

**Office of Chief Counsel
Internal Revenue Service
Memorandum**

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from: Stephanie Bland
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subject: Taxability of Wagering Conducted by Certain Municipalities

This Chief Counsel Advice responds to your request for assistance, dated March 11, 2011, regarding the taxability of wagering conducted by certain municipalities. This advice may not be used or cited as precedent.

ISSUE

Whether municipal governments in Alaska are subject to the wagering and occupational taxes imposed by §§ 4401 and 4411 of the Internal Revenue Code (Code), or whether such governments fall within the exemption set forth in § 4402(3) for wagers placed in a sweepstakes, wagering pool or lottery conducted by an agency of a state.

CONCLUSION

Municipal governments in Alaska are not agencies of a state acting under authority of state law for purposes of § 4402(3). Therefore, Alaska municipalities that engage in taxable wagering activities are subject to tax under §§ 4401 and 4411.

BACKGROUND AND FACTS

Certain Alaska municipalities currently conduct various types of wagering activities, including lotteries, raffles, pull-tab games, and various types of races and contests of skill. A question arose concerning whether these municipalities are liable for tax under §§ 4401 and 4411, or whether they fall within the exemption set forth in § 4402(3). This

advice does not address whether any one particular type of activity is considered wagering for purposes of the Code. Rather, this advice assumes an activity is wagering for purposes of the Code, and only addresses whether an Alaska municipality are subject to the wagering and occupational taxes imposed by §§ 4401 and 4411.

LAW AND ANALYSIS

Section 4401(a) imposes a tax on wagers authorized under state law.

Section 4421 provides the definition of the term “wager.” Under § 4421, the term “wager” includes any wager placed in a lottery conducted for profit.

Section 4402(3) provides that no tax shall be imposed on any wager placed in a sweepstakes, wagering pool, or lottery that is conducted by an agency of a state acting under authority of state law, but only if such wager is placed with the state agency conducting such sweepstakes, wagering pool, or lottery, or with its authorized employees or agents.

Section 4411 imposes an occupational tax on each person who is liable for the tax imposed under § 4401, or who is engaged in receiving wagers for or on behalf of any person so liable.

Alaska Stat. § 05.15.020 provides generally that a municipality or qualified organization may conduct an activity permitted under Alaska’s wagering laws, if the municipality or qualified organization applies for a permit, pays the appropriate permit fee, and receives an annual permit issued by the Alaska Department of Revenue.

Alaska Stat. § 05.15.100 provides generally that the Alaska Department of Revenue may issue a permit to a municipality or qualified organization to conduct bingo, raffles and lotteries, pull-tab games, ice classics, race classics, rain classics, goose classics, mercury classics, deep freeze classics, canned salmon classics, salmon classics, king salmon classics, dog mushers' contests, snow machine classics, fish derbies, animal classics, crane classics, cabbage classics, Calcutta pools, and contests of skill.

Alaska Stat. § 05.15.690(39) provides generally that the term “qualified organization” means a bona fide civic or service organization or a bona fide religious, charitable, fraternal, veterans, labor, political, or educational organization, police or fire department and company, dog mushers' association, outboard motor association, or fishing derby or nonprofit trade association in the state, that operates without profits to its members and that has been in existence continually for a period of three years immediately before applying for the license or permit.

The exemption under § 4402(3) was enacted as part of the Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, § 813(a), in response to Rev. Rul. 64-163, 1964-1 C.B. 403, which held that New Hampshire was subject to the wagering and occupational excise

taxes for a sweepstakes run by the state. The New Hampshire sweepstakes was based on the results of a horse race. As originally enacted, § 4402(3) exempted only wagers placed in a sweepstakes, wagering pool, or lottery (i) conducted by an agency of a state acting under authority of state law, and (ii) the ultimate winners of which are determined by the results of a horse race. Other states subsequently began to have their own lotteries that were not tied to horse racing. In response to these new state lotteries, Congress removed the horse race requirement from § 4402(3) as part of the Tax Reform Act of 1976, Pub. L. No. 94-455, § 1208(a).

The lotteries at issue here are not conducted by Alaska or one of its agencies, but rather by certain municipalities in Alaska. As the legislative history of § 4402(3) amply demonstrates, Congress intended an exemption for state-conducted wagering activities. There is no evidence, however, that Congress intended to expand the § 4402(3) exemption to anything other than state-conducted wagering activities.

Alaska law puts municipalities in the same category as any other “qualified organization” for purposes of wagering activities. Municipalities and other qualified organizations both have to apply for a gaming permit using the same application. Both have to designate natural persons who are in charge of the gaming activity and both have similar restrictions on who such person can be. Therefore, the fact that Alaska law does not distinguish between a municipality and a qualified organization for purposes of wagering activities demonstrates that Alaska municipalities are not agencies of a state acting under authority of state law for purposes of the wagering tax under § 4401 and the related occupational tax under § 4411. Accordingly, Alaska municipalities that engage in taxable wagering activities do not qualify for the § 4402(3) exemption, and are subject to the §§ 4401 and 4411 wagering and occupational taxes.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call (202) 622-3130 if you have any further questions.