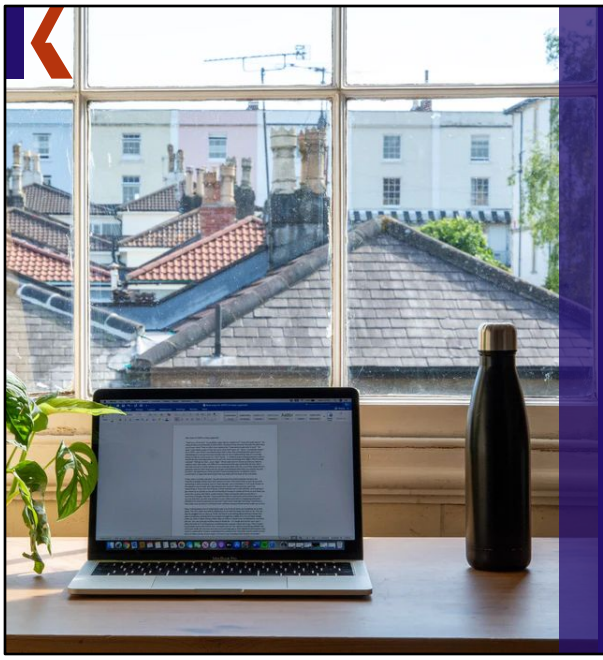

Current Federal Tax Developments

May 8, 2023

Kaplan Financial Education

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This Week We Look At:

IRS issues CCA making clear how strict the §125 substantiation rules are

Taxpayer's lack of documentation forces him to accept preparer's gross gambling winnings and limits his gambling loss deduction

Tax Courts finds that last second rule for filing a Tax Court petition is not the same as for returns filed via eFile

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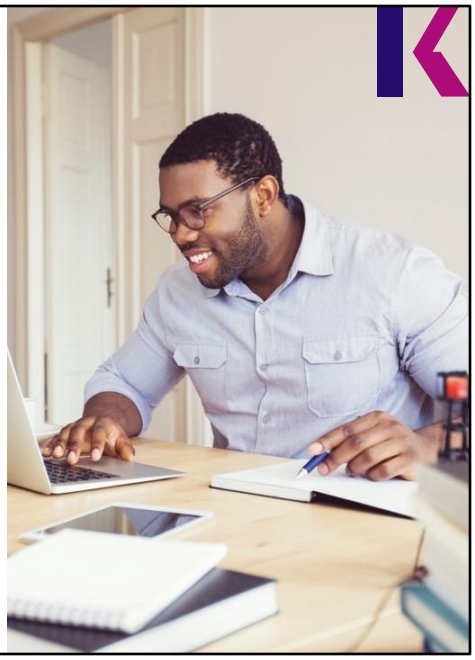

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

- Chief Counsel Advice 202317020, 4/28/23
  - Cafeteria plans under IRC §125 allow employers to allow deferrals from employee wages
  - But as with any tax benefit program, this comes with strings attached
  - A big string involves insuring that medical FSA and dependent care reimbursements be properly documented--and there are no exceptions under the Proposed Regulations

https://www.currentfederaltaxdevelopments.com/blog/2023/5/5/irs-issues-chief-counsel-advice-on-substantiation-rules-for-cafeteria-plans-and-dependent-care-assistance-programs

IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Section 125 allows an employer to establish a cafeteria plan that permits an employee to choose among two or more benefits, consisting of cash (generally, in the form of salary reduction) and qualified benefits, including accident or health coverage. Section 125 provides that the amount an employee contributes to the plan on a pre-tax basis through salary reduction that is applied to purchase the coverage is not included in gross income, even though it is available to the employees and the employee could have chosen to receive cash instead.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

If an employee elects to participate in a health FSA on a pre-tax basis through salary reduction under a section 125 cafeteria plan, the value of the coverage by the health FSA is excludable from gross income under section 106 as employer-provided accident or health coverage, and the amounts reimbursed for section 213(d) medical expenses are excludable from gross income under section 105(b) as amounts reimbursed for section 213(d) medical expenses. If an employee elects to participate in a dependent care assistance program paid for through salary reduction under a section 125 cafeteria plan, the dependent care assistance program benefits are excludable from gross income under section 129.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Prop. Reg. §1.125-1(c)(7)(ii)(G) provides that a failure to comply with the substantiation requirements of Prop. Reg. §1.125-6 results in a failure of the cafeteria plan to operate in accordance with section 125 and the Proposed Treasury Regulations thereunder. ***In general, a cafeteria plan that fails to operate in accordance with these requirements is not a cafeteria plan and employees' elections between taxable and nontaxable benefits result in gross income to the employees.***

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Prop. Reg. §1.125-6(b)(2) provides that all claims for reimbursement must be substantiated. Prop. Reg. §1.125-6(b)(2) provides that "[s]ubstantiating only a percentage of claims, or substantiating only claims above a certain dollar amount, fails to comply with the substantiation requirements of §1.125-1 and this section." See also Treas. Reg. §1.105-2; Rev. Rul. 2003-43, 2003-21 IRB 935 (holding that sampling techniques do not satisfy the substantiation requirements). Prop. Reg. §1.125-6(b)(3) provides that ***all claims for reimbursement must be substantiated by an independent third party and may not be self-substantiated.***

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Specifically, Prop. Reg. §1.125-6(b)(3) provides that "[a]ll expenses must be substantiated by information from a third party that is independent of the employee and the employee's spouse and dependents." All amounts paid under a health FSA that permits self-substantiation are included in gross income, including amounts that are reimbursed for medical expenses, whether or not substantiated. See Notice 2006-69, 2006-31 IRB 107, 109 (holding that self-certification does not satisfy the substantiation requirements).

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Flexible spending arrangements for dependent care assistance must follow the substantiation rules applicable to health FSAs. Prop. Reg. §1.125-6(g) provides additional rules for reimbursing dependent care assistance through a debit card. ***If an employee submits the dependent care expenses to the employer through a debit card, these expenses must be substantiated by providing a statement from the dependent care provider substantiating the dates and amounts for the dependent care services provided.***

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Prop. Reg. §1.125-6(a)(4) provides that reimbursements of dependent care expenses may not be reimbursed before the expenses are incurred. Dependent care expenses are incurred when the care is provided and not when the employee is formally billed or charged for (or pays for) the dependent care.

Prop. Reg. §1.125-6(b)(4) provides that reimbursing expenses before the expense has been incurred or before the expense is substantiated fails to satisfy the substantiation requirements of Treas. Reg. §1.105-2, Prop. Reg. §1.125-1 and Prop. Reg. §1.125-6(b)(4).

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

- Chief Counsel Advice 202317020, 4/28/23
  - Starts with two broad questions
  - IRS gives a series of fact patterns and results
  - IRS uses this to emphasize ***there are no shortcuts.***

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

(1) Are reimbursements of section 213(d) medical expenses to an employee from a health flexible spending arrangement (health FSA) provided in a section 125 cafeteria plan included in an employee's gross income under section 105(b) if any section 213(d) medical expenses of any employee are not substantiated in accordance with proposed regulation §1.125-6(b)?

(2) Will expenses be considered properly substantiated if employees self-certify expenses, if the plan substantiates only some expenses "sampling", if only amounts over a certain level (i.e., de minimis amounts) are substantiated, if charges with favored providers are not required to be substantiated, or if dependent care expenses are reimbursed before the expenses are incurred?

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Reimbursements of section 213(d) medical expenses to an employee from a health FSA provided in a section 125 cafeteria plan are included in the gross income of such employee if any expense of any employee reimbursed by the health FSA is not fully substantiated including if any expenses below a certain threshold are not substantiated.

If a section 125 cafeteria plan does not require an independent third party to fully substantiate reimbursements for medical expenses (for example, by permitting self-certification of expenses, "sampling" of expenses, or certification by favored providers), does not require substantiation for medical expenses below certain dollar amounts, or does not substantiate reimbursements for dependent care assistance expenses, then the plan fails to operate in accordance with the substantiation requirements of Prop. Reg. §1.125-6(b) and is not a cafeteria plan within the meaning of section 125. ***Therefore, the amount of any benefits that any employee elects under the cafeteria plan must be included in gross income and is wages for Federal Insurance Contributions Act (FICA) and Federal Unemployment Tax Act (FUTA) purposes subject to withholding.***

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

In addition, an employer may not exclude reimbursements of dependent care expenses from an employee's gross income if any expenses of any employee under the dependent care assistance program are not substantiated ***after the expense has been incurred.***

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Situation 1. An employer provides a section 125 cafeteria plan with a health FSA that reimburses section 213(d) medical expenses incurred by employees. The plan only reimburses section 213(d) medical expenses that are substantiated by information from a third party that is independent of the employee and the employee's spouse and dependents. In addition, the information from the third party describes the service or product, the date of service or sale, and the amount of the expense.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

In addition, the plan reimburses expenses based on information from an independent third party such as an "explanation of benefits" from an insurance company. The plan requires that information from the independent third party include (i) the date of the section 213(d) medical care, and (ii) the employee's share of the cost of the medical care (that is, coinsurance payments and amounts below the deductible). The plan also requires the employee to certify that any expense paid by the plan has not been reimbursed by insurance or otherwise and that the employee will not seek reimbursement from any other plan covering health benefits.

Lastly, the plan provides debit cards that can be used to reimburse section 213(d) medical expenses that meet the requirements of Prop. Reg. §1.125-6 (c), (d), (e), and (f).

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

In **Situation 1**, the substantiation of all claims complies with the requirements of section 105(b) and the proposed regulations under section 125 including the substantiation requirements under Prop. Reg. §1.125-6(b). Nothing in the way the plan substantiates the claims will prevent the employer from excluding the amounts reimbursed from the employee's income and wages for FICA and FUTA tax purposes.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Situation 2 – Self-Certification of Claims

Situation 2. Self-certification. Instead of only reimbursing expenses that are substantiated as described in Situation 1, the plan also reimburses employees for medical expenses for which an employee only submits information describing the service or product, the date of service or sale, and the amount of the expenses, but does not provide a statement from an independent third party (either automatically or after the transaction) to verify the expenses. Further, the plan does not substantiate debit card charges (including charges that are not auto-substantiated3 expenses for recurring medical expenses incurred at certain providers that match the amount, medical care provider, and time period of previously approved expenses) with a statement from an independent third party.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

In **Situation 2**, the self-certification of claims that are not otherwise substantiated does not ensure that every claim be substantiated. Because the plan does not limit reimbursements or payments of claims to medical expenses that are substantiated, the plan does not satisfy the cafeteria plan substantiation requirements under section 125. See Prop. Reg. §1.125-6(b) requiring substantiation for all claims, regardless of the amount, and Prop. Reg. §1.125-6(b)(3) prohibiting self-substantiation of medical expenses. See also Notice 2006-69, 2006-31, IRB 107 providing that all amounts paid under a health FSA plan that allows self-substantiation of medical claims are included in gross income.

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Situation 3 – Substantiation by Sampling

Situation 3. Sampling. In addition to reimbursing expenses that are substantiated as described in Situation 1, the plan reimburses all charges to the debit card and only requires substantiation of a random sample of otherwise unsubstantiated charges to the debit card (that is, charges that are not auto-substantiated) through third-party information describing the service or product and the date of the service or sale.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

In **Situation 3**, the sampling technique does not ensure that every claim is substantiated. Because the plan does not limit reimbursements or payments of claims to medical expenses that are substantiated, the plan does not satisfy the cafeteria plan substantiation requirements under section 125. See Prop. Reg. §1.125-6(b) requiring substantiation for all claims, regardless of the amount and Rev. Rul. 2003-43 holding that sampling techniques do not satisfy the substantiation requirements.

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Situation 4 - De Minimis Amounts Not Substantiated

Situation 4. De minimis. In addition to reimbursing expenses that are substantiated as described in Situation 1 or expenses that are auto-substantiated, if a charge to the debit card is less than a specified dollar amount, the plan does not require substantiation of the charge to the debit card through additional third-party information describing the service or product and the date of the service or sale.

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In **Situation 4,** the plan does not require employees to substantiate charges to the debit card for claims below a dollar threshold. Because the plan does not limit reimbursements or payments of claims to medical expenses that are substantiated (including expenses that are auto-substantiated), the plan does not satisfy the cafeteria plan requirements for substantiation under section 125. See Prop. Reg. §1.125-6(b) requiring substantiation for all claims, regardless of the amount.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Situation 5 – No Substantiation Required for Amounts Paid to Favored Providers

Situation 5. Favored providers. In addition to reimbursing expenses that are substantiated as described in Situation 1 or expenses that are auto-substantiated, if a charge to the debit card is from certain dentists, doctors, hospitals or other health care providers, the plan does not require substantiation of the charge to the debit card through additional third-party information describing the service or product and the date of the service or sale.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

In **Situation 5**, the plan does not require employees to substantiate charges to the debit card from certain dentists, doctors, hospitals, or other health care providers. Because the plan does not limit reimbursements or payments of claims to medical expenses that are substantiated (including expenses that are auto-substantiated), the plan does not satisfy the cafeteria plan requirements for substantiation under section 125. See Prop. Reg. §1.125-6(b) requiring substantiation for all claims, regardless of the amount.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Full Inclusion in Income Under Situation 2, 3, 4 and 5

In **Situation 2, Situation 3, Situation 4,** and **Situation 5**, the plan fails to satisfy the requirement to substantiate medical expenses. Reimbursements for unsubstantiated medical expenses under the cafeteria plan are not excludable from gross income under section 105(b). Therefore, in Situation 2, Situation 3, Situation 4, and Situation 5 all reimbursements made during the year, including amounts paid to reimburse substantiated medical expenses, are included in the gross income of the employees.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Situation 6 – Advance Substantiation for Dependent Care Assistance Program

Situation 6. Advance Substantiation for Dependent Care Assistance Program. An employer provides a section 125 cafeteria plan with a dependent care assistance program under section 129 that reimburses dependent care expenses incurred by employees. The plan allows employees to submit a form in advance of receiving the dependent care, attesting to the amount of dependent care expenses they will incur in the upcoming year. The plan requires employees to notify the plan sponsor if their dependent care situation changes and they will not incur the amount of qualified dependent care expenses to which they attested for that year. The employee is automatically reimbursed every pay period a pro rata amount of the amount of dependent care assistance expenses to which the employee attested.

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

In **Situation 6,** all claims for payment or reimbursement of the employee's dependent care assistance program are not substantiated because they are claimed in advance without additional verification. Because the plan does not limit reimbursements or payments of claims to dependent care assistance expenses that have been incurred or substantiated, the plan does not satisfy the requirements of section 129 and does not satisfy the cafeteria plan requirements of section 125. Therefore, the reimbursements for dependent care assistance expenses are not excludable from gross income under section 129, and all payments made during the year under the dependent care assistance program are included in the gross income and wages of the employees for FICA and FUTA tax purposes

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IRS Issues Chief Counsel Advice on Substantiation Rules for Cafeteria Plans with FSAs and Dependent Care Assistance Programs

Situations 2-6 Are Also Plan Operational Issues

Further, in **Situation 2, Situation 3, Situation 4, Situation 5**, and **Situation 6,** failure to comply with the substantiation requirements of Prop. Reg. §1.125-6(b) results in the failure to operate in accordance with its written plan or the failure to operate in accordance with section 125 and Prop. Reg. §1.125-1(c)(7)(ii)(G).

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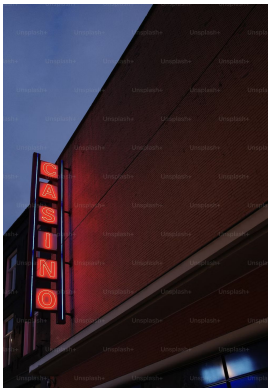
Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation



- *Bright v. Commissioner*, Tax Court Docket No. 10095-22, 5/4/23
  - This decisions is a transcript of an oral decision delivered from the bench
  - Is a cautionary tale for taxpayers
    - Take care when selecting a return preparer
    - Understand the return you are given to sign and where the preparer obtained certain numbers

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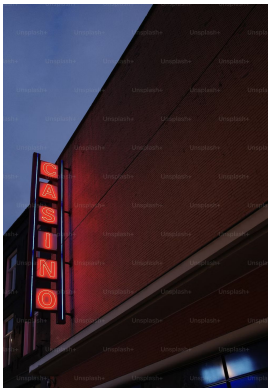
Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation



- *Bright v. Commissioner*, Tax Court Docket No. 10095-22, 5/4/23
  - Issue involves the taxpayers' gambling
    - The IRS decided to accept the taxpayer's gambling income
    - But attempted to disallow all of the gambling expenses

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

Jacob Bright has been gambling for half his life. Mr. Bright is 36 years old. He completed two years of college, where he studied automobile repair, but he performs storm restoration work as his occupation. He began gambling when he was 18, primarily to make money, but also for entertainment. He has gambled more frequently in the last 4 to 5 years. ***He cashes most of his paychecks to gamble and loses substantial amounts of money. His bank account records show that his account frequently had a low or negative balance in 2019. Mr. Bright recognizes and regrets the negative effect that gambling has had on his life.***

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

Mr. Bright principally tries his luck at three casinos. These include Mystic Lake Casino and Treasure Island Resort and Casino in Minnesota, and Diamond Jo Worth Casino in Iowa. He plays different games including slot machines and table games, specifically blackjack, and he bets on sports. He primarily plays slot machines, and his sports betting takes place at Diamond Jo. ***He typically uses a player's card issued by a given casino to place bets from his balance on the card. The casinos track Mr. Bright's gambling activity while using the player's card. He almost always uses his player's card. He has obtained reports from the casinos summarizing his tracked activity for 2019.***

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

According to casino records, Mr. Bright lost money. At Mystic Lake, he had an annual net loss of $22,375. The Mystic Lake activity report calculates the annual net loss as the sum of monthly net wins and losses. The monthly net losses included $1,932 for January, $1,091 for March, $3,886 for April, $160 for June, $78 for July, $16,779 for August, $4,100 for September, and $13,351 for December. The monthly net gains included $2,816 for February and $15,447 for November. The report does not include any data from May or October. At Treasure Island, Mr. Bright had an annual net loss of $16,580. This consisted of a $7,980 net loss from the pit gaming area, and an $8,600 net loss from the slot gaming area. The report calculated these net loss amounts by tracking the annual "dollars in" and "dollars out" per gaming area. For pit gaming, Mr. Bright put in $15,580 and got out $7,600. For slot machines, he put in $42,354 and got out $33,753. At Diamond Jo, he had an annual net loss of $894 from slot machine play; the report does not include amounts won or lost from sports betting in the calculation.

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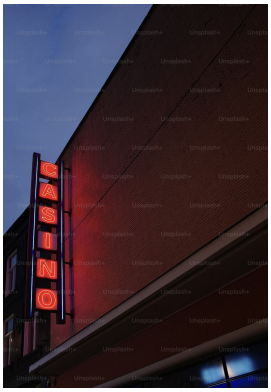
Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation



- *Bright v. Commissioner*, Tax Court Docket No. 10095-22, 5/4/23
  - Mr. Bright did get recommendations for a return preparer - but things didn't quite go as he expected

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

Mr. Bright hired a return preparer who was recommended to him, but he did not get what or whom he expected. Rather than the recommended preparer, the return preparer's daughter actually prepared his return. ***The return preparer reported that Mr. Bright was a professional gambler, although the parties appear to agree that he was not and the evidence does not support him being a professional gambler.*** When the preparer presented Mr. Bright with his completed return, ***he did not review it. He is unaware of how the preparer came up with his reported gambling income.*** As relevant to this Opinion, the return showed $240,895 of gross receipts from "professional gambling" and an equal amount of expenses on Schedule C, Profit or Loss from Business. The expenses reduced the net profit from gambling to zero.

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

The Commissioner determined that the reporting on Mr. Bright's return was incorrect. In a notice of deficiency dated April 22, 2022, the Commissioner determined a tax deficiency of $68,214 and a substantial understatement penalty pursuant to section 6662(a) of $13,643. The Commissioner determined that Mr. Bright was not allowed to report gambling winnings and losses on Schedule C because he was not a professional gambler. ***The Commissioner accepted the reported amount of gambling winnings and moved them on the return but disallowed the gambling losses reported on Schedule C.*** Mr. Bright subsequently filed an amended return on which he reported gambling losses to the extent of his winnings on Schedule A, Itemized Deductions. ***The Commissioner did not allow the adjustments reported on the amended return and based his notice of deficiency on the original return.***

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

At its core, this is a substantiation case. Mr. Bright argues that he should not be bound by the amount of gambling winnings reported on his return. ***Rather, he contends that $110,553, the cumulative reported amount on the Forms W-2G, is the better amount.*** Alternatively, he contends that his gambling income should be zero, because the IRS has no logical basis for using either the amount reported on the returns or the Forms W-2G such that a deficiency based on either figure is a "naked assessment." ***The Commissioner, on the other hand, argues that he reasonably relied on the amount of the gambling winnings reported on the 2019 return.*** The Commissioner further contends that Mr. Bright has failed to meet his burden of proving that the Commissioner's determination is incorrect or that he may deduct losses under section 165(d).

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

Mr. Bright failed to establish that his winnings were less than what he reported on his return. Although he is unaware of how his return preparer calculated the reported amounts, he has failed to demonstrate that the amounts he reported were erroneous. Further, Forms W-2G show that he had gambling winnings from slot machines of at least $110,553, which represents only part of his winnings. Casinos are required to issue Forms W-2G only for slot machine jackpots of $1,200 or more and are not required to keep track of smaller winnings. See Coleman v. Commissioner, T.C. Memo. 2020-146 at *4-5. ***Given the frequency of Mr. Bright's gambling and the fact that he played games other than slot machines, we know that he had winnings beyond what was reported on those forms.*** For example, casino reports show that Mr. Bright gambled during the months for which he was not issued a Form W-2G. I***n sum, the Forms W-2G clearly do not reflect all of Mr. Bright's gambling winnings, and he has failed to negate his own reporting.***

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

Taxpayers bear the burden of proving they are entitled to deductions. Rule 142(a); *INDOPCO, Inc. v. Commissioner,* 503 U.S. 79, 84 (1992). That burden often requires substantiation. *Higbee v. Commissioner*, 116 T.C. 438, 440 (2001). Taxpayers must maintain records sufficient to establish the amount of each deduction. See I.R.C. §6001; *Rogers v. Commissioner*, T.C. Memo. 2014-141, at *17; Treas. Reg. § 1.6001-1(a), (e). ***Where a taxpayer establishes that he paid or incurred a deductible expense but does not establish its precise amount, we may supply an estimate. See Cohan v. Commissioner, 39 F.2d 540 (2d Cir. 1930). However, we must have some basis upon which an estimate can be made. Vanicek v. Commissioner, 85 T.C. 731, 743 (1985).*** We may apply this rule to estimate a gambler's losses for purposes of a deduction pursuant to section 165. See, e.g., *Coleman v. Commissioner*, T.C. Memo. 2020-146 at *13. In past cases, taxpayers have substantiated gambling losses with evidence such as casino ATM receipts, checks made payable to casinos, bank statements, and evidence about the taxpayer's modest lifestyle and overall financial condition, among other things. Id. at *14.

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

Casino documents, coupled with Mr. Bright's testimony, make clear the he suffered substantial gambling losses. He testified that he has lost more than he has gained from gambling, and that gambling has made life financially difficult for him. Indeed, the casino reports confirm his testimony, showing that even with some sizable winnings, he lost more than he won for those times when his wins and losses were captured. ***Although the casino records do not capture the full picture, they provide a sufficient basis upon which we can make an estimate. Because each casino's records report Mr. Bright's activity in a different way, our estimation method differs per casino.***

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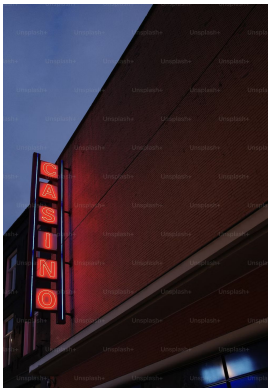

- *Bright v. Commissioner*, Tax Court Docket No. 10095-22, 5/4/23
  - IRS's flat out denial of any deduction not accepted by the court - it is a *Cohan* case
  - But note that even though each casino's report shows a net loss, the taxpayer won't get to the offset he claims should be on the return

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

For Mystic Lake, we estimate a minimum amount of loss by calculating the difference between Mr. Bright's Form W-2G winnings from Mystic Lake for a given month and his net gain or loss from Mystic Lake's casino report for that month. For example, his Form W-2G winnings at Mystic Lake for January totaled $8,162, but he had an overall net loss of $1,192, he must have lost $9,354. For him to have won $8,162 and yet netted a loss of $1,192, he must have lost $9,354. ***Thus, we conclude that Mr. Bright lost at least that much at Mystic Lake in January. For months in which he had a net loss but no Form W-2G winnings, our loss estimate is limited to the net loss.*** We estimate the annual loss from Mystic Lake by adding the monthly amounts.

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

To reach this conclusion, we accept Mr. Bright's testimony that he rarely gambled when not using his casino card. Again, Mr. Bright's testimony in this regard is supported by the documents from the casinos. For example, in November 2019, Mr. Bright won $25,317 in slots at Mystic Lake. On the player's estimated win/loss statement from Mystic Lake, November 2019 is one of only two months where Mr. Bright did not net a loss. When comparing the Forms W-2G and the Mystic Lake statement, it is clear that the W-2G winnings reported by that casino are likewise reflected in the statement. From that, we infer that his W-2G earnings were likewise included in the statements from the other casinos.

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

For Treasure Island, we estimate Mr. Bright's loss differently depending on the type of play. ***Unlike Mystic Lake, the Treasure Island activity report shows only annual net gain or loss, but it tracks the source of the gain or loss as being from either slot machines or the pit area. It also tells us the dollars Mr. Bright put into each area.*** Because he had net losses from both, we know that his actual loss was at least the amount of money he put in. However, for slot machines, we also know that his loss includes the amount of his annual Form W-2G winnings from Treasure Island because for him to have netted a loss, he must have also lost what he won. For the pit, Mr. Bright put in $15,580. For slots, he put in $42,354, and he had annual Form W-2G winnings of $10,526. We estimate his annual losses from Treasure Island by combining these amounts.

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

For Diamond Jo, we estimate Mr. Bright's loss similarly to Mystic Lake. Diamond Jo's records report an annual net loss from slot machines. ***Thus, we estimate loss by calculating the difference between Mr. Bright's annual Form W-2G slot machine winnings from Diamond Jo, or $3,568, and his annual net loss of $894.***

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Taxpayer Denied Portion of Gambling Losses and Stuck with Reported Income Due to Lack of Documentation

Mr. Bright failed to establish that his gambling winnings were less than what he reported on his own return. And he failed to establish gambling losses in the amount he reported on his return. Casino records, however, establish that he had gambling losses of no less than $191,756. ***While we recognize that his gambling losses may have been greater, the record only supports this amount.*** Decision will be entered under Rule 155.

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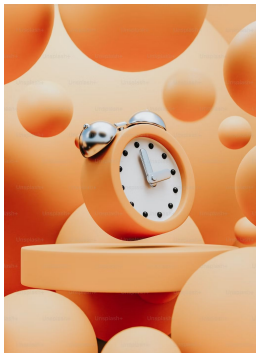
Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides



- *Nutt v. Commissioner*, 160 TC No. 10, 5/3/23
  - Case deals with an issue that has arisen as more things are filed electronically-what is the *last second* for timely filing?
  - Case will illustrate that different rules apply for
    - Filing documents via IRS eFile and
    - Filing petitions with the US Tax Court

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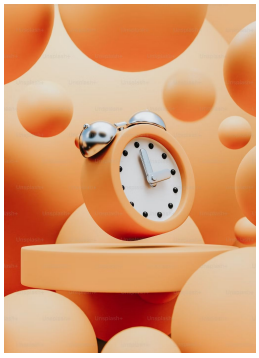

- *Nutt v. Commissioner*, 160 TC No. 10, 5/3/23
  - Returns electronically filed with the IRS
    - Treasury Reg. §301.7502-1(d)(1) provides that the "electronic postmark" applies
    - Treasury Reg. §301.7502-1(d)(3)(ii) looks to the time zone of the *taxpayer* to determine when the clock strikes midnight on timely filing

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

(d) Electronically filed documents.

(1) In general. A document filed electronically with an electronic return transmitter (as defined in paragraph (d)(3)(i) of this section and authorized pursuant to paragraph (d)(2) of this section) in the manner and time prescribed by the Commissioner **is deemed to be filed on the date of the electronic postmark (as defined in paragraph (d)(3)(ii) of this section) given by the authorized electronic return transmitter**. Thus, if the electronic postmark is timely, the document is considered filed timely **although it is received by the agency, officer, or office after the last date, or the last day of the period, prescribed for filing such document.**

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

(d) Electronically filed documents.

(2) ...

(ii) Electronic postmark. For purposes of this paragraph (d), the term electronic postmark means a record of the date and time (in a particular time zone) that an authorized electronic return transmitter receives the transmission of a taxpayer's electronically filed document on its host system. **However, if the taxpayer and the electronic return transmitter are located in different time zones, it is the taxpayer's time zone that controls the timeliness of the electronically filed document.**

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

Example for Tax Returns (Not for Tax Court Petitions)

Taxpayer X resides in Texas, which is in the Central Time Zone. Transmitter Y is an authorized electronic return transmitter, located in Colorado, which is in the Mountain Time Zone. Taxpayer X emails their tax documents to tax professional Z (an ERO) who is also located in Texas on April 18, 2023, at 7:00 PM Central Time. Tax professional Z receives the email and electronically sends the tax return to Transmitter Y at 8:00 PM Central Time. Transmitter Y then transmits the tax return to the IRS at 10:00 PM Mountain Time on April 18, 2023. The IRS acknowledges receipt of the tax return on April 19, 2023, at 1:00 AM Eastern Time.

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

Example for Tax Returns (Not for Tax Court Petitions)

Under the regulations, the tax return is deemed filed on the date of the electronic postmark given by the authorized electronic return transmitter. In this example, the electronic postmark is April 18, 2023, at 10:00 PM Mountain Time, which is timely as that is 11:00 pm Central Time when recast to the taxpayer's time zone. Since the electronic postmark is timely, the tax return is considered filed timely, even though it was received by the IRS after the last day prescribed for filing.

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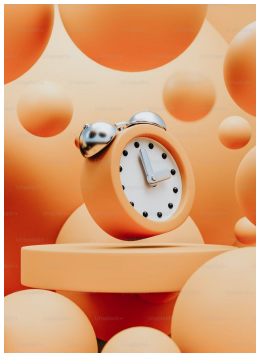

- *Nutt v. Commissioner*, 160 TC No. 10, 5/3/23
  - Tax Court does not use IRS eFile and IRS has issued no regulations under §7502 to cover electronic Tax Court petitions
  - Since the petition was not mailed, the timely mailing rule under §7502 therefore does not apply in this case.

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

The timely mailing rule does not apply to an electronically filed petition. Under section 7502(a), a document that is mailed before it is due but received after it is due is deemed to have been received when mailed. But that rule applies only to documents that are delivered by U.S. mail or a designated delivery service. I.R.C. §7502(a)(1), (f). **Because an electronically filed petition is not delivered by U.S. mail or a designated delivery service, the exception of section 7502 does not apply.** Where section 7502 does not apply, **"we must look to the date the 'petition' was actually received and filed by the Court to determine whether it was timely filed."** *Cassell v. Commissioner*, 72 T.C. 313, 319 (1979).

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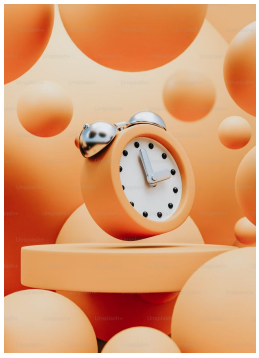

- *Nutt v. Commissioner*, 160 TC No. 10, 5/3/23
  - Taxpayers resided in Alabama (Central Time Zone)
  - Final date to file a petition with the Tax Court was July 18, 2022
  - Petition filed electronically via Tax Court's electronic case management system (DAWSON) at **11:05 pm CDT on July 18, 2022**
  - Cover sheet shows Tax Court received the petition at **12:05 am EDT on July 18, 2022**

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

A petition is ordinarily "filed" when it is received by the Tax Court in Washington, D.C. See, e.g., *Leventis v. Commissioner*, 49 T.C. 353, 354 (1968) ("[A] petition, in order to be timely filed, must be received by the Court in Washington, D.C., on or before the 90th day."). Although the Court may sit at any place within the United States, its principal office, its mailing address, and its Clerk's office are in the District of Columbia. I.R.C. §7445; Rule 10. As a result, documents such as petitions are often mailed to the Court for filing. ***And unless the timely mailing rule of section 7502 applies, a document is not considered to be filed until it is received.*** See *Guralnik*, 146 T.C. at 240, 242; E*ichelburg v. Commissioner*, T.C. Memo. 2013-269, at *6-8.

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

Rule 22(a) provides that a paper "must be filed with the Clerk in Washington, D.C., during business hours" unless it is electronically filed. As for electronic filings, Rule 22(d) provides that a "paper will be considered timely filed if it is electronically filed at or before 11:59 p.m., eastern time, on the last day of the applicable period for filing."

The Court's website also instructs petitioners how to electronically file a petition through DAWSON in accordance with this Rule. See United States Tax Court, How to eFile a Petition, https://ustaxcourt.gov/efile_a_petition.html (last visited Mar. 30, 2023). The first instruction states:

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

Check the Deadline for Filing

You may have received a notice in the mail from the Internal Revenue Service (IRS). ***The Court must receive your electronically filed Petition no later than 11:59 pm Eastern Time on the last date to file.*** Petitions received after this date may be dismissed for lack of jurisdiction.

Id.

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Deadline to File Tax Petition is Midnight Eastern Time on Last Day to File Regardless of Where the Taxpayer Resides

The Nutts' Petition was untimely because it was filed in Washington, D.C., after the last day for filing prescribed by section 6213(a). The period within which to file a petition cannot be extended by the Court, and we must dismiss a case for lack of jurisdiction if the petition is not filed within the prescribed time. Rule 25(b)(2)(C); *Hallmark Rsch. Collective v. Commissioner*, No. 21284-21, 159 T.C., slip op. at 42 (Nov. 29, 2022); *Blum v. Commissioner*, 86 T.C. 1128, 1131 (1986). ***If we were to hold that the Nutts' electronically filed Petition was timely because it was still the last day to file in Alabama, even though the last day had ended in the District of Columbia, we would impermissibly be extending the number of days available for filing.*** See *Justice*, 682 F.3d at 664; *McCleskey*, 2020 WL 9601835, at *1. Accordingly, we must dismiss this case for lack of jurisdiction.

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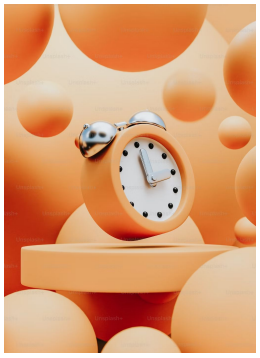

- *Nutt v. Commissioner*, 160 TC No. 10, 5/3/23
  - Practical rule: Don't file anything so late that these rules become important
    - *Boyle* makes it clear that being even slightly late on filing the return/extension means its late (*United States v. Boyle*, 469 U.S. 241 (1985))
    - Many things can go wrong if you keep going late on a due date (ISP goes down, power goes out, computer or other hardware failure)
    - Best practice - get electronic filings out early that could mail it in if the electronic process becomes unavailable

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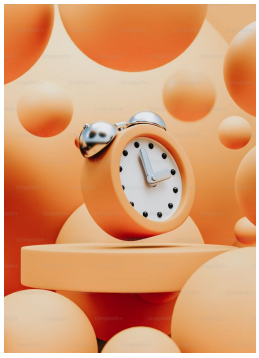

- *Nutt v. Commissioner*, 160 TC No. 10, 5/3/23
  - If you are going to ignore the first rule (and I know many of you are going to do just that)
    - Be sure you double check the law and the specific issue of which time zone is going to determine midnight in your case
    - Be sure you understand how your tax software provider is going to handle ePostmark timestamps - and remember when you start transmission to your provider isn't the actual timestamp

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