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Internal Revenue Service (I.R.S.)

Technical Advice Memorandum

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Section 4401 -- Wagering Tax (Taxable v. Not Taxable)
4401.00-00 Wagering Tax (Taxable v. Not Taxable)

TR-32-217-91

District Director * * *
Taxpayer's Name: * * *
Taxpayer's Address: * * *
Taxpayer's Identification No.: * * *
Years Involved: * * *
Conference Held: * * *

LEGEND:

X = * * *
Y = * * *

ISSUE

Is a pull-tab ticket operation conducted by X, an Indian tribal government, as part of its bingo gaming operation a lottery subject to the federal excise taxes on wagering imposed under sections 4401(a) and 4411 of Chapter 35 of the Internal Revenue Code?

FACTS

X is a federally recognized Indian tribe under 25 U.S.C. section 1758(a) and has a federally protected right to conduct bingo gaming operations on its reservation free of regulation by the State of Y.
In 1986, X commenced public bingo gaming operations. Patrons participate in these bingo games by purchasing an admission to a bingo hall, which entitles them to a basic package of bingo playing cards. Generally, patrons come for an entire bingo session, arriving before games commence and leaving at the end of the session. These operations have always included the sale of pull-tab tickets during the bingo sessions. Pull-tab tickets are sold only at the bingo hall during bingo sessions. Patrons must purchase their admission to the bingo game in order to have the opportunity to purchase pull-tabs, as well as additional bingo playing cards over and above the basic package sold with the admission. Pull-tabs are sold by X individually, for a price of between $.25 and $2.00 for each ticket. When a patron purchases a ticket, he is required to open the tabs on the ticket without leaving the premises; the ticket is void if the patron leaves the premises before opening the ticket. If the ticket is a winning ticket, the patron is paid the prize immediately upon presenting the opened ticket. X purchases tickets from vendors who sell tickets in boxes containing between 2,000 and 24,000 tickets each. X knows the predetermined number of winning tickets in each box. Each box is used until all tickets are sold, but if any tickets remain unsold at the end of a bingo session they become available for sale at the next session.
All revenues from X's bingo operations, including net revenues from the sale of pull-tab

tickets, are deposited in the general fund of X and expended solely for the operation of the tribal government.

APPLICABLE LAW

Section 4401(a)(1) of the Code imposes on any wager authorized under the law of the State in which accepted an excise tax equal to 0.25 percent of the amount of such wager.
Section 4401(a)(2) of the Code imposes on any wager not described in section 4401(a)(1) an excise tax equal to 2 percent of the amount of such wager.
Section 4401(c) of the Code provides that each person who is engaged in the business of accepting wagers shall be liable for and shall pay the tax under this subchapter on all wagers placed with him. Each person who conducts any wagering pool or lottery shall be liable for and shall pay the tax under this subchapter on all wagers placed in such pool or lottery. Any person required to register under section 4412 who receives wagers for or on behalf of another person without having registered under section 4412 the name and place of residence of such other person shall be liable for and shall pay the tax under this subchapter on all such wagers received by him.
Section 4411 of the Code imposes a special wagering tax to be paid by each person who is liable for tax under section 4401.
Section 4421(1) of the Code provides that the term "wager" means, among other wagers, any wager placed in a lottery conducted for profit. Section 4421(2)(A) of the Code provides that the term "lottery" includes the numbers game, policy and similar types of wagering, but does not include any game of a type in which usually, (i) the wagers are placed, (ii) the winners are determined, and (iii) the distribution of prizes or other property is made, in the presence of all persons placing wagers in such game.
Section 44.4421-1(b) of the Wagering Tax Regulations provides that--
(1) The term "lottery" includes the numbers game, policy, and similar types of wagering. In general, a lottery conducted for profit includes any scheme or method for the distribution of prizes among persons who have paid or promised a consideration for a chance to win such prizes, usually as determined by the number or symbols on tickets drawn from a lottery wheel or other receptacle, or by the outcome of an event, provided such lottery is conducted for profit. . . . The operation of a punchboard or a similar gaming device for profit is also considered to be the operation of a lottery.
Section 4421-1(b)(2) of the regulations provides that--
(i) Section 4421 specifically excludes from the term "lottery" any game of a type in which usually (a) the wagers are placed, (b) the winners are determined, and (c) the distribution of prizes or other property is made, in the presence of all persons placing wagers in such game. Thus, for example, no tax would be payable with respect to wagers made in a bingo or keno game since such a game is usually conducted under circumstances in which the wagers are placed, the winners are determined, and the distribution of prizes is made in the presence of all persons participating in the game. For the same reason, no tax would apply in the case of card games, dice games, or games involving wheels of chance, such as roulette wheels and gambling wheels of a type used at carnivals and public fairs.
Revenue Ruling 57-258, 1957-1 C.B. 418, holds that a pull-tab game is a taxable lottery as that term is used in section 4421 of the Code.
Section 4402(3) of the Code exempts state-conducted lotteries from federal wagering taxes.
Section 7871(a)(2) of the Code provides that an Indian tribal government shall be treated as a State subject to subsection (b), for purposes of any exemption from, credit or refund of, or payment with respect to an excise tax imposed by--
(A) chapter 31 (relating to tax on special fuels),
(B) chapter 32 (relating to manufacturers excise taxes),
(C) subchapter B of chapter 33 (relating to communications excise tax), or
(D) subchapter D of chapter 36 (relating to tax on use of certain highway vehicles).
Section 7871(b) of the Code provides that paragraph (2) of subsection (a) shall apply

with respect to any transaction only if, in addition to any other requirement of this title applicable to similar transactions involving States or political subdivisions thereof, the transaction involves the exercise of an essential government function of the Indian tribal government.
In 1988 Congress enacted The Indian Gaming Regulatory Act, Pub. L. 100- 497, 25 U.S.C. section 2701 (the "IGRA") which, effective October 7, 1988, permits Indian tribes to conduct certain "Class II" games, which are defined as including bingo and, if played in the same location, pull-tabs.
Section 20(d) of the IGRA, 25 U.S.C. section 2719(d) (here-after section 2719(d)), provides that--
(1) The provisions of title 26 [the Internal Revenue Code] (including sections 1441, 3402(q), 6041, and 6050I, and chapter 35 of such title) concerning the reporting and withholding of taxes with respect to the winnings from gaming or wagering operations shall apply to Indian gaming operations conducted pursuant to this chapter, or under a Tribal-State compact entered into under section 2710(d)(3) of this title that is in effect, in the same manner as such provisions apply to State gaming and wagering operations.

RATIONALE

X argues that it is not subject to the federal excise taxes on wagering.
First, X argues the pull-tab game conducted by X is not a "lottery" within the meaning of section 4421(a) of the Code. Pull-tab games conducted as part of X's bingo operations fall outside the statutory definition of "lottery" because they are "live" or "instant" games within the scope of the exemption described in section 4421(2)(A). As operated by Indian tribal governments, the pull-tab games are sub-games of bingo, played in connection with a live bingo session. In X's games, all tickets must be purchased and redeemed during a single bingo session, and can only be purchased by patrons who have purchased an admission to the particular bingo session. Congress has expressly recognized in the IGRA that, as routinely played in connection with Indian bingo operations, the pull-tab game is closely related to the "live" bingo game conducted at Indian bingo halls throughout the country.
In the alternative, X argues that since the enactment of the IGRA, X's pull-tab games are entitled to the express exemption granted to state lotteries under section 4402(3) of the Code by virtue of section 2719(d).
The position of the Internal Revenue Service, as set forth in Rev. Rul. 57-258, is that pull-tab games are subject to federal wagering taxes because they are essentially nothing more than a type of punchboard. Section 44.4421- 1(b) of the regulations provides that punchboards are lotteries for purposes of the wagering taxes. The regulation is in accord with S. Rep. No. 781, 82nd Cong., 1st Session (1951), 1951-2 C.B. 458, which was issued in connection with the wagering tax provisions enacted by the Revenue Act of 1951, section 471, 26 U.S.C. sections 3285-3287. The Report, at page 540, indicates that a punchboard would not normally be excluded by section 4421(2)(A) of the Code from the definition of a lottery.
In its report that accompanied the Revenue Act of 1951, the House Committee on Ways and Means indicated that for purposes of the excise tax on wagers the definition of a lottery is intended to be broad in scope. With regard to the term "lottery" the Committee stated that--
Although the bill does not contain an all-inclusive definition of the term "lottery", in general the term is intended to mean any scheme for the distribution of property by chance among persons who have paid or have agreed to pay a valuable consideration for the chance, whether called a lottery, raffle, gift enterprise, or some other name.
H.R. 586, 82nd Cong., 1st Sess. (1951), 1951-2 C.B. 357, 398.
Thus, the definition of the term "lottery," as envisioned by Congress, is broad enough to include pull-tab gaming unless, as provided for under the exclusion in section 4421(2)(A) of the Code, the pull-tab game is of a "type in which USUALLY (i) the wagers are placed, (ii) the winners are determined, and (iii) the distribution of prizes or other property is

made in the presence of all persons placing wagers in such game." (Emphasis added.) As played in retail establishments, county fairs, charitable events, etc., pull-tab games are not USUALLY operated so that the wagers are placed, winners determined, and prizes are distributed in the presence of all bettors.

In addition, although Congress has, for purposes of the IGRA, included in the same category both bingo and pull-tab games if played at the same location and bingo is excluded from tax under section 44.4421-1(b)(2) of the regulations, such recognition does not effect the taxability of pull-tab games for federal excise tax purposes.

X's second argument concerns the effect of section 2719(d) upon the gaming operations of Indian tribes. X asserts that section 2719(d) provides that Indian gaming operations will be treated, for purposes of the federal wagering taxes, in the same manner as state gaming operations. Section 4402(3) of the Code exempts state-conducted lotteries from federal wagering taxes. In pertinent part, section 2719(d) provides that, "[t]he provisions of title 26 (including sections 1441, 3402(q), 6041, and 6050I, and chapter 35 of such title) concerning the reporting and withholding of taxes with respect to the winnings from gaming or wagering operations shall apply to Indian gaming operations . . . in the same manner as such provisions apply to State gaming and wagering operations."

A literal reading of section 2719(d) leads to the conclusion that section 2719(d) only relates to provisions of the Internal Revenue Code concerning THE REPORTING AND WITHHOLDING OF TAXES WITH RESPECT TO WINNINGS. X argues that, since chapter 35 does not contain specific reporting or withholding requirements for states, if the Service only applies the section 2719(d) treatment of tribes as states to the sections of the Code relating to the reporting and withholding of taxes with respect to winnings, it will render meaningless the statutory reference to chapter 35. This, X asserts, is an impermissible reading since, under a basic principle of statutory construction, a statute should not be construed in a way that renders portions or phrases superfluous. King v. Internal Revenue Service, 688 F.2d 488, 491 (7th Cir. 1982).

Additionally, X argues that it is a settled principle of statutory construction that federal statutes affecting Indian tribes are to be "liberally construed, doubtful expressions being resolved in favor of the Indians." Bryan v. Itasca County, 426 U.S. 373, 392, (1976). X also notes that, in accord with this principle, Congress, in enacting the IGRA, indicated that:

[c]ourts will interpret any ambiguities on these issues in a manner that will be most favorable to tribal interests consistent with the legal standard used by courts for over 150 years in deciding cases involving Indian tribes.

S. Rep. No. 446, 100th Cong., 2d Sess., at 15, reprinted in 1982 U.S. Code, Cong. & Admin. News 3081, 3085.

Accordingly, in applying these principles of construction, X reads the section 2719(d) qualifying clause to describe provisions of the Internal Revenue Code that EITHER concern "the reporting and withholding of taxes with respect to the winnings from gaming OR concern "wagering operations." X believes that Congress' use of the disjunctive word "or" in section 2719(d) indicates that it intended that the terms connected by the disjunctive be given separate meanings. By arguing that the "or" separates the reference to "the reporting and withholding of taxes with respect to winnings from gaming," from the reference to "wagering operations," X believes that the operative language of section 2719(d) regarding chapter 35 is that--

The provisions of the Internal Revenue Code of 1986 (including . . . chapter 35 of such Code) concerning . . . wagering operations shall apply to Indian gaming operations conducted pursuant to this chapter . . . in the same manner as such provisions apply to State gaming and wagering operations.

This reading, X asserts, gives meaning to the section 2719(d) reference to chapter 35, but a reading that is limited to "the reporting and withholding of taxes with respect to winnings" effectively repeals the chapter 35 reference because states have no reporting or withholding requirements under that chapter.

We do not find X's reading of section 2719(d) to be persuasive. Such a reading ascribes too much meaning to the use of the disjunctive "or" in the descriptive phrase "gaming or

wagering," particularly where section 2719(d) later refers to "gaming and wagering" operations. The grammatical object of the reporting and withholding requirements is "taxes with respect to winnings from gaming or wagering operations," with the phrase "gaming or wagering" being merely an adjectival phrase descriptive of the term "operations." As drafted, the term "operations" in section 2719(d) must be read with both adjectives, "gaming" and "wagering", even though a disjunctive is used, and the parenthetical reference to chapter 35 should not be read as applying only to "wagering operations" with the remaining references in the parenthetical applying only to "gaming." There is no basis for separating the parenthetical reference. Also, although the parenthetical reference in section 2719(d) should not be ignored, it is an unnecessary reference that is not controlling in interpreting section 2719(d). Without the parenthetical the meaning of section 2719(d) is clear:

[t]he provisions of title 26 . . . concerning the reporting and withholding of taxes with respect to the winnings from gaming or wagering operations shall apply. . . .

Should title 26 be amended to add or delete provisions concerning the reporting and withholding of taxes, the meaning of section 2719(d) would remain unchanged.

X's argument also fails to take into account that state governments are not totally exempt from wagering taxes. The exemption is limited to certain specific types of wagers, placed with specified state agencies. If a state agency enters into a wager that is not an exempt wager (for example, if a state agency accepts a wager on a sporting event that is not a pari-mutual wager), the state is liable for wagering tax and must abide by the recordkeeping and reporting requirements of the Code. Thus, an Indian tribal government that is required to report taxable wagers is treated in the same manner as a state that is required to report taxable wagers.

Additionally, section 2719(d) actually imposes a reporting burden on the Indian tribal governments. The Internal Revenue Code sections enumerated in section 2719(d) require states to report and withhold tax on winnings in excess of stated dollar amounts. Treating Indian tribal governments in the same manner as states for purposes of those sections requires the tribal governments to report and withhold tax on their customers' winnings from gaming activities. Concededly, the reference to chapter 35 is less clear because there are no specific requirements for reporting or for withholding of tax contained in chapter 35, other than requirements implicit in the registration requirements under section 4412. However, we believe that in considering, (1) what excise tax exemptions Congress has extended to Indian tribal governments, and (2) the legislative history of section 2719(d), it is apparent that Indian tribal governments are not entitled to exemption under section 2719(d).

In considering exemptions for Indian tribal governments, section 7871(a)(2) of the Code provides that an Indian tribal government will be treated as a state for purposes of certain enumerated federal excise taxes. Wagering taxes are not enumerated. Thus, prior to the IGRA it is evident that Congress did not intend to exempt Indian tribal governments from the wagering taxes.

In order to ascertain whether Congress intended to grant a wagering tax exemption to tribal governments in the IGRA we have reviewed the legislative history of the IGRA. S. Rep. No. 446 details changes made by the Senate Committee on Indian Affairs to the text of S. 555 (the bill underlying IGRA). As originally introduced, section 20(d) of the bill read as follows--

Provisions of the Internal Revenue Code of 1986, concerning the TAXATION and the reporting and withholding of taxes with respect to gambling or wagering operations shall apply to Indian gaming operations conducted pursuant to this Act the same as they apply to State operations. (Emphasis added.)

As enacted, section 20(d)(1) makes no reference to TAXATION with respect to Indian gaming operations. The focus of the section, as enacted by Congress, was the application of the reporting and withholding requirements to Indian tribal governments. The reference to the taxation of such governments was specifically deleted prior to enactment. Further, the "Section by Section Analysis" in S. Rep. No. 446 also indicates Congressional intent by providing that section 20(a)-(d) of the Act:

Sets forth policies with respect to lands acquired in trust after enactment of this act and applies the Internal Revenue Code to WINNINGS from Indian gaming operations. (Emphasis added.)
The wagering taxes imposed by sections 4401 and 4411 of the Code are concerned with the TAXATION of persons engaged in the business of accepting wagers. Section 2719(d) specifically applies to the WINNINGS from gaming or wagering operations and is concerned only with what is won by the bettor and to what extent Indian tribal governments should report and withhold taxes with respect to those winnings.

CONCLUSION

The pull-tab ticket operation conducted by X as part of its bingo gaming operation is a lottery subject to the federal excise taxes on wagering imposed under sections 4401(a) and 4411 of the Code.
A copy of this technical advice is to be given to the taxpayer. Section 6110(j)(3) of the Code provides that it shall not be used or cited as precedent. Under section 6110(c) names, addresses, and identifying numbers have been deleted.

END OF DOCUMENT