



News Release

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For Immediate Release

GAMBLING MAY RAISE YOUR TAXES... EVEN IF YOU LOST

NEW YORK, January, 2007 – The basic tax rule for gamblers is that winnings are taxable, but losses are deductible only to the extent of winnings. “Many taxpayers do not realize that the winnings and losses are reported in different places on the tax return. The net effect of this is that the losses you are allowed to report on your return are unlikely to completely prevent the winnings from increasing the tax you owe,” advises Bob D. Scharin, RIA Senior Tax Analyst from Thomson Tax & Accounting.

Gambling winnings increase your adjusted gross income. If you win big, the casino, state lottery commission, or other payor of the winnings will notify the IRS. (The reporting threshold depends on the type of gambling activity.)

At the same time, gambling losses, for all but professional gamblers, can be deducted (1) only as a miscellaneous itemized deduction and (2) only to the extent of winnings for the year. The good news is that this miscellaneous itemized deduction is not subject to the 2% of adjusted gross income deduction floor that applies to things like employee business expenses and investment advisory fees. The bad news is that itemized deductions are subtracted from adjusted gross income. Consequently, you cannot deduct gambling losses if you claim the standard deduction.

“Including gambling winnings in adjusted gross income and then deducting losses as an itemized deduction creates a mismatch of tax treatments,” says Scharin. Here are some examples of how the mismatch can cost you tax dollars. Assume you have \$20,000 of gambling winnings and \$20,000 or more of losses for 2006:

- Suppose you and your spouse would normally claim the standard deduction of \$10,300 on your 2006 joint return because your itemized deductions, aside from the gambling losses, total only \$5,000. Because your gambling winnings are taxable, you may itemize your deductions and claim \$20,000 of gambling losses (i.e., an amount equal to your gambling winnings). That brings your itemized deductions to \$25,000. This amount is only \$14,700 more than the standard deduction. Thus, your taxable income will be \$5,300 (\$20,000 of gambling income less \$14,700 increased deduction) higher because of the gambling activity.

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- Now assume you would have itemized your deductions even if you did not have the gambling income and losses. The deductions you itemize therefore increase by \$20,000—the same as the taxable gambling winnings. “At first glance, this looks like a wash for tax purposes; on closer inspection, however, you may feel like you’ve been hosed,” Scharin points out. “Because your adjusted gross income increased by \$20,000, tax deduction phaseouts may apply to you that otherwise would not.”

These phaseouts include a reduction in itemized deductions; college tuition tax credits or deductions; IRA deduction or Roth IRA contribution eligibility; and personal exemptions. “Sometimes moderate income retirees may find that they owe more tax on their Social Security benefits because their gambling winnings raised their adjusted gross incomes, even though their gambling losses prevented those winnings from raising their wealth,” Scharin says.

When it comes to gambling, the government is a fair-weather partner—taxing gains but not permitting deductions for net losses. In addition, if you win some and lose even more, the government often comes out ahead.

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