

The following is for use by assistive readers and users who prefer a text version of this course.

## Charitable Gaming for Exempt Organizations Course

1

Leagle – Welcome to the Charitable Gaming for Exempt Organizations Course.

This course is presented by the Exempt Organizations office of the IRS.

2

Leagle: Hi. I'm Leagle, the StayExempt Eagle, and I'll guide you through the courses here at StayExempt.

Before you start, there are a few things you should know. First, if you like to take written notes, you might want to print this course first. The print out may make it easier to follow along, especially if you haven't taken many online courses.

Next, if you have any problems navigating the courses here at StayExempt, feel free to take a look at our navigation tutorial.

This course also includes questions and activities that test your knowledge. You'll be instructed to click on the screen to participate in the activities.

3

Leagle: In this course we'll talk about the rules for Section 501(c)(3) organizations that conduct gaming activities. We'll also discuss how to determine withholding amounts - and how and when to report those gaming taxes appropriately.

4

Richard: Hi, I'm Richard. I am on the board of a Section 501(c)(3) organization called Cute and Curly Animal Rescue - and I've heard that charitable gaming can be a good way to fundraise. Can you help me?

Leagle: I sure can, Richard. From the Saturday night bingo in the church hall, to the video lottery at the veterans' club, and the poker tournament at the fraternal lodge – all are examples of gaming (or gambling) for organizations exempt from federal income tax.

Richard: Wow, that's a lot of different games.

Leagle: Charitable gaming is one of the most common and successful methods of producing income for many tax-exempt organizations. But remember that for almost all tax-exempt organizations, including 501(c)(3)s, gaming activities don't – by

themselves – further an exempt purpose. So you have to be careful about how much gaming you do - and pay attention to the additional tax and reporting requirements your gaming activities may produce.

Let's talk about how your organization can comply with IRS rules while conducting gaming activities.

5

Richard: Can you explain the rules for conducting charitable gaming?

Leagle: No problem! First, lawful gaming usually requires a gaming license from the state where your organization conducts the games.

And, to prevent gaming activities from jeopardizing your organization's federal tax exemption, you need to make sure the gaming doesn't become a substantial part of your organization's activities.

For certain games, some specific excise taxes and filing requirements may apply. And unless your game meets one of the exceptions to being treated as an unrelated business activity, the income may be "unrelated business income, (or UBI for short)," which is taxable to your organization, just like regular income.

Richard: What kinds of games or gambling fall under these rules?

Leagle: There are many games that may be exempt from UBI. Select the link for some examples.

6

Richard: I've taken your StayExempt course on Unrelated Business Income [link] and learned about the Three-Part test for Unrelated Business Income. Does the Three-Part test apply to gaming activities, too?

Leagle: Yes, it does, Richard. Generally, your gaming activity will be considered a trade or business – which is part one of the test – and, as I said earlier, it's not related to furthering your organization's exempt purpose, which is part three of the test.

So, if your organization regularly conducts gaming activity – part two of the test – the gaming income will be considered "unrelated business income," unless an exception applies.

7

Leagle: So consider this: Many states – as a condition of issuing a charitable gaming license – require games to be conducted by volunteers. How do you think that requirement will affect the tax treatment of your gaming income?

Richard: Well, I've already heard of the volunteer labor exception to UBI, so I assume that conducting an activity using a team of volunteers shouldn't generate any UBI.

Leagle: That's right! Gaming activities that are run using volunteer labor won't be treated as a source of UBI.

So, do you remember the "gaming-specific" UBI exception from the UBI course....

Richard: Let's see....Oh! How about the "bingo" exception?

Leagle: That's it! This exception applies to any game that's the traditional type of bingo, where all wagers are placed, all winners are determined and all prizes are awarded in the presence of everyone playing in that game. The game also has to be legal under state and local law, and has to be played in a jurisdiction where bingo games are not regularly conducted by for-profit organizations.

8

Leagle: There are a couple of other gaming-related exceptions to UBI.

The first – income from qualified public entertainment activities – will meet the exception if it's conducted by a qualifying organization and is the type of activity traditionally conducted at a fair or exposition promoting agriculture and education. A "qualifying organization" is an organization exempt under Section 501(c)(3), Section 501(c)(4) or Section 501(c)(5) that regularly conducts an agricultural and educational fair or exposition as one of its substantial exempt purposes.

Here's an example: Organization X, a 501(c)(5) agricultural organization, conducts harness racing at an agricultural fair in State L pursuant to a state law that permits the organization to conduct parimutuel betting in connection with the races. Income from wagers placed is excluded from the tax on unrelated business income.

The last UBI exception I'll mention includes most games of chance conducted by exempt organizations in North Dakota, as long as the conduct of the games doesn't violate a state or local law.

More details on these exceptions can be found in the "Public entertainment activity" and "Gambling activities other than bingo" paragraphs of Publication 598. [http://www.irs.gov/publications/p598/ch03.html#en\\_US\\_2011\\_publink1000267780](http://www.irs.gov/publications/p598/ch03.html#en_US_2011_publink1000267780)

9

Richard: So I get it - my organization's charitable gaming might be taxable if it doesn't meet one of these exceptions.

Leagle: You catch on fast, Richard. Remember that your taxable income involves two wagering excise taxes you need to know about. One applies to the amount wagered, the other applies to the people accepting the wagers. But neither applies to traditional, legal bingo. These excise taxes also don't apply to charitable gaming as long as none of the proceeds benefit private individuals or insiders.

This is good news for organizations exempt under Section 501(c)(3), because their income must not benefit private individuals or insiders. So, a properly operated 501(c)(3) wouldn't be subject to the federal wagering excise taxes for any legal gaming activities it conducts.

But for the benefit of any non-(c)(3) organizations that might be looking in, we'll go ahead and touch on these two excise taxes:

The first is a tax based on the gross amount of wagers received, which is reported and paid on Form 730 every month. The second wagering excise tax is an annual occupational tax imposed on each person liable for the tax on wagers or upon any person engaged in receiving wagers.

An organization would be liable for these taxes even if it doesn't conduct charitable gaming activities very often; just an annual raffle, for example. An organization also might be liable for these excise taxes even if its charitable gaming activity meets one of the UBI income tax exceptions.

Next, let's talk about the requirements for reporting winnings and withholding tax when conducting charitable gaming.

10

Leagle: So Richard, it's Saturday night and your organization is hosting a bingo game meeting the statutory bingo exclusion. Vernon pays \$5 for a bingo card and sits down to play. "B-I-N-G-O!!!" It's Vernon's lucky night. He wins the game and the jackpot of \$1,200. In tax terminology, the "wager" is \$5 and the "winnings" are \$1,200. Did you know that your organization must report Vernon's winnings to the IRS?

Richard: Wow, really? How do we know what to report? What form do we use?

Leagle: We'll go through all that now - and I'll point you to some resources you can use later.

To start, unless the winnings are from bingo, slot machines, keno or poker tournaments, you must report winnings, including raffle prizes, when the amount paid is:

- \$600 or more, and
- At least 300 times the amount of the wager

In determining whether the \$600 threshold is met, you have to subtract the wager from the winnings, depending on the type of gaming. See Publication 3079 for details.

You'll report to both the IRS and the winner on Form W2-G, Certain Gambling Winnings. The winner should provide you with proper identification, including his or her Social Security number, so you can report accurately. Send paper copies of copy A of Form W-2G to the IRS using Transmittal Form 1096.

11

Leagle: If your organization conducts bingo, keno, operates slot machines or runs a poker tournament the reporting rules differ slightly from those just described.

Richard: How so?

Leagle: For bingo and slot machines, you must report if gross winnings (before deducting the wager) equal \$1,200 or more.

With keno, if winnings after deducting the wager are \$1,500 or more, you'll report them.

For poker tournaments, the reporting threshold is higher – the winnings need to be more than \$5,000 after deducting the wager. In poker tournaments, the wager is usually called the entry or “buy-in” fee.

Richard: When do you file the W-2G?

Leagle: You complete and give copies B and C of Form W-2G to the winner at the same time you pay the winnings, or no later than by January 31 of the year after the year in which you paid the winnings. Send copy A to the IRS by February 28 or 29 of the year after the year in which you paid the gaming winnings.

[Note there are special reporting rules that apply to Foreign winners (Form 1042-S) and when the person receiving the winnings is not the actual winner or is a member of a group of winners to group winners (Form 5754). However, these topics are beyond the scope of this course.]

Now it's time to learn about the situations when you have to withhold tax on gaming winnings.

12

Richard: What is withholding?

Leagle: “Regular” withholding is the collection and depositing of federal income tax from the amount won. In some cases, when paying and reporting gambling winnings to prizewinners, tax-exempt organizations are required to withhold income tax from those winnings. (There is also “back-up” withholding, which we'll cover in a minute.)

The general rule for regular withholding is that you must withhold income tax from a payment of winnings when the proceeds from the wager are more than \$5,000 and the wager was placed in:

- A sweepstakes, wagering pool, lottery, raffle, or poker tournament; or,
- Any other wagering transaction, if such proceeds are at least 300 times the amount wagered.

The “proceeds from a wager” are the difference between the amount of the winnings and the amount of the wager.

13

Leagle: Remember that you do not need to withhold from traditional bingo, keno, or slot machines winnings no matter what the amount won. You don't need to withhold on winnings from a poker tournament either, as long as you report the winnings on Form W-2G.

Richard: OK, so I know when and when not to withhold – but how much does my organization withhold? And what does it do with the withheld amounts?

Leagle: The regular withholding rate is 25%. But check the instructions for Form W-2G to verify the rate for the year when you're paying a prize. The amount subject to withholding is the difference between the amount of the winnings and the amount of the wager. Withhold on the entire amount, not just on that portion greater than \$5,000.

Your organization will show the amount withheld in Box 4 of the Form W-2G that it will give to the winner and will send to the IRS.

In addition, your organization will report annually the total amount of federal income tax it withheld during the year on Form 945, Annual Return of Withheld Federal Income Tax, by January 31 following the close of the reporting year.

You also asked about what your organization should do with the withheld amount. Hang on to that question – We'll get back to it in a minute when we discuss Form 945 in more detail.

14

Richard: You mentioned another type of withholding a minute ago – “backup withholding” What is that, and how is it different?

Leagle: The backup withholding rate is higher, and under certain circumstances, you'll have to use it. So, when

- The winner of reportable winnings doesn't furnish a correct taxpayer identification number, or (TIN, for short),
- 25% has not been withheld, and
- The winnings are at least \$600 and at least 300 times the wager, or
- the winnings are at least \$1,200 from bingo or slot machines or
- \$1,500 from keno or
- more than \$5,000 from a poker tournament, then

Your organization will withhold and remit 28% of the winnings. If it chooses, your organization can reduce the amount of the winnings by the amount of the wager before figuring the withholding amount.

Remember that I said regular withholding doesn't apply to bingo, slot machines or keno. If a winner of one of these types of games doesn't provide you with his or her TIN, then the winnings will be subject to backup withholding if they are above the limits I just mentioned.

If your organization mistakenly pays a winner the entire prize when the winner hasn't provided his or her TIN, then your organization will be responsible for paying the backup withholding amount.

Like regular withholding, your organization must report backup withholding using Form W-2G and Form 945.

Next, let's talk about withholding when the prize is something other than cash

15

Richard: What if we conduct a fundraising raffle or other game where the prize is a car - or a big screen TV - or some other non-cash item? Does the organization still have to withhold taxes?

Leagle: Yes, the same withholding rules – and reporting rules, for that matter – apply whether the prize is cash or non-cash.

So if your organization is giving away prizes like a vacation or a big screen TV, the fair market value of the item won is the amount of the winnings. Regular or backup withholding rates will apply to these prizes just like they do for the cash prizes we've already discussed.

In the case of a non-cash prize that's large enough to require withholding, the winner may pay the 25% regular withholding amount to the organization. The organization would collect it when the prize is awarded.

The organization may opt to pay the regular withholding on behalf of the prize winner. However, if it does, the withholding rate is 33.33% of the fair market value of the prize.

And if the winner doesn't provide his or her identification number, your organization would backup withhold, just like it would for a cash prize.

Richard: So let me see if I've got it: Let's say my organization sells raffle tickets for \$2 for a grand prize of a flat screen TV with a fair market value of \$2,000. We'll give the winner a Form W-2G because the fair market value of the TV minus the wager (one ticket) is more than \$600 and more than 300 times the amount of the wager. We won't withhold though, because the total prize value is less than \$5,000. Right?

Leagle: Yes, as long as he or she gave your organization his or her correct TIN.

Now we've talked a little about reporting using Form 945 - but there's more you should know about the form.

16

Leagle: First of all, the IRS term for any taxes withheld from gaming winnings is "non-payroll withheld taxes." You report these withheld taxes on Form 945, Annual Return of Withheld Federal Income Tax, separately from any taxes you might have withheld from your organization's employees.

You'll report all non-payroll withheld taxes in one Form 945 filing, which is due no later than January 31 of the year after the year in which the taxes were withheld.

If the total tax withheld from your games' winners is less than \$2,500 for the entire year, your organization can pay it in full when it files the Form 945. Use the payment voucher Form 945-V to do this.

If the total withheld taxes will be \$2,500 or more for the year, your organization will need to deposit them by electronic funds transfer either monthly or semi-weekly. See section 11 of Publication 15 (Circular E), Employer's Tax Guide, for deposit instructions.

And for a non-cash prizes, remember to collect any required withholdings from the winners before your organization gives them their prize! If it doesn't, your organization will have to pay the taxes.

17

Leagle: Let's test your knowledge.

Select the correct answer. Which of the following statements is true of Form W-2G, Certain Gambling Winnings?

18

Leagle: Here's another question. Select the correct answer: For situations where a non-cash prize requires tax to be withheld, the organization should do what?

19

Richard: So, what kind of filing errors can my organization, or I, be penalized for?

Leagle: If your organization fails to file correct or complete information returns by the due date - or fails to furnish correct and complete payee statements without reasonable cause - it can incur penalties.

In addition, if your organization doesn't withhold and deposit taxes as required, a trust fund recovery penalty may apply. Under this penalty, the officers or employees of your organization – that's you, Richard – become personally liable for payment of taxes required to be collected, accounted for, and paid to the government (like withholding taxes) in an amount equal to the unpaid taxes.

Next, let's review what we've discussed.

20

Leagle: Here's what we've covered so far.

First, we learned some basics about Charitable Gaming – and I explained that it's a common and successful method for producing income for tax-exempt organizations. Gaming doesn't further the exempt purpose of an organization, so it will probably generate UBI. There are exceptions, exclusions and deductions that can apply.

There are also modifications to the UBI test that specifically apply to gaming. They explain when gaming is likely to be exempt from UBI tax. Remember to refer back to the graphic if you need help.



Then we went over the filing requirements for reporting winnings and the special requirements for keno, bingo and slot machines – and we talked about withholding requirements for regular withholding, backup withholding, withholding for non-cash prizes and reporting and depositing the amounts withheld.

Finally, we covered penalties.

21

Leagle: Let's test your knowledge. Select the correct answer: When the winner fails to provide his or her Taxpayer Identification Number, the game operator must do what?

When you're done, select the "submit" button to check your answer.

22

Leagle – Great job! You've completed the charitable gaming course. Remember that all of these topics and more are covered in detail in IRS Publication 3079, Tax-Exempt Organizations and Gaming.

Thanks for taking our course –and watch for more updated courses here at StayExempt!

23

Leagle: There were a lot of resources in this course, so feel free to go back through it. Here are some of the links to the major resources in this course.

24

Leagle: On behalf of everyone in the IRS Exempt Organizations division, thank you for taking the Charitable Gaming for Exempt Organizations Course.

**Leagle:** On behalf of Bobby and everyone in the IRS Exempt Organizations division, thank you for taking this *"Employment Issues"* Course.

If you have feedback for the Exempt Organizations team, feel free to [send us an email](#).

After you complete this review, print out your own [Certificate of Completion](#) as recognition for attending.