

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

Number: **200725036**

Release Date: 6/22/2007

CC:ITA:B01:
POSTF-106091-05

UILC: 165.08-00

date: February 9, 2007

to: Associate Area Counsel (Las Vegas)
(Small Business/Self-Employed)

from: Andrew M. Irving
Senior Counsel, Branch 1
(Income Tax & Accounting)

subject: Partnership Wagering Gains and Losses

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

LEGEND

Taxpayer:

Partnership:

Business:

Other Activities:

Year 1:

ISSUE

Whether Taxpayer, a partner in Partnership may combine his share of the Partnership's wagering gains or losses with his personal wagering gains and losses in calculating his deductible wagering losses under § 165(d) of the Internal Revenue Code (the Code).

CONCLUSION

Taxpayer may combine his share of the Partnership's wagering gains or losses with his personal wagering gains and losses in calculating his deductible wagering losses under § 165(d) of the Code.

FACTS

Taxpayer has an ownership interest in Partnership, which owns and operates Business. Business provides entertainment in the form of gambling and related activities (Other Activities) to the public. As a part of its operation Business engages in wagering transactions.

In Year 1, Partnership's opening year, Business sustained an overall operating loss primarily the result of significant startup expenditures. (Operating losses are very unusual in Business's industry.) However, Business realized a gain on its wagering transactions. That year, Taxpayer lost substantial sums in personal wagering transactions.

Partnership issued to Taxpayer a Form K-1 reflecting Taxpayer's share of Partnership's ordinary business loss (line 22 of Form 1065) for Year 1, which Taxpayer reported as a non-passive ordinary loss for Year 1. Partnership separately stated the Taxpayer's share of Partnership's wagering gains and losses.

On an amended Form 1040, Taxpayer combined his share of Partnership's wagering gains and losses (a net gain) with Taxpayer's personal wagering gains and losses (a net loss) to calculate his deductible wagering losses under § 165(d). The adjustment gave Taxpayer a higher § 165(d) limit on the deductibility of his personal wagering losses.

LAW AND ANALYSIS

Section 165(a) allows a deduction for any uncompensated loss sustained during the tax year. Section 165(d) states that losses from wagering transactions are allowed only to the extent of the gains from such transactions. To determine the § 165(d) limit on losses from wagering transactions (i.e., the gains from wagering transactions), a taxpayer must calculate wagering gains and losses separately from other (non-wagering) income or loss.

Section 1.702-1(a)(8)(i) of the Income Tax Regulations provides that each partner shall take into account separately, as part of any class of income, gain, loss, deduction, or credit, the partner's distributive share of certain items, including "gains and losses from wagering transactions (section 165(d))" Pursuant to § 1.702-1(a)(8)(i), wagering gains and losses realized by a partnership are separately stated and pass through to its partners as separate items. The partner may then combine his separate share of the partnership's wagering gains and losses with his personal wagering gains and losses in calculating the partner's wagering losses deductible under § 165(d). In other words, § 165(d) is applied at the partner level, not the partnership level. The regulation is consistent with the legislative history behind § 702(a)(7), the statutory provision authorizing the regulation:

Paragraph (8) [current § 702(a)(7)] is a "catch-all" provision which authorizes the Secretary or his delegate to prescribe regulations to require each partner to take into account separately his distributive share of any other items of income, gain, loss, deduction, or credit, the character of which would affect the computation of the partner's personal income tax. For example, partnership gain or loss from gambling operations may be required to be segregated in order to permit individual partners to offset personal gambling gains and losses against their shares of such gains and losses realized by the partnership.

S. Rep. No. 1622, 83d Cong., 2d Sess. 377 (1954).¹ In effect, the separate passthrough of partnership wagering gains and losses to the partner ensures that a partner will account for all his/her wagering activity, including wagering conducted through a partnership, separately from other activities, as contemplated in § 165(d).

Under § 1.702-1(a)(8)(i), a partnership's wagering gains and losses are separately stated and passed through to its partners without regard to whether the other (non-wagering) activities of the partnership are profitable. For example, while it may be unusual, it is possible for a partnership to have a net gain from wagering and a loss from overall business operations, or a net loss from wagering and a gain from overall business operations. In either case, the partnership's wagering gains and losses flow to the partners as separate items.

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.

¹ See also *Jennings v. Commissioner*, 110 F.2d 945 (5th Cir. 1940), *cert. denied*, 311 U.S. 704 (1940); *Joseph v. Commissioner*, 43 B.T.A. 273 (1941). Cf. *Gordon v. Commissioner*, 63 T.C. 51, 81-82 (1974), *rev'd and rem'd on another issue*, 572 F.2d 193 (9th Cir. 1977) (income averaging context).

Please call if you have any further questions.

LEWIS J. FERNANDEZ
Associate Chief Counsel
(Income Tax & Accounting)

By: _____
Andrew M. Irving
Senior Counsel, Branch 1
(Income Tax & Accounting)