶⁸ 26 U.S.C. §165(d) (2012); *see also* I.R.S. Notice 2015-21, *supra* note 25.

⁶⁹ I.R.S. Memo AM2008-011, *supra* note 66, at 4.

⁷⁰ *Id.*

⁷¹ *See* Borkes, *supra* note 54.

⁷² *See id.*

⁷³ *See id.*

B. The Problem

Why does the per-bet method appear to continue for non-resident players despite the change from “per-bet” to “per-session” in determining gambling income? Are gamblers required to compute gambling winnings on every winning bet—i.e. every winning pull of the slot machine? Or can they report the overall gambling income minus gambling losses from a session of gambling?

IV. THE TRANSITION—OFFICE OF CHIEF COUNSEL MEMORANDUM AM2008-011, *SCHOLLENBERGER*, AND *PARK*

In 2008, the Office of Chief Counsel issued Memorandum AM2008-011 (hereinafter referred to as CCA) outlining how a casual gambler determines his or her wagering gains or losses from slot machine play.⁷⁴ Noting §165(d)’s guidance on words “gains and losses” from wagering transactions lacked an explanation of technical meaning, the IRS advised casual gamblers who play slot machines to recognize gains or losses at the time they redeem their tokens.⁷⁵ This CCA would later be used to justify the change from the per-bet to per-session-basis for non-resident taxpayers and used by the courts in their analysis in post-2008 cases.

The reason non-resident taxpayers are now permitted to use the per-session-basis for slot machine play ironically developed in a case involving U.S. citizens. In 2009, U.S citizen taxpayers in *Shollenberger* argued that they were entitled to offset their gambling winnings against their gambling losses (which exceeded their winnings) in determining their gross income.⁷⁶ While playing slot machines in a West Virginia casino, Mr. Schollenberger hit a \$2,000 jackpot on a dollar slot machine playing at the casino after withdrawing \$500 from a joint checking account.⁷⁷ Mr. and Mrs. Schollenberger “each took \$200 out of the jackpot winnings for additional slot machine play” and later left the casino with \$1,600, which was deposited into their joint account.⁷⁸ On their Form 1040A, the Schollenbergers did not report any gambling winnings.⁷⁹ “By notice of deficiency, the [IRS] determined that [the Schollenbergers] had \$2,000 of unreported income from gambling winnings.”⁸⁰

The Shollenbergers argued the court should interpret §165(d) to allow the calculation of gross income from slot machine play by netting all their 2005

⁷⁴ I.R.S. Memo AM2008-011, *supra* note 66, at 4.

⁷⁵ *Id.* at 3-4.

⁷⁶ *Shollenberger*, 2009 T.C.M. LEXIS 310, at *5.

⁷⁷ *Id.* at *2 (2009).

⁷⁸ *Id.*

⁷⁹ *Id.*

⁸⁰ *Id.*

slot machine gains and losses.⁸¹ The Court disagreed and held “[s]ection 165(d) does not define gross income but instead limits the deductibility of losses on wagering ‘transactions’ to the amount of gains from wagering ‘transactions,’” noting that the per-session-basis applied to casual gamblers.⁸² Thus, the Schollenbergers had \$1,100 of unreported gross income and were not entitled to a deduction for gambling losses because U.S. citizens do not treat every play or wager as a taxable event, and as a result, they measure their gambling winnings and losses on a per-session-basis.⁸³

The two formally separate worlds of how U.S. citizens determine gambling income versus how non-resident aliens computed gambling income collided in Sang J. Park’s journey through the judicial system. Park, a South Korean citizen, “played slot machines recreationally in the United States in 2006 and 2007.”⁸⁴ During 2006 and 2007, Park won \$431,658 and \$103,874.⁸⁵ “Park did not report those winnings on his 2006 and 2007 federal income tax returns” because he argued that if the per-session approach is the best approach for U.S. citizens to measure gambling gains, there is no reason non-resident taxpayers should not be permitted to use the same approach.⁸⁶ “After the IRS sent deficiency notices for 2006 and 2007, Park petitioned the Tax Court for relief.”⁸⁷ The Tax Court held that income from a non-resident taxpayer’s earnings of \$436,658 and \$103,874 over the course of two years “was taxable to the United States because an existing treaty between the United States and South Korea did not exempt the gambling winnings of South Korean citizens from U.S. tax and the income was not effectively connected with a U.S. trade or business.”⁸⁸ Park appealed.⁸⁹

In 2013, *Park* was decided upon appeal from the United States Tax Court.⁹⁰ At the United States Court of Appeals, District of Columbia Circuit, Park, the non-resident taxpayer, did not take the approach of arguing whether the income was taxable.⁹¹ Instead, Park argued against the IRS’s assertion that he had to pay taxes based upon the per-bet method, calculating income on every winning pull at the slot machine under Title 26 U.S.C. section

⁸¹ *See id.* at *2-3, *7-8.

⁸² *Id.* at *8.

⁸³ *Id.*

⁸⁴ Charles J. Reichert, *D.C. Circuit Rejects Per-Bet Approach for Nonresident Alien*, J. OF ACCT. (Sept. 30, 2013), <http://www.journalofaccountancy.com/issues/2013/oct/per-bet-approach.html>.

⁸⁵ *Id.*

⁸⁶ *Id.*

⁸⁷ *Id.*

⁸⁸ *Id.*; *Park*, 722 F.3d at 387.

⁸⁹ *See Park*, 722 F.3d at 384.

⁹⁰ *Id.* at 385.

⁹¹ Reichert, *supra* note 84.

871(a)(1)(A).⁹² While the IRS argued that the per-session approach applied only to U.S. citizens and that gambling gains for non-resident taxpayers should be calculated on a per-bet basis because of old case law, Park was persistent in arguing the per-session analysis in *Schollenberger* applied to him too.⁹³

The IRS's "non sequitur" response was to persuade the court to follow the per-bet method by citing *Barba v. United States*, a Claims Court decision from 1983.⁹⁴ This strategy failed. The D.C. court rejected the argument that *Barba* was binding because "[t]he [*Barba*] case did not consider whether to measure gains on a per-session-basis or a per-bet basis."⁹⁵ In writing its decision, the court also completely dismantled IRS's theory that per-session only applied to U.S. citizens by highlighting IRS's contradicting statements.⁹⁶ On one hand, in the case against Park, the IRS advocated for a per-bet method of accounting for slot machine gambling income.⁹⁷ On the other hand, an IRS memorandum offered guidance to the public in calculating slot machine income; the IRS advocated for a per-session approach because "the per-session approach avoids the considerable administrative and practical difficulties that would arise if slots players had to track the wins [per-bet]."⁹⁸ If the per-session theory of calculating income on a per-session-basis was good enough for the IRS in their memorandum to the public, the per-session-basis was good enough for both U.S. citizens and non-resident taxpayers.⁹⁹

In a final blow to the IRS's theory that non-resident gamblers should only be allowed to use the per-bet method, the court wrote:

Nothing in the IRS's [Memorandum AM 2008-11, Office of Chief Counsel, Internal Revenue Service 4(2008)] turned on the fact that the gamblers were U.S. citizens. . . .we are persuaded that the per-session approach and not the per-bet approach is the better approach [for non-resident taxpayers] for the reasons the IRS itself persuasively explained [in its memorandum]. . . .We thus decline the IRS's invitation to read the term "gains" in Section 871 to mean something different from what it has been interpreted to mean in Section 165(d). We conclude that the relevant provision of the Tax Code, Section 871, allows non-resident [taxpayers] to calculate winnings or losses on a *per-session* basis.¹⁰⁰

Ultimately, the D.C. Circuit Court of Appeals followed the same rationale as the court in *Schollenberger*, even though non-resident taxpayers generally were treated differently from U.S. citizen gamblers.¹⁰¹ In order to be clear in

⁹² *Park*, 722 F.3d at 386.

⁹³ *Id.*; Reichert, *supra* note 84.

⁹⁴ *Park*, 722 F.3d at 387.

⁹⁵ *Id.*

⁹⁶ *See generally id.*

⁹⁷ *Id.* at 385-86.

⁹⁸ *Id.* at 386-87.

⁹⁹ *See generally id.*

¹⁰⁰ *Id.* at 386-87.

¹⁰¹ *See id.* at 385-86.

illustrating the prior unfairness to non-resident taxpayer, the Court specifically noted the differences by way of a hypothetical. In the first example, a U.S citizen could walk into a casino to play slots and at first win \$100 but then lose \$100 before leaving and report \$0 in income because of the per-session-basis.¹⁰² In the second example, a non-resident taxpayer who, if put in the same situation as the U.S citizen, wins \$100 and loses \$100, the non-resident would have to report \$100 in income because the IRS interpreted the tax code to require non-resident taxpayers to pay taxes on gains from each bet.¹⁰³ By correcting IRS's prior incorrect methodology of assessing a per-bet method on non-resident taxpayer slot machine gains, the court set a precedent that will dramatically affect the gambling experience for these players and income for casinos catering to international gamblers.

Although some interpret the *Park* decision to mean only non-resident taxpayers are now eligible for refunds, their interpretation falls short of the ultimate impact of the case.¹⁰⁴ Because of the court's holding that the per-session analysis applies to non-resident taxpayers, the withholding requirement for the casinos has been effectively removed until the end of the player's gambling session. Thus, the withholding requirement, if any, is determined at the end of the session and allows the casino an opportunity to win more of the money back from the player. Accordingly, amounts formerly withheld now have a very good chance of landing on the casinos' income statement. The process of how to implement a system that follows the case law above and provides opportunities for casinos is explained in the following segment.

A. The Opportunity Arising from Slot Machine Based Session Tracking

"Every year roughly \$265 million is spent on regulating the gaming industry, including [regulating] slot machines."¹⁰⁵ Before reaching the casino floor and ultimately consumers, slot machines are picked apart by lengthy compliance tests before the games are approved by regulators.¹⁰⁶ The extensive testing is conducted to add an extra layer of security to the gambler and regulators so that the games are "fair and reliable."¹⁰⁷

Previously, it was a complicated process to change a slot machine.¹⁰⁸ A specially trained employee had to stop any play on the machine, open it, replace the computer chip inside, and then change the marketing display.¹⁰⁹ "The alteration usually took a day and could cost thousands of dollars, from

¹⁰² *Id.* at 385.

¹⁰³ *See id.* at 385-87.

¹⁰⁴ *See generally* McDevitt, *supra* note 43.

¹⁰⁵ AM. GAMING ASS'N, *supra* note 6.

¹⁰⁶ *Id.*

¹⁰⁷ *Id.*

¹⁰⁸ Richtel, *supra* note 27.

¹⁰⁹ *Id.*

ordering parts to modifying the machine.”¹¹⁰ Now, casino executives can go to their office and control the machines with the touch of a button.¹¹¹ Technological advances in player tracking cards make it easier and less costly to monitor game play and each gambler’s purchase in a casino.¹¹²

To track the gambling session, casino operators need only make slight software modifications to player tracking systems and internal controls standard in most gaming properties. Modern slot machine player tracking technology is represented as a marketing activity; however, it does in fact track the amount wagered and the amount won during slot machine play provided that the player uses a card that is integrated into the slot machine.¹¹³ Most slot machines today are largely credit based devices that track the amounts tendered into the machines, as well as the result of each wager made in a running balance fashion.¹¹⁴ Modern slot machines do not employ the use of cash or tokens as they have in the past, but instead use Ticket-In/Ticket-Out (TITO) methods of accounting for wagering activity.¹¹⁵

Newly developed software could be used in connection with a player tracking card, which could be employed to withhold amounts equal to the required withholding under §1441(a) as the session progresses. In effect, well-designed software could keep any potential tax withholding due in escrow until the end of the session. For most, it is expected that losses will offset winnings during the session. Accordingly, less withholding should occur, resulting in money formerly withheld now being available for the casino to win back.

Many casinos already segregate their large denomination slot machines into VIP areas that provide a higher level of security and observation of play making it easier to track sessions.—Complementing this already existing internal control, a casino should consider employing existing systems to provide an automated tax complainant system, which could withhold, or place in escrow, winnings on a per-bet basis. Then, benefiting the non-resident and casino, the system would release all or part of the amounts back after accounting amounts actually owed using the session-basis. This process may also be completed after the session but before the gambler returns home. However, if the process is automated as indicated above with a player tracking card, it would enhance the

¹¹⁰ *Id.*

¹¹¹ *Id.*

¹¹² See Chris Warner, *Slot Machines Get Personal with Player Tracking*, ADVANTAGE BUS. MEDIA (July 8, 2014, 9:18 AM), <https://www.pddnet.com/article/2014/07/slot-machines-get-personal-player-tracking>.

¹¹³ Z. Wang & H. Aquino, *Casino Technology: Player Tracking and Slot Accounting Systems*, 6 UNLV GAMING RES. & REV. J. 43, 43–44 (2002).

¹¹⁴ See *History of Slots*, POKERSTARS, <https://onlinecasino.pokerstars.com/guide/slots-in-popular-culture-and-facts/> (last visited Oct. 2, 2016).

¹¹⁵ Armando Flores, *Why Ticket-In/Ticket Out is the Way to Go*, OFF THE ROLL (Dec. 30, 2014), <http://transact-tech.com/blog/why-ticket-inticket-out-is-the-way-to-go>.

players' gaming experience.

It is of absolute importance that all wins and losses of the non-resident taxpayer be accounted for during the session.¹¹⁶ The \$1,200 reporting threshold only applies to form W-2Gs, not 1042-S forms. Failure to account for each win and loss would place the casino at risk of fine or penalty for failure to comply with various tax regulations.¹¹⁷

In order for each property to get a sense of what is at stake, they should query their accounting department regarding the total withholding from slot machine play reflected on their Form 1042. Such an analysis should compare the historical withholding on a per-bet basis with pro forma current per-session rule results against the same data. The results of this analysis will offer an idea of the potential increase in win on an annual basis. Such an analysis would also identify patrons of U.S casino properties who could benefit from this opportunity.

V. IRS NOTICE 2015-21 AND STATUTORY GUIDANCE – THE COUNTERARGUMENTS

A. IRS Notice 2015-21

The main reason that may prevent some casino properties from altering their current withholding practices is that the IRS has not publicly come out and acknowledged that per-session-basis applies to non-resident taxpayers. On March 4, 2015, the IRS published Notice 2015-21.¹¹⁸ “Notice 2015-21 contains a proposed revenue procedure that would permit gamblers engaging in electronically tracked slot machine play an optional safe harbor method to determine a wagering gain or loss from their slot machine play based on day-long play sessions.”¹¹⁹ However, Notice 2015-21 is misleading for three reasons. First, although the notice correctly states what slot machines are and the per-session-basis rule, it fails to include the per-session applicability to non-resident taxpayers. Second, Notice 2015-21 neglects to provide guidance going forward to casinos in order to correct improperly withheld gambling income from non-resident taxpayers. Third, by failing to offer a solution, Notice 2015-12 encourages the over-reporting of withholding on slot machine winnings. By

¹¹⁶ See 26 U.S.C. §§ 871 (a)(1)(A), 871(j) (2012). 871(a)(1)(A) imposes the tax to gambling income and 871(j) provides exceptions. Slot machines are not included in the exceptions and therefore subject to the tax.

¹¹⁷ Paula Singer, *Form 1042/1042-S-Related Penalties Part 1: Failure to Meet Withholding Obligations*, THOMSON REUTERS: TAX & ACCT. BLOG (Apr. 29, 2013), <https://tax.thomsonreuters.com/onesource-nonresident-alien-taxation/form-10421042-s-related-penalties-part-1-failure-to-meet-withholding-obligations/>.

¹¹⁸ I.R.S. Notice 2015-21, *supra* note 25.

¹¹⁹ Sally P. Schreiber, *IRS Proposes New Slot Machine Tax Rules*, J. OF ACCT. (Mar. 3, 2015), <http://www.journalofaccountancy.com/news/2015/mar/calculating-gambling-gains-or-losses-201511896.html>.

not addressing the fact that casinos are not required to withhold until the end of the session of play for non-resident gamblers, players and casinos are misled into believing that their only remedy is a refund. Encouraging the refund model instead of advising casino properties not to withhold until the end of the session only benefits the IRS and not the player nor the casinos. The IRS gains more tax revenue by over-reporting on a per-bet model and putting a band-aid on the problem by offering a piecemeal refund.

The beginning of Notice 2015-21 starts out by defining electronically tracked slot machine play as: “slot machine play using an electronic player system that is controlled by the gaming establishment (such as through the use of a player’s card or similar system) and that records the amount a specific individual won and wagered on slot machine play.”¹²⁰ The notice goes on to also accurately describe the safe-harbor provision, in which “a taxpayer would recognize a wagering gain if, at the end of a single session of play, the taxpayer’s total gains exceeded his or her losses and would recognize a loss if, at the end of the session, the total amount of wagers exceeds the amount of payouts.”¹²¹

After *Park* was decided in 2013, the IRS conveniently ignored the fact that they unfairly treated non-resident taxpayers gains on slot machines play and neglected to acknowledge losing the *Park* case in Notice 2015-21. Notice 2015-21 provides authority for session-based accounting for slot machine play only for U.S. citizens and omits the per-session applicability to non-resident taxpayers, despite the 2013 *Park* decision which indicates that the per-session analysis now has equal importance for both domestic and non-resident taxpayers in determining gross income from the casual gamblers slot machine player.¹²² Any reference to the treatment of non-resident taxpayers is buried in section 7 and only describes refund examples for taxes withheld from non-resident taxpayers instead of providing counsel on how to prevent the withholding errors going forward.¹²³

Tax refunds most commonly occur when the taxpayer pays more tax during the year than he or she actually owes to the government.¹²⁴ However, there is no need for the government and the taxpayer to go through the lengthy refund process when slot machine income is not withheld in the first place based upon the per-session method. The IRS muddles the issue of which session method to use with the concept of refunds in Notice 2015-21 and cited section 873, suggesting that deductions are otherwise limited, and offered

¹²⁰ I.R.S. Notice 2015-21, *supra* note 25, at 6.

¹²¹ I.R.S. Notice 2015-21, *supra* note 25, at 7.

¹²² *See generally* I.R.S. Notice 2015-21, *supra* note 25; *see generally Park*, 722 F.3d at 384.

¹²³ *See* I.R.S. Notice 2015-21, *supra* note 25, at 10.

¹²⁴ *What is a Tax Refund?*, TURBOTAX, <https://turbotax.intuit.com/tax-tools/tax-tips/General-Tax-Tips/Video—What-Is-a-Tax-Refund-/INF14680.html> (last visited Mar. 2, 2017).

“deductions are allowed only to the extent that they are connected with income that is effectively connected with the conduct of a trade or business within the United States.”¹²⁵ By simply regurgitating section 873 and allowing only for the possibility of refunds, the IRS confuses deductions and refunds with the per-session-based determination of gross income that predicates the subject withholding, as explained in *Park*.¹²⁶

The Proposed Revenue Procedure contained in Notice 2015-21 provides a limited explanation of per-session-based determination of income from slot machine play but does not address W-2G or 1042-S returns which currently report on the per-bet basis.¹²⁷ Continuing reporting on the per-bet basis and not the per-session-basis results in substantial over-reporting.¹²⁸ For example, after the *Park* decision, Enrique Pacheco, a non-resident taxpayer brought suit to recover a tax refund in excess of \$16 million accounting for the refund of amounts previously over withheld under the per-bet method.¹²⁹

It is important to note “[t]he safe harbor will not be available until it is published as a final revenue procedure, after which it would apply to tax years ending on or after that date.”¹³⁰ In the interim, the IRS’s Proposed Revenue Procedure in Notice 2015-21 defines a session in section 3 paragraph 4 as follows:

A session of play begins when a patron places the first wager on a particular type of game and ends when the same patron completes his or her last wager on the same type of game before the end of the same calendar day. For purposes of this section, the time is determined by the time zone of the location where the patron places the wager. A session of play is always determined with reference to a calendar day (24-hour period from 12:00 a.m. through 11:59 p.m.) and ends no later than the end of that calendar day.¹³¹

Applying this definition to an example, a casual gambler could play slot machines at Casino A from 10:00 a.m. to 12:00 p.m. and from 3:30 p.m. to 5:00 p.m.¹³² All of these time frames could “be combined into one session per this revenue procedure (if it is finalized).”¹³³ However, that same gambler

¹²⁵ See I.R.S. Notice 2015-21, *supra* note 25, at 1.

¹²⁶ See generally *id.*; see also *Park*, 722 F.3d at 384-87.

¹²⁷ See generally I.R.S. Notice 2015-21, *supra* note 25.

¹²⁸ See *supra*, Part III (A) and (B); see also *Park*, 722 F.3d at 384 (Court simplified example in the differences of \$100 wagering win and loss for both a U.S. citizen and non-resident taxpayer); *Free-Pacheco*, 117 Fed. Cl. at 228.

¹²⁹ See *Free-Pacheco*, 117 Fed. Cl. at 235.

¹³⁰ Schreiber, *supra* note 119.

¹³¹ I.R.S. Notice 2015-21, *supra* note 25, at 6.

¹³² Russ Fox, *IRS Proposes Session Method for Slot Machine Play and a Revision to the Regulations on Gambling Information Returns*, TAXABLE TALK (Mar. 3, 2015), <http://www.taxabletalk.com/2015/03/03/irs-proposes-session-method-for-slot-machine-play-and-a-revision-to-the-regulations-on-gambling-information-returns/>.

¹³³ *Id.*

could not play slot machines from 11:00 p.m. to 1:00 a.m. and claim that only one session had occurred.¹³⁴ Instead, there would be a total of two sessions, 11:00 p.m. to 11:59 p.m. and 12:00 a.m. to 1:00 a.m.¹³⁵ If the revenue procedure is finalized, gamblers would not be permitted to offset gains and losses from two different sessions.¹³⁶ “Once a gambler goes to another [casino], a new session would begin, even if it is on the same calendar day.”¹³⁷

Due to the Revenue Procedure contained in Notice 2015-21, taxpayers and casinos now have the proposed IRS definition of what a casual gamblers slot machine play session is.¹³⁸ Applying this definition of a session to slot play of a non-resident taxpayer determines income from slot machine play. Regardless of Notice 2015-21’s lack of clear direction as to non-resident taxpayers, casinos can still be assured that a determination of income from casual slot machine play is valid for non-resident taxpayers because of the *Park* decision.¹³⁹ Next, an examination of the statutes that require withholding on the gambling winnings of non-resident taxpayers who are not otherwise exempt by treaty will follow.

B. Sections 871 and 1441(a)—Statutes Imposing Tax on Non-Resident Players and Withholding Requirements on Casinos

As discussed earlier in the gross income section, non-resident taxpayers “pay tax on U.S.-source income that is effectively connected to a U.S. trade or business at graduated rates and pay tax on fixed or determinable annual or period income and certain other income at a flat rate (generally, 30%).”¹⁴⁰ The tax is imposed on all “interest . . . dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income.”¹⁴¹ The key term in the context of analyzing a non-resident gambler income is the term “gains.”¹⁴² It is important to note that only fixed gains are subject to tax.¹⁴³ Here, in the gambling context, gains from slot play are determined by a per-session-basis.¹⁴⁴

¹³⁴ *Id.*

¹³⁵ *Id.*

¹³⁶ Schreiber, *supra* note 119.

¹³⁷ *Id.*

¹³⁸ See I.R.S. Notice 2015-21, *supra* note 25, at 6.

¹³⁹ See *Park*, 722 F.3d at 387.

¹⁴⁰ Danny Hollingsworth, *Tax Treatment and Planning Strategies for Nonresident Individuals*, THE TAX ADVISER (June 30, 2015), <http://www.thetaxadviser.com/issues/2015/jul/hollingsworth-jul15.html>.

¹⁴¹ 26 U.S.C. § 871 (a)(1)(A) (2015); *Park*, 722 F.3d at 386.

¹⁴² *Park*, 722 F.3d at 386.

¹⁴³ 26 U.S.C. § 871 (a)(1)(A) (2015).

¹⁴⁴ See, e.g., *Park*, 722 F.3d at 386; *Shollenberger*, 2009 T.C.M. LEXIS 310, at *3; *Laplante v. Comm’r*, 98 T.C.M. (CCH) 305, at *5 (2009).

26 U.S.C. section 1441(a) is the authority that imposes the deduction, withholding of tax on non-resident taxpayers, and creates a burden on the casino to withhold such tax on income.¹⁴⁵ But, under the per-session-basis, when there is no taxable gain under section 871, it follows there will be no withholding under section 1441(a) for non-resident individuals.¹⁴⁶ As aforementioned, because the odds favor the casino over time, the per-session-based method of determining income is expected to yield fewer gross income events under section 871(a) that would require withholding under section 1441(a).¹⁴⁷

VI. ATTORNEY INTEREST IN FILING REFUND CLAIM RETURNS

The consideration of this issue would not be legitimate without mentioning some scholars feel that “casinos should not in any way interpret *Sang Park* to be a relief from their obligation to withhold.”¹⁴⁸ Instead, they argue that withholding should continue as it has before.¹⁴⁹ The application of *Park*, as proposed in this note, would prevent the practice of over-withholding that causes the conditions for most claims. Some counsel resist change from the status quo because it would be bad for business of firms who profit from filing refund claims. We should measure this potential influence when considering articles addressing this subject matter.

Nonetheless, given the ruling in *Park*, the per-session guidance for determining wins and loses does, in fact, form the basis of a claim for the subject refunds.¹⁵⁰ However, casinos that withhold gambling winnings using the per-session-basis in real time accurately determine the correct gross income of the casual slot machine player, thereby avoiding the need for over-withholding and the costly claim process entirely.¹⁵¹ What most fail to recognize is that it is the casino that is in the best position through their tracking devices, use of internal controls, and other real time processing technology to account for the session properly in the first place, thereby eliminating the need for the refund process to a great extent.¹⁵²

¹⁴⁵ 26 U.S.C. § 1441(a) (2014).

¹⁴⁶ *Id.*; see *Park*, 722 F.3d at 387; 26 U.S.C. § 871(a)(1)(A) (2015).

¹⁴⁷ *The Odds of Gambling*, PBS, <http://www.pbs.org/wgbh/pages/frontline/shows/gamble/odds/odds.html> (last visited Sept. 29, 2016); 26 U.S.C. § 871(a)(1)(A) (2015); 26 U.S.C. § 1441(a) (2014).

¹⁴⁸ McDevitt, *supra* note 43, at 106.

¹⁴⁹ *Id.*; See also *Barba*, 2 Cl. Ct. 674, 677 (1983) (stating the purpose of enacting withholding on gross income is to increase revenue and make administration of laws easier).

¹⁵⁰ See *Park*, 722 F.3d at 387.

¹⁵¹ See generally Terry Sheridan, *Tax Compliance Will Cost Americans \$409 Billion in 2016*, ACCT. WEB (June 22, 2016), <http://www.accountingweb.com/tax/irs/tax-compliance-will-cost-americans-409-billion-in-2016>.

¹⁵² Flores, *supra* note 115.

The software adjustments that a casino implements to track play on a per-session-basis have benefits for the taxpayer too. A non-resident taxpayer's effort to file a claim for refund on the per-session-basis presents challenges. For example, non-resident taxpayers would be required to piece together an accounting of a casual activity that happened years ago when the need for records was not foreseen, provided for, or retained in the ordinary course of the casino's business. It is doubtful that such an effort by the non-resident taxpayer would produce an equally accurate result when a casino proactively calculates accurate compliance from the start. Ultimately, following the proposal of waiting until the end of the session to calculate taxpayer gains and losses would assist non-resident customers of casinos in avoiding a time sucking refund process, while at the same time allowing the casinos to keep more money in play.

VII. CONCLUSION

The United States, as well as many other countries, is experiencing a progressive expansion of legalized gambling.¹⁵³ Therefore, the issue of the taxation of gaming will be increasingly important as states looking for tax revenue resources legalize gambling.¹⁵⁴

At this point in history, the gaming environment is facing a great deal of change.¹⁵⁵ From dealing with how to address Internet gaming, to trying to reinvent Las Vegas for the next generation, the casinos in Las Vegas and around the country are under increasing pressure.¹⁵⁶ During these challenging times, we see big properties are for sale, some are going through bankruptcy, and others being torn down.¹⁵⁷ But, for properties that are able to adapt to ever changing laws, the payoff could be big considering slot machines generate over \$7 billion annually in Nevada alone.¹⁵⁸

¹⁵³ Kurt Eggert, *Truth in Gaming: Toward Consumer Protection in the Gambling Industry*, 63 MD. L. REV. 217, 218 (2004).

¹⁵⁴ See *States Roll the Dice on Legal Gambling*, CBSNEWS (Jan. 25, 2009, 9:57 PM), <http://www.cbsnews.com/news/states-roll-the-dice-on-legal-gambling/>.

¹⁵⁵ See *Design by Evolution: How to Maximize and Reinvent Every Space in Your Existing Casino*, HNEDAK BOBO GROUP (Jan. 11, 2016), <http://www.hbginc.com/design-by-evolution-how-to-maximize-and-reinvent-every-space-in-your-existing-casino/>.

¹⁵⁶ Roberto Coppola, *Is Your Casino Optimized for Millennials?*, MARKETING RES. ASS'N (Apr. 28, 2015), <http://www.marketingresearch.org/article/your-casino-optimized-millennials>.

¹⁵⁷ See *Famous Las Vegas Casino Demolished*, TELEGRAPH (June 14, 2016, 3:48 PM), <http://www.telegraph.co.uk/news/2016/06/14/famous-las-vegas-casino-demolished/>; see generally Angelo Young, *Caesars Entertainment Bankruptcy: Company Seeks Timeout as Creditors Clash with Private Equity Firms*, INT'L BUS. TIMES (June 6, 2016, 9:29 PM), <http://www.ibtimes.com/caesars-entertainment-bankruptcy-company-seeks-timeout-creditors-clash-private-equity-2378784>.

¹⁵⁸ Richtel, *supra* note 27; See generally *Free-Pacheco*, 117 Fed. Cl. at 2235 (the

Recent developments in the interpretation of how slot machine gambling winnings are determined for non-resident players may present an opportunity for casinos to prevent over-withholding and over-reporting of gambling winnings.¹⁵⁹ Based upon a consideration of slot machine play in the United States, the amount over reported on Form 1042-S is substantial.¹⁶⁰ Under current law, casinos have sufficient authority under *Park* and *Schollenberger* for using a per-session-basis of accounting for determining gross gambling income and any required withholding for non-resident slot machine players.¹⁶¹

After considering market demographics, individual casinos may use this analysis as a marketing strategy to attract more foreign players to the United States and increase their bottom line. The changes relative to the laws concerning non-resident casual gamblers who play slot machines would cause fewer interruptions throughout play and increase enjoyment in their gaming experience.¹⁶² If properly implemented and paired with a well-designed session-based compliance processes, these changes offer a positive step in the direction of addressing tax-driven competitive disadvantages imposed on U.S. gaming businesses.

taxpayer sought a refund of more than \$16 million).

¹⁵⁹ See generally *Park*, 722 F.3d at 387.

¹⁶⁰ Richtel, *supra* note 27.

¹⁶¹ See *Park*, 722 F.3d at 386-87; *Shollenberger*, 2009 T.C.M. LEXIS 310, at *3.

¹⁶² See *Park*, 722 F.3d at 386.