

TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



The IRS Could Collect Over a Billion Dollars in Taxes From Unreported Wagering Income

September 30, 2024

Report Number: 2024-300-064

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

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Why TIGTA Did This Audit

In May 2018, the U.S. Supreme Court struck down the 1992 Professional and Amateur Sports Protection Act, which had restricted the growth of sports betting by preventing States from authorizing it. The Supreme Court's decision gave each State the ability to determine and establish its own regulated sports betting law(s).

This audit was initiated to evaluate the IRS's efforts to promote income tax compliance for individuals who have reported winnings from gambling activities and compliance by gaming operators responsible for payment of associated excise taxes on wagering. The gambling industry has reached unprecedented levels of popularity across the United States with total gross gambling revenue reaching an all-time high of \$60.5 billion in Calendar Year 2022. Internal Revenue Code § 61 states that all income, including winnings derived from gambling activities, is includible in a U.S. resident's gross income.

Impact on Tax Administration

The gross Tax Gap is the estimated difference between the amount of tax that taxpayers should pay, and the amount paid voluntarily and on time. The annual gross Tax Gap is estimated to be \$688 billion for Tax Year 2021, and approximately \$77 billion (11 percent) is due to nonfilers. Nonfilers are taxpayers who do not timely file a required tax return and timely pay the tax due for such delinquent returns.

What TIGTA Found

The IRS has not enforced income tax return filing requirements for recipients of millions of Forms W-2G, *Certain Gambling Winnings*, reporting billions of dollars in gambling winnings. TIGTA reviewed all Forms W-2G issued to individual taxpayers during Tax Years (TY) 2018 through 2020 (as of March 2023) and found 148,908 individuals who

were issued Forms W-2G with a total amount of more than \$15,000 per individual in gambling winnings and did not file a tax return. These nonfilers were associated with approximately \$13.2 billion in total gambling winnings. Further TIGTA analysis determined that 139,045 of these nonfilers were included in the IRS's nonfiler case creation process inventory. In response to our audit work, the IRS analyzed 17,436 TY 2018 high-income nonfilers with total positive income greater than or equal to \$100,000 and calculated that it could potentially increase tax revenue by approximately \$1.4 billion through addressing the 139,045 individual nonfilers with gambling winnings.

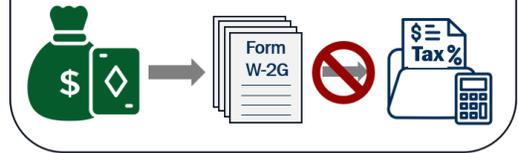
In addition, hundreds of Forms W-2G do not include a Taxpayer Identification Number (TIN) required to trace the income to the recipient. Finally, the IRS has few processes in place to identify potential excise tax noncompliance by entities accepting wagers, particularly in emerging areas such as online sports wagering.

What TIGTA Recommended

TIGTA recommended that the Commissioner, Small Business/Self-Employed Division: 1) begin appropriate enforcement actions for nonfilers with gambling winnings from TYs 2018 through 2020; 2) review nonfilers with gambling winnings for TYs 2018 through 2020 who were not identified by the IRS's nonfiler system; 3) analyze Forms W-2G with missing TINs to determine what forms of wagering and/or gambling institutions may be noncompliant; 4) expand the wager codes to specifically include sports betting; and 5) conduct an environment scan of the current and potential future conditions of the sports betting and online gambling industries.

The IRS agreed with three recommendations and plans to begin enforcement action, if appropriate, and scan the conditions of the sports betting and online gambling industries. However, the IRS disagreed with analyzing Forms W-2G with missing TINs to determine what forms of wagering and/or gambling institutions may be noncompliant. Lastly, the IRS partially agreed to explore the potential productivity and feasibility of expanding the wager codes.

TIGTA identified almost 150K recipients of Forms W-2G reporting \$13B in gambling winnings over a three-year period who did not file a tax return.





TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

U.S. DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20024

September 30, 2024

MEMORANDUM FOR: COMMISSIONER OF INTERNAL REVENUE

Danny Verneuille

FROM: Danny R. Verneuille
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The IRS Could Collect Over a Billion Dollars in Taxes From Unreported Wagering Income (Audit No.: 202230021)

This report presents the results of our review to evaluate the Internal Revenue Service's efforts to promote income tax compliance for individuals who have reported winnings from gambling activities and compliance by gaming operators responsible for payment of associated excise taxes on wagering. This review was part of our Fiscal Year 2022 Annual Audit Plan and addresses the major management and performance challenges of *Improving Tax Reporting and Payment Compliance to Reduce the Tax Gap* and *Addressing Emerging Threats to Tax Administration*.

Management's complete response to the draft report is included as Appendix III. If you have any questions, please contact me or Frank O'Connor, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations).

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Background

Internal Revenue Code (I.R.C.) § 61 states that all income, including winnings derived from gambling activities, is includible in a U.S. resident's gross income.¹ For most individuals, gains from gambling transactions are fully taxable and must be reported by individual taxpayers as income.² Gambling losses may be deductible for recreational gamblers who itemize deductions and for professional gamblers up to the amount of the winnings.

The gambling industry has reached unprecedented levels of popularity across the United States. According to the American Gaming Association (AGA), total gross gambling revenue (GGR) reached an all-time high of \$60.5 billion in Calendar Year (CY) 2022. This total was over \$7 billion more than the previous annual record of \$53 billion in CY 2021 reported by the AGA. The GGR from sports betting and online gambling was a significant contributor to the increase, rising approximately 77 percent from \$4.3 billion in CY 2021 to \$7.6 billion in CY 2022.³

In May 2018, the U.S. Supreme Court struck down the 1992 Professional and Amateur Sports Protection Act, which had restricted the growth of sports betting by preventing States from authorizing it, effectively banning commercial sports betting in most States.⁴ The Supreme Court's decision gave each State the ability to determine and establish its own regulated sports betting law(s).⁵ According to the AGA, as of May 2023, sports betting was legal in 35 States and Washington, D.C. As a result of this change, the gambling industry in the United States has consistently grown over the past five years, except for CY 2020 due to unprecedented shutdowns prompted by the Coronavirus Disease 2019 Pandemic. Figure 1 shows the growth of gambling industry revenue.

¹ See Appendix IV for a glossary of terms.

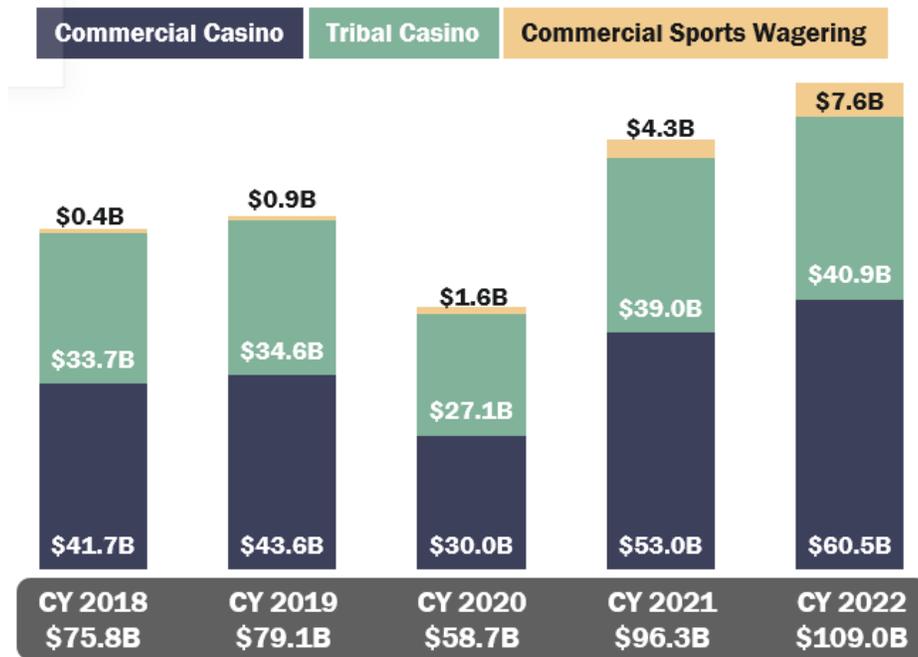
² The tax treatment of individuals with gambling income and losses varies significantly depending on whether the gambler is a professional or engaged in gambling as a recreational activity. Prior to the passage of the Tax Cuts and Jobs Act of 2017, a professional gambler with business expenses in excess of net gambling winnings could report a business loss (and thus a net operating loss). The Tax Cuts and Jobs Act of 2017 reversed this treatment for tax years beginning after 2017 and before 2026.

³ This does not include sports betting in tribal casinos or any illegal sports betting.

⁴ Pub. L. 102-559, and *Murphy v. National Collegiate Athletic Association*, 138 S. Ct. 1461 (2018).

⁵ *Murphy v. National Collegiate Athletic Association*, 138 S. Ct. 1461 (2018).

Figure 1: The GGR for CYs 2018 to 2022



Source: The AGA Commercial Casino Industry annual "State of the States" analysis and the National Indian Gaming Commission.

The Internal Revenue Service (IRS) projected the annual gross Tax Gap to be \$688 billion for Tax Year (TY) 2021, with approximately \$77 billion (11 percent) due to nonfiling. It is a crime for any taxpayer to willfully fail to file a tax return that is due, which is punishable by a fine of not more than \$25,000 (\$100,000 in the case of a corporation) or imprisonment of not more than one year, or both.⁶ In previous reports, the Treasury Inspector General for Tax Administration (TIGTA) expressed concerns about the lack of priority the IRS places on high-income nonfilers. For example, in a Fiscal Year (FY) 2020 report, TIGTA found there were over 800,000 high-income nonfilers in TYs 2014 through 2016 that the IRS did not pursue.⁷ Similarly, in a FY 2021 report, TIGTA found almost 104,000 individual nonfilers with approximately \$3 billion in income reported on Form 1099-K, *Payment Card and Third Party Transactions*, that were not pursued by the IRS.⁸

In addition to its annual appropriation, the IRS also received approximately \$79.4 billion in supplemental funding when the President signed the Inflation Reduction Act of 2022 (IRA) into law in August 2022.⁹ However, in June 2023, the enactment of the Fiscal Responsibility Act of 2023 rescinded approximately \$1.4 billion of IRA funding provided to the IRS, and the Further

⁶ I.R.C. § 7203. In this context, "willfully" means intentionally and in violation of known legal duty. See *United States v. Burton*, 737 F.2d 439, 441 (5th Cir. 1984) (citing *United States v. Pomponio*, 97 S. Ct. 22, 23 (1976)).

⁷ TIGTA, Report No. 2020-30-015, *High-Income Nonfilers Owing Billions of Dollars Are Not Being Worked by the Internal Revenue Service* (May 2020).

⁸ TIGTA, Report No. 2021-30-002, *Billions in Potential Taxes Went Unaddressed From Unfiled Returns and Underreported Income by Taxpayers That Received Form 1099-K Income* (Dec. 2020).

⁹ Pub. L. No. 117-169, 136 Stat. 1818.

Consolidated Appropriations Act 2024 rescinded an additional \$20.2 billion.¹⁰ Therefore, current IRA funding is approximately \$57.8 billion.

After passage of the IRA, the IRS developed the *IRS Inflation Reduction Act Strategic Operating Plan, FYs 2023 – 2031*, which includes an objective focusing on the Tax Gap (Objective 3: Focus expanded enforcement on taxpayers with complex tax filings and high-dollar noncompliance to address the Tax Gap).¹¹ In addition, two initiatives within the IRS's *Inflation Reduction Act Strategic Operating Plan* specifically relate to nonfilers:

- Initiative 2.6, *Expand engagement with non-filers*, states that the IRS will provide early, tailored outreach to taxpayers who do not file on time.
- Initiative 3.4, *Expand enforcement for high-income and high-wealth individuals*, states that the IRS will increase enforcement activities to help ensure tax compliance of high-income and high-wealth individuals.

The IRS can take various enforcement actions on nonfiler cases, depending on the particular facts of the case. The Small Business/Self-Employed (SB/SE) Division's Collection function has overall responsibility for the nonfiler program. The IRS identifies a potential nonfiler systemically through the Individual Master File Case Creation Nonfiler Identification Process (IMF CCNIP). Typically, nonfiler enforcement starts with the Return Delinquency program where at least one notice is sent to the taxpayer to solicit the unfiled tax return. If the taxpayer does not resolve their return delinquency in the notice process, they may progress to a Taxpayer Delinquency Investigation (TDI) for additional enforcement. The TDI may be assigned to the Automated Collection System, a system that generates letters to taxpayers who can contact call centers where IRS Collection representatives try to resolve the issue. Collection may also assign the TDI to a revenue officer, who may directly contact the taxpayer to solicit the delinquent tax return.

The TDI may also be assigned to the Automated Substitute for Return program, which determines and assesses the tax liability based on Information Return Program information submitted by payers, combined with other internally available information, but does not allow for deductions or other income about which the IRS is unaware.¹² Similarly, the TDI may be referred to the Examination function where a Substitute for Return may be prepared based on available information. However, given the high volume of compliance cases, the TDI may remain in the Collection queue, a repository for unassigned collection work. The most serious cases, particularly high-income repeat offenders, can be referred to Criminal Investigation.

Reporting requirements of gambling activity

Gambling winnings and any Federal tax withheld from gambling activities should generally be reported to the IRS by the gambling entity (hereafter referred to as a payer) on Form W-2G, *Certain Gambling Winnings*, (see Figure 2). The payer should file a Form W-2G with the IRS and issue a copy of the Form W-2G to the winner (hereafter referred to as a payee). The payee uses this information to help determine their tax liability for the tax year. The requirements for reporting gambling winnings and withholding Federal tax depend on the type of gambling

¹⁰ Pub. L. No. 118-5, § 251 and Pub. L. No. 118-47.

¹¹ IRS Publication 3744 (Rev. 4-2023).

¹² Internal Revenue Manual 5.19.18.5.8.2(3) and (4) (July 8, 2013).

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activity, the amount of the gambling winnings, and the ratio of the winnings to the wager.¹³ Payers must issue a Form W-2G if one of the following criteria applies:

- The winnings from a bingo game or slot machine (not reduced by the wager) are \$1,200 or more.
- The winnings from a keno game (reduced by the wager) are \$1,500 or more.
- The winnings from a poker tournament (reduced by the wager or buy-in) are more than \$5,000.
- The winnings (except winnings from bingo, slot machines, keno, and poker tournaments) reduced, at the option of the payer, by the wager (including horse racing) are \$600 or more and at least 300 times the amount of the wager.
- The winnings are subject to Federal income tax withholding, either regular gambling withholding or backup withholding (see Figure 3).

Pursuant to I.R.C. § 3402(q), Federal tax is generally withheld on proceeds from a wager through regular withholding at 24 percent and is reported in Box 4, Federal income tax withheld, on the Form W-2G. According to I.R.C. § 3402(q)(5), regular withholding is not applicable to winnings from bingo, keno, or slot machines. Figure 2 provides an example of Form W-2G.

Figure 2: Form W-2G

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0238	
PAYER'S name, street address, city or town, province or state, country, and ZIP or foreign postal code		1 Reportable winnings	2 Date won
		\$	
PAYER'S federal identification number		3 Type of wager	4 Federal income tax withheld
			\$
PAYER'S telephone number		5 Transaction	6 Race
WINNER'S name		7 Winnings from identical wagers	8 Cashier
		\$	
Street address (including apt. no.)		9 Winner's taxpayer identification no.	10 Window
City or town, province or state, country, and ZIP or foreign postal code		11 First identification	12 Second identification
		13 State/Payer's state identification no.	14 State winnings
			\$
		15 State income tax withheld	16 Local winnings
		\$	\$
		17 Local income tax withheld	18 Name of locality
		\$	
Under penalties of perjury, I declare that, to the best of my knowledge and belief, the name, address, and taxpayer identification number that I have furnished correctly identify me as the recipient of this payment and any payments from identical wagers, and that no other person is entitled to any part of these payments.		This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.	
Signature ►		Date ►	
Form W-2G (Rev. 1-2021)		www.irs.gov/FormW2G	
		Department of the Treasury - Internal Revenue Service	

Source: IRS.gov.

¹³ According to IRS Publication 3908, *Gaming Tax Law and Bank Secrecy Act Issues for Indian Tribal Governments* (Rev. 9-2019), the gross amount of the wager upon which tax is imposed is the amount risked by a bettor, including any charge or fee incident to the placing of the wager.

Figure 3 shows that regular withholding from gambling winnings is applicable if the winnings minus the wager are more than \$5,000 and come from sweepstakes, wagering pools, lotteries, or other wagering transactions, if the winnings are at least 300 times the amount wagered.

Figure 3: Summary of Withholding Requirements for Form W-2G

Summary of Withholding Requirements		
Type of Gaming	Regular Withholding at 24% if Winnings Are:	Backup Withholding at 24% if Winner Does Not Provide TIN and Winnings Are:
Bingo	N/A	≥ \$1,200
Slot machines	N/A	≥ \$1,200
Keno	N/A	≥ \$1,500
Sweepstakes, wagering pools, lotteries and raffles	> \$5000	\$600 to \$5,000
Wagering transactions when winnings are at least 300 times the amount wagered	> \$5,000	\$600 to \$5,000
Poker tournaments	N/A if winnings are reported on Form W-2G	> \$5,000

Source: IRS Publication 3079, *Tax-Exempt Organizations and Gaming (Rev. 10-2018)*.

Backup withholding of 24 percent is also required if the payee does not furnish a correct Taxpayer Identification Number (TIN), regular withholding was not 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, \$1,500 from keno, or more than \$5,000 from a poker tournament).

In May 2021, TIGTA reported that noncompliance with backup withholding requirements continued to result in payers avoiding payment of billions of dollars in withholding each year.¹⁴ In the review, TIGTA identified 182,075 payers in TY 2018 that submitted 440,404 information returns for which the payee TIN was either missing or incorrect, yet the payers did not collect backup withholding of \$13.3 billion on \$55.6 billion in reported income.¹⁵ TIGTA did not make a formal recommendation about the lack of backup withholding because the IRS had committed to develop a cross-functional working group to analyze backup withholding policies and procedures and make recommendations in response to a previous TIGTA report in July 2017.¹⁶ According to IRS officials, the IRS has taken steps to address TIGTA’s recommendations. Specifically, IRS officials stated that they developed the Cincinnati Campus Backup Withholding Program Unit to review information returns for compliance, updated training materials to

¹⁴ TIGTA, Report No. 2021-40-030, *Backup Withholding Noncompliance and Underreported Employment Taxes Continue to Contribute Billions of Dollars to the Tax Gap* (May 2021).

¹⁵ This review included all related information returns including Form W-2G.

¹⁶ TIGTA, Report No. 2016-40-078, *Due to the Lack of Enforcement, Taxpayers Are Avoiding Billions of Dollars in Backup Withholding* (Sept. 2016).

include backup withholding sections, and were in the process of developing a computerized application to assist examiners in evaluating information returns.

When filing Form W-2G, the payer is also required to report the type of gambling activity in Box 3 of the form. If the payer files a paper Form W-2G, the payer should provide a description of the wager, such as Daily Double, Big 50, bingo, or poker tournament in Box 3. If the payer files Form W-2G electronically, they are required to enter one of the wager codes shown in Figure 4 in Box 3, rather than entering a description of the wager. Figure 4 provides the wager codes and definitions used when electronically filing Form W-2G.

Figure 4: Wager Codes and Definitions

Category	Code
Horse race track (or off-track betting of a horse track nature)	1
Dog race track (or off-track betting of a dog track nature)	2
Jai-alai	3
State-conducted lottery	4
Keno	5
Bingo	6
Slot machines	7
Poker winnings	8
Any other type of gambling winnings	9

Source: Publication 1220, Specifications for Electronic Filing of Forms 1097, 1098, 1099, 3921, 3922, 5498, and W-2G (Rev. 9-2023).

According to IRS Publication 1220, any payer that issues 250 or more information returns, such as a Form W-2G, must file such returns electronically.¹⁷ The portal through which a payer can file information returns electronically is called the Filing Information Returns Electronically system.

Payers may have the payee complete a Form W-9, *Request for Taxpayer Identification Number and Certification*, to obtain a person's correct TIN.¹⁸ A payer's failure to obtain and report a correct TIN can result in a penalty.¹⁹ Additionally, a payer's failure to subject a payee to backup

¹⁷ IRS Publication 1220 (Rev. 9-2023).

¹⁸ Form W-9 requires the payee to certify, under penalties of perjury, that the number shown on the form is the correct TIN and the individual is a U.S. person (including a U.S. resident alien) when the customer signs and dates the form.

¹⁹ I.R.C. § 6109(a)(1) imposes the obligation to supply TINs along with information returns, and I.R.C. § 6721(a)(1) imposes a penalty of \$250 for each incorrect return, which can be reduced to \$50 when the return is corrected. I.R.C. § 6721(f) provides that penalty amounts be annually adjusted for inflation for calendar years beginning after 2014. The penalty for TYs 2018 through 2022 ranges between \$530 to \$570 per return.

withholding as required under the law can subject the payer to liability of the amount that should have been subject to withholding.²⁰

Excise tax filing and payment requirements on gambling activity

Excise taxes are taxes imposed on certain goods, services, and activities. For example, excise taxes are imposed for accepting certain types of wagers and for being in the business of accepting wagers for oneself or on behalf of someone else.²¹ Sports betting and certain online gambling, such as sports wagering and daily fantasy sports, are subject to excise tax. Wagers exempt from excise tax include the following:

- Pari-mutuel wagering licensed under any State law.
- Wagers placed in a coin-operated device.
- Any wager placed in a sweepstakes, wagering pool, or lottery which is conducted by a State agency acting under authority of State law.²²

All payers accepting wagers, other than those listed previously, are liable for excise tax on those wagers and must file a Form 730, *Monthly Tax Return for Wagers (Section 4401 of the Internal Revenue Code)*. Form 730 is due each month by the last day of the month following the month for which the payer is reporting taxable wagers. Form 730 must be filed monthly whether or not there are taxable wagers to report. If the payer stops accepting wagers, they should check the “final return” box on their last Form 730 filed. Figure 5 provides an example of Form 730.

²⁰ I.R.C. § 3403.

²¹ I.R.C. §§ 4401-4424 provide for the imposition of excise taxes, which are independent of income taxes, on certain types of wagers.

²² I.R.C. § 4402. Treasury Regulation § 44.4421-1(b)(2)(i) states Section 4421 specifically excludes from the term “lottery” any game of a type in which usually (a) the wagers are placed, (b) the winners are determined, and (c) the distribution of prizes or other property is made, in the presence of all persons placing wagers in such game. Thus, for example, no tax would be payable with respect to wagers made in a bingo or keno game since such a game is usually conducted under circumstances in which the wagers are placed, the winners are determined, and the distribution of prizes is made in the presence of all persons participating in the game. For the same reason, no tax would apply in the case of card games, dice games, or games involving wheels of chance, such as roulette wheels and gambling wheels of a type used at carnivals and public fairs.

Figure 5: Form 730

Form 730 (Rev. December 2017) Department of the Treasury Internal Revenue Service		Monthly Tax Return for Wagers (Section 4401 of the Internal Revenue Code)		OMB No. 1545-0235	
▶ Go to www.irs.gov/Form730 for the latest information.				For IRS Use Only	
Enter your name, address, employer identification number, and month and year of return.	Name		Month and year		T
	Number, street, and room or suite no.		Employer identification number		FF
	City or town, state or province, country, and ZIP or foreign postal code				FD
					FP
				I	
				T	
Check applicable boxes: <input type="checkbox"/> Final return <input type="checkbox"/> Address change					
1	Gross amount of wagers accepted during month (not including laid-off wagers) (see instructions)			1	
2	Gross amount of laid-off wagers accepted during month (see instructions)			2	
3	Add lines 1 and 2			3	
4a	Tax on wagers authorized under the law of the state in which accepted. Enter the amount of these wagers included in line 3; multiply by the amount shown and enter the result . . . \$ _____ × 0.0025 =			4a	
b	Tax on wagers other than wagers described on line 4a. Enter the amount of these wagers included in line 3; multiply by the amount shown and enter the result . . . \$ _____ × 0.02 =			4b	
c	Tax on wagers. Add lines 4a and 4b			4c	
5	Credits. No credit is allowed unless supported by evidence (see instructions)			5	
6	Balance due. Subtract line 5 from line 4c (see instructions)			6	
File this return, your payment, and voucher with the IRS as shown under <i>Where to file</i> in the instructions. Make your check or money order payable to "United States Treasury." Write your name, address, EIN, "Form 730," and the tax period on it.					
Sign Here Keep a copy of this return for your records.	Under penalties of perjury, I declare that I have examined this return, including any accompanying certificates and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.				
	Signature _____		Date _____		
Paid Preparer Use Only	Print/Type preparer's name		Preparer's signature		Date
	Firm's name ▶		Firm's EIN ▶		Check <input type="checkbox"/> if self-employed
	Firm's address ▶		Phone no.		
For Paperwork Reduction Act Notice, see instructions.			Cat. No. 20585U		Form 730 (Rev. 12-2017)

Source: IRS.gov.

The excise tax rate applied to the wager amount depends on whether the wager is considered authorized or unauthorized. "Authorized" wagers (permitted under State law) are taxed at 0.25 percent of the gross amount of the wager while "unauthorized" wagers (illegal under State law) are taxed at 2 percent of the gross amount of the wager.²³ Whether a wager is considered authorized or unauthorized is based on each State's laws regarding the type of wager and the types of entities allowed to accept the wager.

²³ I.R.C. § 4401.

Results of Review

The IRS has not enforced income tax return filing requirements for recipients of millions of Forms W-2G reporting billions of dollars in gambling winnings. In addition, hundreds of Forms W-2G do not include a TIN needed to trace the income to the recipient. Finally, the IRS has few processes in place to identify potential excise tax noncompliance by entities accepting wagers, particularly in emerging areas such as online sports wagering.

Income Tax Filing Requirements for Hundreds of Thousands of Individuals With Reported Gambling Winnings Have Gone Unaddressed

Our review of the approximately 43 million Forms W-2G with approximately \$156 billion issued to individual taxpayers during TYs 2018 through 2020 (as of March 2023) identified approximately 772,000 unique individual taxpayers with total gambling winnings greater than \$15,000.²⁴ Of these individual taxpayers, we found 148,908 (19 percent) who were issued one or more Forms W-2G reporting a total amount of more than \$15,000 per individual but did not file a tax return (hereafter referred to as a nonfiler).²⁵ These nonfilers were associated with approximately 4 million Forms W-2G with \$13.2 billion in total gambling winnings and \$288 million in Federal taxes withheld from the winnings (approximately 2 percent of the total winnings). Of these 148,908 individual nonfilers:

- 103,074 (69 percent) never entered the IRS's compliance inventory stream, *i.e.*, were never issued any delinquency notice, which is the first step to bring taxpayers into compliance. Total gambling winnings for this population were approximately \$7.1 billion.

TIGTA identified almost 150K recipients of Forms W-2G reporting \$13B in gambling winnings over a three-year period who did not file a tax return.



²⁴ Our analysis included Forms W-2G that were issued by payers, such as commercial and tribal casinos and State-run lotteries. The IRS does not have any validation processes in place to verify Form W-2G data during submission. In attempting to validate Form W-2G data, we noted discrepancies throughout the population, including possible duplicate forms and erroneous data that could not be reconciled. Of the 43 million Forms W-2G, we identified approximately 5.3 million (13 percent) forms that were potential duplicate records with gambling winnings of approximately \$12 billion (8 percent of \$156 billion). There may be differences in amounts due to rounding. Because we could not confirm whether the records were duplicates, we did not remove these records from our analysis. However, as discussed in footnote 25, we removed a total of 5,625 TINs because of concerns with the validity of the Form W-2G data.

²⁵ Of these 148,908 nonfilers, there were 125,152 unique nonfilers. There were 23,756 nonfilers that appeared in two or more tax years. We removed a total of 5,625 TINs associated with approximately \$20.3 billion in gambling winnings from our nonfiler population because of concerns with the validity of the Form W-2G data. For example, there were four Forms W-2G in our population that reported over \$1 billion in gambling winnings each and approximately \$18.8 billion in total. According to the IRS's data, these nonfilers appear to have valid TINs. Internal Revenue Manual 3.13.5 defines a valid TIN as when the taxpayer's Social Security Number and the name control match to the names and Social Security Numbers assigned by the Social Security Administration.

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- 17,690 (12 percent) requested a filing extension but had not filed a tax return as of March 2023. Total gambling winnings for this population were approximately \$2.0 billion.
- 28,144 (19 percent) had some sort of IRS compliance action on their account, such as being sent a notice or being placed in the IRS's compliance inventory stream without being worked as of March 2023. Total gambling winnings for this population were approximately \$4.2 billion.

Figure 6 summarizes by tax year the gambling winnings and withheld Federal tax associated with the 148,908 nonfilers outlined previously.

Figure 6: Summary of Nonfilers With Reported Gambling Winnings²⁶

Tax Year	Nonfilers	Gambling Winnings	Federal Tax Withheld	Percent of Tax Withheld
2018	38,972	\$3.1B	\$0.1B	2.2%
2019	45,297	\$4.7B	\$0.1B	1.9%
2020	64,639	\$5.5B	\$0.1B	2.4%
TOTAL	148,908	\$13.2B	\$0.3B	2.2%

Source: TIGTA's analysis of Form W-2G information from the Information Returns Master File database and other tax account information obtained from the Individual Master File on TIGTA's Data Center Warehouse (DCW).

To determine the estimated tax due for each nonfiler, we matched the 148,908 nonfilers to the IMF CCNIP inventory and found that 139,045 were also present in the IMF CCNIP inventory.²⁷ Based on IMF CCNIP data, the estimated net tax due for these nonfilers was approximately \$3.4 billion. Furthermore, 51,792 (37 percent) of the nonfilers were considered high-income nonfilers by the IRS and accounted for approximately \$3.1 billion (90 percent) of the estimated \$3.4 billion net tax due.²⁸ However, the IMF CCNIP estimated net tax due does not consider gambling losses and/or deductions that may reduce the tax due.

In response to our audit work, the IRS analyzed 17,436 TY 2018 high-income nonfilers with total positive income greater than or equal to \$100,000 and calculated the difference between the estimated net tax due on the IMF CCNIP and the actual net tax due. The IRS estimated that the actual net tax due was 60 percent less than the IMF CCNIP estimate of \$3.4 billion resulting in approximately \$1.4 billion in estimated net tax due. See Appendix II for additional details.

²⁶ There may be differences in amounts due to rounding.

²⁷ Of the 148,908 nonfilers, 9,863 did not match to the IMF CCNIP. Collection officials stated that there are several circumstances that may cause a potential nonfiler to not be shown in the IMF CCNIP. However, they do not know with certainty the reason these cases did not match to the IMF CCNIP and may be unaware of these potential nonfilers.

²⁸ At the beginning of FY 2023, the IRS increased the threshold that defines high-income nonfilers as nonfilers with total positive income of \$200,000 or more. However, during TYs 2018 through 2020, the threshold of high-income nonfilers was total positive income of \$100,000 or more. Because our analysis covered TYs 2018 through 2020, we used the threshold of \$100,000. There may be differences in amounts due to rounding.

Figure 7 shows a detailed summary of the nonfilers for TYs 2018 through 2020 that matched to the IMF CCNIP and the estimated tax due.

Figure 7: Summary of Estimated Tax Due for Nonfilers With Reported Gambling Winnings

Tax Year	Nonfilers	Gambling Winnings	Federal Tax Withheld	IMF CCNIP Estimated Net Tax Due	Estimated Net Tax Due (per IRS analysis)
2018	37,650	\$2.9B	\$0.1B	\$0.8B	\$0.3B
2019	43,200	\$4.5B	\$0.1B	\$1.2B	\$0.5B
2020	58,195	\$5.0B	\$0.1B	\$1.4B	\$0.6B
TOTAL	139,045	\$12.4B	\$0.3B	\$3.4B	\$1.4B

Source: TIGTA's analysis of Form W-2G information from the Information Returns Master File database and other tax account information obtained from the Individual Master File on TIGTA's DCW matched against IMF CCNIP nonfiler data from the IRS's Compliance Data Warehouse. In addition, the IRS's analysis of the estimated net tax due on the IMF CCNIP.

We further identified the top 100 Form W-2G nonfilers based on the gross gambling winnings for TYs 2018 through 2020. The top 100 Form W-2G nonfilers had gambling winnings totaling approximately \$1.6 billion representing 12 percent of the total gambling winnings related to the 148,908 nonfilers identified in Figure 6. We matched the top 100 Form W-2G nonfilers for each tax year to the IMF CCNIP and found 289 nonfilers with an estimated tax due of \$423 million.²⁹ We provided these top 100 nonfilers for each tax year to the IRS for review; as of the date of this report, the IRS has not responded.

Approximately 69 percent (103,074) of the 148,908 nonfilers were never issued a delinquency notice, the first step to place nonfilers into the IRS's compliance inventory stream. We believe that the IRS should send notices to these nonfilers to begin the process of bringing them into compliance. Because 51,792 were high-income nonfilers and accounted for 90 percent of the estimated \$3.4 billion net tax due per the IMF CCNIP, we believe that more emphasis should be placed on high-income nonfilers with wagers.

In addition, we identified 1,011 individual taxpayers who were issued Forms W-2G totaling more than \$15,000 and did not have a tax account on file, *i.e.*, no filing history with the IRS. Total gambling winnings for this population were approximately \$49 million. For these 1,011 individual nonfilers, 144 (14 percent) were issued Forms W-2G in at least two of the three tax years we analyzed and accounted for 39 percent (approximately \$19 million) of the total gambling winnings within this population.

²⁹ When we matched the top 100 nonfilers with gambling winnings for TYs 2018 through 2020 (total of 300) to the IMF CCNIP, 11 did not match. As previously mentioned, Collection officials stated that there were several circumstances that may cause a potential nonfiler to not be shown in the IMF CCNIP. However, they do not know with certainty the reason these cases did not match to the IMF CCNIP and may be unaware of these potential nonfilers.

More resources should be allocated to address high-income nonfilers

In past audits, TIGTA has identified serious lapses with the IRS's nonfiler strategy.³⁰ In May 2020, TIGTA reported that more needs to be done to address high-income nonfilers. That review identified 879,415 high-income nonfilers that did not have a satisfied filing requirement, with an estimated tax due of \$45.7 billion.³¹ During that review, TIGTA reported that the nonfiler programs were spread across multiple functions with no one IRS area responsible for the program as a whole, which may make it challenging for the IRS to evaluate the overall effectiveness of the nonfiler programs. TIGTA suggested that one way the IRS may be able to improve efficiency in working high-income nonfiler cases is by creating a team, consisting of Collection and Examination function employees, that specifically focuses on these types of cases, ensuring that the appropriate skill set is applied, and these cases will continue to be worked. At the time of TIGTA's report, the IRS was struggling with declining resources and stated that its resources must be applied in a balanced approach across its different compliance programs. While IRS management agreed that high-income nonfilers constituted a problem, in response, they created and completed a specialized Revenue Officer Compliance Sweeps tool at the beginning of CY 2020, which focused on addressing high-income nonfilers. As of April 2024, the IRS has performed 77 Revenue Officer Compliance Sweeps to work on addressing this problem. However, according to IRS management, this is not an ongoing compliance program to address high-income nonfilers, but just a tool used on a limited, intermittent basis.

In February 2024, the IRS announced a new initiative focused on high-income taxpayers who failed to file Federal income tax returns in more than 125,000 instances between TYs 2017 and 2021. This initiative included the issuance of compliance letters to 25,000 nonfilers with more than \$1 million in income, and over 100,000 nonfilers with income between \$400,000 and \$1 million.

High-income nonfilers pose a significant noncompliance risk and working these cases can generate a large return on investment. As TIGTA has previously reported, enhancements are needed in resource allocations to ensure that the most egregious nonfilers are pursued. The IRS's failure to do so could result in high-income taxpayers concluding that the IRS's efforts in this area are temporary, and the recent initiative is unlikely to have a long-term effect on voluntary tax compliance.

The Commissioner, SB/SE Division, should:

Recommendation 1: Begin appropriate enforcement actions, starting with notice issuance, on the population of nonfilers with gambling winnings for TYs 2018 through 2020, prioritizing high-income nonfilers, including the top 100 nonfiler cases identified by TIGTA.

Management's Response: The IRS agreed with this recommendation and will identify high-income nonfilers for TYs 2018 through 2020 with gambling winnings where no enforcement actions have been taken, including the top 100 nonfiler cases identified by

³⁰ TIGTA, Report No. 2017-30-078, *A Significantly Reduced Automated Substitute for Return Program Negatively Affected Collection and Filing Compliance* (Sept. 2017) and TIGTA, Report No. 2016-30-085, *Improvements to the Nonfiler Program Could Help the Internal Revenue Service More Effectively Address Additional Nonfilers Owing Billions of Dollars in Taxes* (Sept. 2016).

³¹ TIGTA, Report No. 2020-30-015, *High-Income Nonfilers Owing Billions of Dollars Are Not Being Worked by the Internal Revenue Service* p. 12 (May 2020).

TIGTA. If appropriate, the IRS will begin enforcement by issuing the first return delinquency notice.

Recommendation 2: Review the population of nonfilers with gambling winnings for TYs 2018 through 2020 that were not identified by the IMF CCNIP and begin appropriate enforcement actions as warranted.

Management’s Response: The IRS agreed with this recommendation and will review and profile the population of nonfilers with gambling winnings for TYs 2018 through 2020 that were not identified by the IMF CCNIP. This research will determine potential reasons why the nonfiler returns were not identified and assess the current state of these returns to determine if the filing requirement has been satisfied. If the filing requirement has not been satisfied and enforcement is applicable, then manual enforcement of return delinquency will be considered by either Collection or Exam.

Payers Are Issuing Forms W-2G With Missing Taxpayer Identification Numbers and No Backup Withholding

We identified 23,013 Forms W-2G, with total gambling winnings of approximately \$363 million, issued to payees with TINs identified as invalid by the IRS.³² Each of the Forms W-2G had gambling winnings greater than \$5,000 with no Federal tax withheld. We further analyzed the 23,013 Forms W-2G and found 616 with missing TINs, *i.e.*, 000-00-0000. These 616 Forms W-2G were issued by 171 payers and had combined gambling winnings of approximately \$11.3 million. Figure 8 provides the details of the 616 Forms W-2G with missing TINs.

Figure 8: Forms W-2G Issued With Missing TINs and No Backup Withholding

Filing Year	Number of Forms W-2G	Number of Payers	Gross Gambling Winnings	Federal Tax Withheld	Estimated Uncollected Withholding
2018	143	65	\$1.5M	\$0.00	\$0.4M
2019	101	29	\$3.9M	\$0.00	\$0.9M
2020	224	40	\$4.3M	\$0.00	\$1.0M
2021	148	37	\$1.6M	\$0.00	\$0.4M
TOTAL	616	171	\$11.3M	\$0.00	\$2.7M

Source: TIGTA’s analysis of Form W-2G information from the Information Returns Master File database and other tax account information obtained from the Individual Master File.

³² We used the IRS’s validity indicator to identify invalid TINs. Internal Revenue Manual 3.13.5 defines one of the most common reasons for an invalid TIN is when the taxpayer’s Social Security Number and the name control do not match to the names and Social Security Numbers assigned by the Social Security Administration.

The 171 payers associated with the 616 Forms W-2G with missing payee TINs over four years represented 133 unique payers, *i.e.*, some payers were included in more than one year. We provided the list of 133 unique payers to the IRS for review, and as of March 2024, none of them have been selected to be worked.

IRS officials stated that Forms W-2G issued with missing or invalid TINs do not contribute a significant amount to the Tax Gap. Furthermore, they believe that when compared, the total volume of Forms W-2G filed with invalid or missing TINs is an insignificant percentage of the total annual volume of Forms W-2G received. However, without a valid payee TIN for the Form W-2G, there is no way for the IRS to trace the income back to a payee to ensure compliance. While this inventory is small, issued Forms W-2G with missing TINs are easily identifiable and should be used to determine what forms of wagering and/or gambling institutions may be noncompliant.

The 133 unique payers should have immediately initiated backup withholding of approximately \$2.7 million (24 percent) from the gambling winnings. Furthermore, these payers could be subject to approximately \$344,960 in penalties for their failure to file a Form W-2G with a correct TIN. We further analyzed the 133 payers and found that 11 had at least one code indicating that a penalty for failing to file a correct information return applied to their tax account during TYs 2018 through 2021. These penalties totaled approximately \$370,000 and may have included penalties applied because of other information returns.³³ These 11 payers were associated with 145 of the 616 Forms W-2G with missing payee TINs. For the remaining 122 payers that issued 471 Forms W-2G with missing payee TINs with gambling winnings of approximately \$7.2 million, the IRS should pursue backup withholding of at least \$1.7 million (24 percent) and penalties of at least \$250,000.

Findings from earlier Tax Gap analyses show that compliance is higher when income is subject to information reporting and even higher when also subject to withholding. According to IRS Publication 1281, *Backup Withholding for Missing and Incorrect Names/TIN(s)*, payers are instructed to “begin backup withholding immediately on any reportable payments” when the payee refuses or neglects to provide a correct TIN.³⁴ Failure to file correct information returns, *i.e.*, with a missing/incorrect TIN, or other missing or incorrect information, may result in a penalty for each information return.³⁵ In addition, payers are liable for the taxes on the income subject to backup withholding when these amounts are not withheld by the payers.³⁶

Recommendation 3: The Commissioner, SB/SE Division, should analyze Forms W-2G with missing TINs to determine what forms of wagering and/or gambling institutions may be noncompliant. If the cases identified are related to another IRS division, share the results with that division. The results of this analysis should be shared with Exam Case Selection and influence future taxpayer outreach.

³³ These penalties may have included other information returns and not exclusively the Forms W-2G identified in our analysis.

³⁴ IRS Publication 1281 (Rev. 12-2023). According to this publication, a TIN is considered missing if it is not provided or if it is obviously incorrect.

³⁵ The maximum penalty for intentional disregard of the information return filing requirement under I.R.C. § 6721 ranges from \$530 to \$560 per return for the tax years covered by this review.

³⁶ I.R.C. § 3406.

Management’s Response: The IRS disagreed with this recommendation. TIGTA’s analysis identified a very insignificant percentage, .0010 percent of Forms W-2G with missing TINs. The IRS has processes in place to identify and address compliance with information reporting and considers TIGTA’s finding of an insignificant error rate to be a positive reflection of IRS efforts.

Office of Audit Comment: According to Publication 1281, payers should “begin backup withholding immediately on any reportable payments” when the payee refuses or neglects to provide a correct TIN. While this population may not be large in absolute terms, we believe that the amount of backup withholding that should have been withheld is significant and that the IRS should analyze payers that issue Forms W-2G with missing TINs. Furthermore, although IRS management stated that processes are in place to identify and address compliance with information reporting, none of these 616 Forms W-2G were selected for review.

The IRS Has Limited Processes to Identify Nonfiling or Underreporting of Excise Tax for Gambling Activities

Sports betting and certain online gambling wagers such as sports wagering and daily fantasy sports, both authorized and unauthorized, are subject to excise tax. The IRS received 104,569 Forms 730 reporting excise taxes on wagers during Processing Years 2018 through 2022.³⁷ IRS officials explained that efforts to identify nonfiling or underreporting of excise tax are conducted solely through excise tax examinations, which are primarily initiated through referrals from other IRS functions.³⁸ According to IRS officials, the SB/SE Division’s Excise Tax program has four initiatives in place to determine the accuracy of information reported on Forms 730.³⁹ However, these initiatives have been limited to the following results:

- During FYs 2018 through 2022, the IRS closed [REDACTED]
- In FYs 2023 and 2024, the IRS closed 263 examinations of Forms 730 under the *Illegal Bookmaking Activities* and the *Wagering – Online Activity* initiatives.
- As of March 2024, the IRS had not closed any examinations of Forms 730 under the *Legal Gambling* or *Workload Return System* initiatives.

Other than the referral process and the four initiatives, IRS officials stated that they are not aware of any other actions taken to follow up on nonfiled Forms 730. Furthermore, the Excise Tax program does not leverage information reported by payers on the Form W-2G to evaluate compliance with excise tax and has conducted minimal research in this area.

³⁷ As previously mentioned, the Form 730 is used to report the excise taxes imposed for being in the business of accepting wagers for oneself or on behalf of someone else. I.R.C. §§ 4401-4424 provide for the imposition of excise taxes, which are independent of income taxes, on certain types of wagers.

³⁸ From FY 2018 through FY 2022, the Excise Tax function closed 2,555 examinations of Forms 730, resulting in assessments of approximately \$8.6 million.

³⁹ These four initiatives are: *Illegal Bookmaking Activities* (Jan. 2021), *Wagering – Online Activity* (Jan. 2021), *Legal Gambling* (Jan. 2021), and *Workload Return System* (initiated in CY 2005 and revised Sept. 2023).

According to Publication 1220, payers are required to report the type of gambling activity in Box 3, Type of wager, when filing Form W-2G. This information is a key component of the Form W-2G and could be used as a tool to identify potential nonfilers and underreporters of excise tax related to gambling winnings. However, the Form W-2G has not evolved with the growth of the gambling industry. For example, the wager codes on Form W-2G include only nine specific types of gambling activities, which do not include a wager code for sports betting. If there was a wager code specifically for sports betting, the IRS could use this information to identify potential nonfilers and underreporters of excise tax related to these gambling activities. Additionally, some gambling entities are incorrectly issuing Form 1099-MISC, *Miscellaneous Income*, instead of Form W-2G for winnings from wagers associated with Daily Fantasy Sports, despite an IRS Office of Chief Counsel Advice Memorandum, dated September 14, 2020, stating that Daily Fantasy Sports entities must issue Form W-2G.⁴⁰ As a result, these entities are potentially not paying the excise tax associated with the wagers for these gambling activities.

We analyzed the Forms W-2G with a Wager Code 9 issued during TYs 2018 through 2020.⁴¹ Wager Code 9 has a high potential for gambling activities related to sports betting.⁴² We matched these Forms W-2G to all Forms 730 filed to determine whether the payers filed the required Form 730. Our analysis found an annual average of 42 payers that did not file any Forms 730 despite issuing more than 3.8 million Forms W-2G with a Wager Code 9. The combined gambling winnings reported on these Forms W-2G was \$16.7 billion with \$1.5 billion in Federal tax withheld, an effective rate of only 9 percent, instead of the required 24 percent.⁴³

As cited in a July 2023 Congressional Research Service report, AGA data indicated that the GGR from commercial wagering operations, *i.e.*, excluding tribal casinos, reached \$60.5 billion in CY 2022, which was substantially higher than previous years.⁴⁴ Sports betting and online gambling significantly contributed to this growth because they are the fastest growing segments of the gambling industry. Figure 9 shows the increase in the commercial gambling industry from CY 2018 through CY 2022.

⁴⁰ The IRS Office of Chief Counsel initially issued a General Legal Advice Memorandum on July 23, 2020, that concludes that entry fees for daily fantasy sports contests are taxable wagers, and thus, daily fantasy sports operators are liable for the excise tax on wagers.

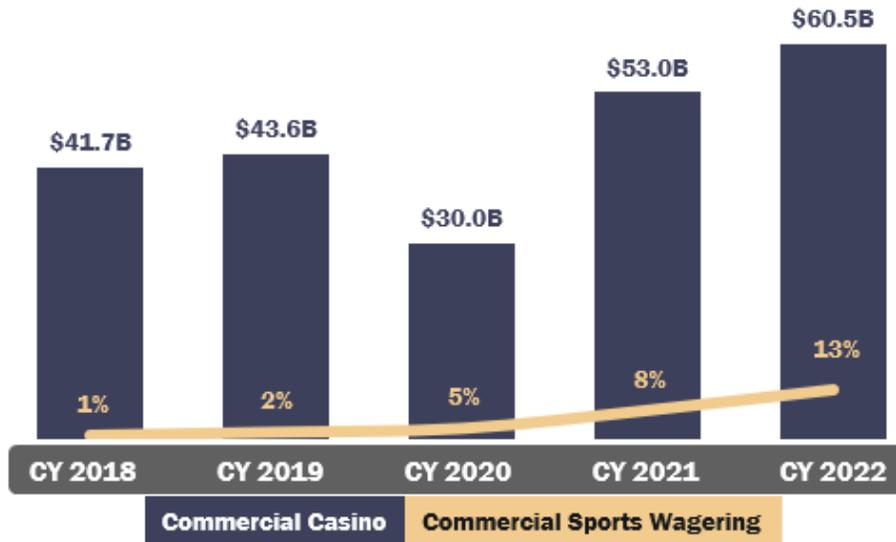
⁴¹ We identified 903,174 (2 percent) of approximately 43 million Forms W-2G that did not show a wager code, which we removed from our analysis and may also be subject to excise tax.

⁴² Gambling activities associated with Wager Code 9 are potentially subject to excise tax and include sports betting, certain online gambling such as sports wagering and daily fantasy sports, and any other gambling activity that is not defined by Wager Codes 1 through 8, as shown in Figure 4.

⁴³ Because the Form W-2G does not record the amount of the wager, there is no way to determine the amount of unreported excise tax associated with these Forms W-2G.

⁴⁴ This information was also reported in Congressional Research Service, In Focus Report Number IF12461, *Casino Gambling and Economic Development* (July 2023).

Figure 9: Legal Commercial Sports Wagering As a Percentage of Total Commercial Gambling



Source: TIGTA analysis of the AGA’s Commercial Casino Industry annual “State of the States” analysis.

According to the AGA, the GGRs for sports betting increased from \$430.7 million in CY 2018 to \$7.56 billion in CY 2022, and the GGRs for online gambling increased from \$520 million in CY 2019 to \$5.02 billion in CY 2022.⁴⁵ Despite this significant growth, the IRS has conducted minimal research in these areas. In February 2016, the Excise Case Selection Joint Operations Center conducted research on the Daily Fantasy Sports industry and estimated that the fantasy sports industry was a \$2 billion industry as of May 2015. In September 2020, the Excise Case Selection Joint Operations Center completed a preliminary analysis of the sportsbook wagering industry and identified 14 casino taxpayers that showed significant statistical anomalies, which were referred to the SB/SE Division’s Excise Tax function for further review. As of December 2023, examinations of eight of the 14 taxpayers were surveyed, *i.e.*, closed without completion of the audit, due to short statutes, and the remaining six taxpayers were still awaiting assignment for further review. Outside of research related to specific casework, the IRS has not conducted any research since September 2020 on the overall gambling industry that assesses the current and future conditions of sports betting and online gambling industries as well as the industries’ risks and impact on tax compliance.

The authorized wagers reported to the IRS on Forms 730 for a five-year period were approximately \$44 billion less than a trade group estimate for the same period.

The AGA claims that wagers for legal (authorized) sports betting alone totaled approximately \$192 billion during CYs 2018 through 2022.⁴⁶ However, during the same period, all wagering activity reported on the Forms 730 filed with the IRS totaled approximately \$148 billion,

⁴⁵ Online gambling includes sports betting as well as other gambling activities.

⁴⁶ The AGA does not track sports betting at tribal casinos.

approximately \$44 billion less than the total wagers that the AGA claimed for legal (authorized) sports betting.⁴⁷

According to new AGA research on illegal gaming operations, Americans wager an estimated \$511 billion annually on illegal and unregulated sportsbooks, online gambling websites, and unregulated electronic gaming devices in bars, convenience stores, and other non-casino locations. While it is impossible to verify an estimate of illegal revenue, it is essential for the IRS to conduct research to evaluate the risk of Form 730 noncompliance from nonfilers and underreporters of excise tax throughout the gambling industry and develop a strategy to bring payers into compliance with Form 730 filing requirements and excise tax payments.

The Commissioner, SB/SE Division, should:

Recommendation 4: Expand the wager codes to specifically include sports betting and use the wager code as a tool to identify potential noncompliance of excise taxes.

Management's Response: The IRS partially agreed with this recommendation and will explore the potential productivity and feasibility of expanding the wager codes to specifically include sports betting.

Office of Audit Comment: According to Publication 1220, payers are required to report the type of gambling activity in Box 3, *Type of wager*, when filing a Form W-2G. This information allows the IRS to categorize the source of the gambling income and can be used as a tool to identify potential nonfilers and underreporters of excise tax related to gambling winnings. However, the Form W-2G has not evolved with the growth of the gambling industry. Currently, the wager codes on Form W-2G include nine specific types of gambling activities, including one for jai alai, but do not include a wager code for sports betting. The IRS could use this information to identify potential nonfilers and underreporters of excise tax related to these gambling activities.

Recommendation 5: Conduct an environment scan of the current and potential future conditions of the sports betting and online gambling industries, the industries' risks, and the impact on tax compliance, and develop a process to identify and address Form 730 nonfilers and underreporter noncompliance.

Management's Response: The IRS agreed with this recommendation and will conduct an environment scan of the current and potential future conditions of the sports betting and online gambling industries, the industries' risks, and impact on tax compliance, and update existing or create new charters to identify noncompliance.

⁴⁷ Because Form 730 does not allow for reporting of wager types, there is no way to distinguish between types of wagering activity. Therefore, this \$148 billion of legal wagers was not limited to sports wagering.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this audit was to evaluate the IRS's efforts to promote income tax compliance for individuals who have reported winnings from gambling activities and compliance by gaming operators responsible for payment of associated excise taxes on wagering. To accomplish our objective, we:

- Obtained an understanding of IRS operations and efforts to promote income tax filing and reporting compliance associated with individual wagering by researching and analyzing IRS policies and procedures and Federal and State laws, and interviewing IRS management responsible for promoting income tax filing compliance efforts associated with individuals with winnings reported on Forms W-2G.
- Extracted available Form W-2G data from the TIGTA DCW and analyzed the data for obvious income tax filing and reporting noncompliance, significant outliers, and other readily identifiable trends.
- Researched and analyzed Federal and State laws associated with excise taxes on wagering as well as IRS procedures, guidance, and best practices used to promote compliance in the filing, reporting, and payment compliance of excise taxes on wagering.
- Researched and interviewed IRS management to determine how the IRS evaluates risk associated with excise taxes in the gambling industry and identifies potential noncompliance. We used extract-available Business Returns Transaction File data associated with the Form 730 and analyzed the data for obvious instances of potential noncompliance, which may not have been identified by the IRS's efforts.
- Evaluated the risk for fraud, waste, and abuse to obtain reasonable assurance that widespread improprieties do not exist in the processes or functions included in our testing.

Performance of This Review

This review was performed with information obtained from the SB/SE Division located in Lanham, Maryland, during the period March 2022 through March 2024. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Major contributors to the report were Matthew Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations); Phyllis Heald London, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations), Frank O'Connor, Acting Assistant Inspector General for Audit (Compliance and Enforcement Operations); Robert Jenness, Director; Tina Fitzsimmons, Audit Manager; Curtis Kirschner, Audit Manager; Charles Nall, Lead Auditor; Daniel O'Keefe, Senior Auditor; Charles Gambino, Auditor; and Thomas Lipski, Auditor.

Data Validation Methodology

For this review, we relied on data obtained from TIGTA DCW extracts of the Information Returns Master File, the IMF CCNIP, and the Business Returns Transaction File. These files are extracted by and maintained at TIGTA's DCW. Before relying on the data, we evaluated their sufficiency and reliability to ensure that the data fields were accurately stated. In addition, we assessed the appropriateness of data within the requested fields against information obtained from the IRS's Integrated Data Retrieval System as well as working with our Applied Research and Technology Data Analytics group to develop tests to ensure that we were using the most accurate data available to report on. We determined that the data were sufficiently reliable for purposes of this report.

Internal Controls Methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: the IRS's policies and procedures related to tax reporting and compliance of wagering activity. We evaluated these controls by reviewing and analyzing relevant data; interviewing IRS management and personnel; reviewing relevant guidance; and performing analysis on Forms W-2G, Forms 730, and IMF CCNIP data.

Appendix II

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to Congress.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; \$1,378,183,554 in additional tax revenue by addressing 139,045 individual nonfilers with total gambling winnings greater than \$15,000 during TYs 2018 through 2020 (see Recommendations 1 and 2).¹

Methodology Used to Measure the Reported Benefit:

We analyzed all Forms W-2G issued to individual taxpayers during TYs 2018 through 2020 (as of March 2023) and identified 148,908 individual taxpayers who were issued one or more Forms W-2G (with a total amount reported of more than \$15,000 per individual) and did not file a tax return. These nonfilers were associated with 4,068,132 Forms W-2G with \$13,190,213,630 in total gambling winnings and \$287,542,768 in Federal taxes withheld from these winnings (approximately 2 percent of the total gambling winnings).

We matched these 148,908 nonfilers to IMF CCNIP inventory and found that 139,045 were also present in IMF CCNIP inventory. Based on IMF CCNIP data, the estimated net tax due for these nonfilers was \$3,445,458,886. Furthermore, 51,792 (37 percent) of the 139,045 nonfilers were considered high-income nonfilers by the IRS and accounted for \$3,108,659,742 (90 percent) of the estimated \$3,445,458,886 net tax due.

The IMF CCNIP estimated tax due does not consider losses and/or deductions that may adjust the taxable income if the taxpayer filed a tax return, which could reduce the potential tax due. In response to our audit work, the IRS analyzed a population of 17,436 TY 2018 high-income nonfilers with total positive income greater than or equal to \$100,000. Based on this data, the IRS calculated that 40 percent of the IMF CCNIP estimated net tax due was actually assessed. Therefore, the IRS recommended that the potential outcome measure projection of the IMF CCNIP estimated tax due amount be reduced by 60 percent. Based on the IRS analysis, we reduced the \$3,445,458,886 of estimated net tax due for these nonfilers by 60 percent as follows:

- $\$3,445,458,886 \times .60$ (estimated net tax due from nonfilers) = \$2,067,275,332
- $\$3,445,458,886 - \$2,067,275,332 = \$1,378,183,554$

¹ Using income reported on information returns alone is not an exact method to estimate the taxpayer's potential tax due, and it may be overstating the tax due for some taxpayers. For example, if the taxpayer files their income tax return, they may report gambling losses and/or deductions that reduce their taxable income, therefore reducing their tax due.

Management's Response: The IRS agreed with the potential \$1,378,183,554 in additional tax revenue by addressing 139,045 individual nonfilers with total gambling winnings greater than \$15,000 during TYs 2018 through 2020.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; \$1,733,703 in additional tax revenue by addressing 471 Forms W-2G that were issued by 122 unique payers with no backup withholding applied and missing TINs (see Recommendation 3).

Methodology Used to Measure the Reported Benefit:

We analyzed all Forms W-2G issued during Filing Years 2018 through 2021 and identified 23,013, with total gambling winnings of \$362,811,188, that were issued to payees with TINs identified as invalid by the IRS.² Each of the Forms W-2G had gambling winnings greater than \$5,000 with no Federal tax withheld. We further analyzed the 23,013 Forms W-2G and found 616 with missing TINs, *i.e.*, 000-00-0000. These 616 Forms W-2G were issued by 171 payers and had combined gambling winnings of \$11,333,230.

The 171 payers associated with the 616 Forms W-2G with missing payee TINs over four years represented 133 unique payers, *i.e.*, some payers were included in more than one year. These 133 payers should have immediately withheld backup withholding of \$2,719,975 (24 percent of \$11,333,230) from the gambling winnings.

We further analyzed the 133 payers and found that 11 had at least one code indicating that a penalty for failing to file a correct information return applied to their tax account during TYs 2018 through 2021. These penalties totaled \$370,470 and may have included penalties applied because of other information returns.³ These 11 payers were associated with 145 of the 616 Forms W-2G with missing payee TINs. For the remaining 122 payers that issued 471 Forms W-2G with missing payee TINs with gambling winnings of \$7,223,762, the IRS should pursue backup withholding of at least \$1,733,703. We calculated the value of this outcome as follows:

- $\$7,223,762 \times .24$ (backup withholding rate) = \$1,733,703

Management's Response: The IRS disagreed with our potential outcome measure. IRS management does not have available information about the winnings associated with the subset of 471 Forms W-2Gs identified to verify this outcome measure. To verify the outcome measure, the IRS would need to analyze the specific amounts associated with the 122 unique payers, as well as compare these amounts against other backup withholding information. Under I.R.C. § 3402(d), backup withholding is reduced if the payee reported the income and paid the tax, and payers may secure Forms 4669 signed by the payee stating that the income was reported by the payee, which would serve to ultimately abate backup withholding under I.R.C. § 3402(d).

² We used the IRS's validity indicator to identify invalid TINs. Internal Revenue Manual 3.13.5 defines one of the most common reasons for an invalid TIN is when the taxpayer's Social Security Number and the name control do not match to the names and Social Security Numbers assigned by the Social Security Administration.

³ These penalties may have included other information returns and not exclusively the Forms W-2G identified in our analysis.

Office of Audit Comment: We maintain our position that the outcome measure is valid and reasonable as presented. We based the estimate on Forms W-2G issued with missing TINs, *i.e.*, 000-00-0000, and having gambling winnings greater than \$5,000 with no Federal tax withheld. According to IRS guidance, payers should “begin backup withholding immediately on any reportable payments” when the payee refuses or neglects to provide a correct TIN. While the IRS suggests scenarios where withholding may have not been applicable, the facts and circumstances around why backup withholding was not applied cannot be determined without further outreach, review, or an examination. We provided a list of the payers to the IRS for review, and the IRS stated that none of the payers within our population had been selected for review. However, we acknowledge that if the IRS reviewed the identified tax accounts, the actual amount of increased revenue may be higher or lower than our estimate.

Appendix III

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

September 26, 2024

MEMORANDUM FOR DANNY R. VERNEUILLE
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT
Amalia C. Colbert

FROM: Lia Colbert
Commissioner, Small Business/Self-Employed Division

Digitally signed by Amalia
C. Colbert
Date: 2024.09.26
13:12:31 -04'00'

SUBJECT: Draft Audit Report – The IRS Could Collect Over a Billion Dollars
in Potential Taxes from Unreported Wagering Income
(Audit No.: 202230021)

Thank you for the opportunity to review and comment on the subject draft audit report. Tax compliance on wagering activities is an important area of focus for the IRS. In May 2018, the United States Supreme Court struck down the 1992 Professional and Amateur Sports Protection Act, which had restricted the growth of sports betting by preventing States from authorizing it. The Supreme Court's decision gave each state the ability to determine and establish its own regulated sports betting law(s). Although this decision led to rapid expansion of sports betting activities, the IRS has existing procedures in place to effectively address tax compliance from wagering activities.

We are committed to improving tax compliance and appreciate your acknowledgement of the efforts we have taken to establish a cross-functional group to analyze backup withholding policies and procedures. In addition, the work on this audit identified extremely low error rates on Forms W-2G, *Certain Gambling Winnings*, filed by taxpayers.

Although we have initiatives already in place to identify non-compliance for income and excise taxes on wagering activities, we will review our initiatives and evaluate their effectiveness. In addition, we agree to review the population of nonfilers with gambling winnings and prioritize enforcement efforts on high income nonfilers. We strive to properly serve compliant taxpayers while upholding the nation's tax laws. Using fair and impartial audit plans, we make tough choices each year regarding where to deploy our finite resources across the breadth of our responsibilities.

Attached are our comments in response to your recommendations and proposed outcome measures. If you have any questions, please contact me, or Rich Tierney, Director Examination, Small Business/Self-Employed Division.

Attachment

Attachment

Recommendations

The Commissioner, SB/SE Division, should:

RECOMMENDATION 1:

Begin appropriate enforcement actions starting with notice issuance, on the population of nonfilers with gambling winnings for TYs 2018 through 2020, prioritizing high-income nonfilers, including the top 100 nonfiler cases identified by TIGTA.

CORRECTIVE ACTION:

We agree. For Tax Years (TY) 2018 through 2020, the IRS will identify high income nonfilers with gambling winnings where no enforcement actions have been taken, including the top 100 nonfiler cases identified by TIGTA. If appropriate, the IRS will begin enforcement by issuing the first return delinquency notice, CP59.

IMPLEMENTATION DATE:

October 15, 2025

RESPONSIBLE OFFICIAL:

Director, Collection Inventory Delivery and Selection, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:

We will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 2:

Review the population of nonfilers with gambling winnings for TYs 2018 through 2020 that were not identified by the IMF CCNIP and begin appropriate enforcement actions as warranted.

CORRECTIVE ACTION:

We agree. We will review and profile the population of nonfilers with gambling winnings for TYs 2018 through 2020 that were not identified by the IMF CCNIP (Individual Master File Case Creation Nonfiler Identification Process). This research will determine potential reasons why they were not identified and assess the current state of these returns to determine if the filing requirement has been satisfied. If the filing requirement has not been satisfied and enforcement is applicable, then manual enforcement of return delinquency will be considered by either Collection or Exam.

IMPLEMENTATION DATE:

April 15, 2026

RESPONSIBLE OFFICIAL:

Director, Collection Inventory Delivery and Selection, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:

We will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 3:

The Commissioner, SB/SE Division, should analyze Forms W-2G with missing TINs to determine what forms of wagering and/or gambling institutions may be noncompliant. If the cases identified are related to another IRS division, share the results with that division. The results of this analysis should be shared with Exam Case Selection and influence future taxpayer outreach.

CORRECTIVE ACTION:

We disagree. TIGTA's analysis identified a very insignificant percentage, .0010%, of Forms W-2G with missing TINs. The IRS already has processes in place to identify and address compliance with information reporting and considers TIGTA's finding of an insignificant error rate to be a positive reflection of IRS efforts.

IMPLEMENTATION DATE:

N/A

RESPONSIBLE OFFICIAL:

N/A

CORRECTIVE ACTION MONITORING PLAN:

N/A

The Commissioner, SB/SE Division, should:

RECOMMENDATION 4:

Expand the wager codes to specifically include sports betting and use the wager code as a tool to identify potential noncompliance of excise taxes.

CORRECTIVE ACTION:

We partially agree. We will explore the potential productivity and feasibility of expanding the wager codes to specifically include sports betting.

IMPLEMENTATION DATE:

October 15, 2025

RESPONSIBLE OFFICIAL:

Director, Specialty Policy, Examination, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:

We will monitor this corrective action as part of our internal management system of controls.

RECOMMENDATION 5:

Conduct an environment scan of the current and potential future conditions of the sports betting and online gambling industries, the industries' risks, and the impact on tax compliance, and develop a process to identify and address Form 730 nonfilers and underreporter noncompliance.

CORRECTIVE ACTION:

We agree. We will conduct an environment scan of the current and potential future conditions of the sports betting and online gambling industries, the industries' risks, and impact on tax compliance, and update existing or create new charters to identify noncompliance.

IMPLEMENTATION DATE:

February 15, 2026

RESPONSIBLE OFFICIAL:

Director, Exam Case Selection, Small Business/Self-Employed Division

CORRECTIVE ACTION MONITORING PLAN:

We will monitor this corrective action as part of our internal management system of controls.

Outcome Measure 1:

Increased Revenue – Potential; \$1,378,183,554 in additional tax revenue by addressing 139,045 individual nonfilers with total gambling winnings greater than \$15,000 during TYs 2018 through 2020 (see Recommendations 1 and 2)

IRS Response:

We agree.

Outcome Measure 2:

Increased Revenue – Potential; \$1,733,703 in additional tax revenue by addressing 471 Forms W-2G that were issued by 122 unique payers with no backup withholding applied and missing TINs (see Recommendation 3).

IRS Response:

We disagree. We do not have available information about the winnings associated with the subset of 471 Forms W-2Gs identified to verify this outcome measure. To verify the outcome measure, we would need to analyze the specific amounts associated with the 122 unique payers. In addition, we would have to compare these amounts against other backup withholding information. Under IRC 3402(d), backup withholding is reduced if the payee reported the income and paid the tax, and payers may secure Forms 4669 signed by the payee stating that the payee reported the income, which will serve to ultimately abate backup withholding under 3402(d).

Glossary of Terms

Term	Definition
American Gaming Association	A national trade group for the U.S. casino industry.
Automated Collection System	A system that generates notices to taxpayers who can contact call centers where IRS Collection representatives try to resolve the issue.
Automated Substitute for Return Program	<p>The Automated Substitute for Return program was developed to systemically promote compliance with taxpayers who have not filed tax returns voluntarily and for whom income information is available to substantiate a significant income tax liability without costly field investigation. The purpose of this program is to assess the tax liability and promote compliance by either:</p> <ul style="list-style-type: none"> • Securing a valid voluntary income tax return from the taxpayer. • Computing tax, interest, and penalties based upon Information Returns Program documents submitted by payers, or other internally available information.
Backup Withholding	Persons (payers) making certain payments to payees must withhold and pay to the IRS a specified percentage of those payments under certain conditions. The Backup Withholding Rate Percentage is 24 percent, effective for all subject payments made after December 31, 2017.
Collection Queue	An automated holding file for unassigned inventory of delinquent cases for which revenue officers are unable to be immediately assigned for contact due to limited resources.
Criminal Investigation	An IRS business unit that investigates potential criminal violations of the I.R.C. and related financial crimes.
Data Center Warehouse	A collection of IRS databases containing several types of taxpayer accounts and IRS and TIGTA employee information that is maintained by TIGTA for the purpose of analyzing data for ongoing audits.
Fiscal Year	Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government’s fiscal year begins on October 1 and ends on September 30.
Gross Gambling Revenue	The difference between the amount of money players wager minus the amount that they win.
High-Income Nonfilers	A term used by the IRS to identify any nonfiler with a total income greater than or equal to \$100,000 prior to December 2022, and greater than \$200,000 thereafter.
Individual Master File	The IRS database that maintains transactions or records of individual tax accounts.

The IRS Could Collect Over a Billion Dollars in Taxes From Unreported Wagering Income

Term	Definition
Information Returns Master File	Maintains a master batch file of current tax year information returns and maintains access to nine prior years. Beginning in January of each year, extracts are made from the entire Individual Returns Master File on a weekly basis.
Information Returns Program	Identifies taxpayers who have underreported their income by matching information documents received by third parties to the income reported on the individual's tax return.
Internal Revenue Code	The body of law that codifies all Federal tax laws. These laws constitute Title 26 of the United States Code, which is a consolidation and codification by subject matter of the general and permanent laws of the United States.
Nonfilers	Individual and business taxpayers who have been identified as liable to file a tax return but who have not filed a tax return by the return due date or extended due date.
Online gambling	Online gambling allows gamblers to play virtual casino and poker games using their own mobile devices or home computers via accounts they have established with operators of gaming websites.
Processing Year	The calendar year in which the IRS processes the tax return or document.
Revenue Officer	An IRS employee in the Collection function who provides customer service by explaining taxpayer rights and responsibilities, collects delinquent accounts, secures delinquent returns, counsels taxpayers on their tax filing and payment obligations, conducts tax investigations, files Notices of Federal Tax Lien, releases Federal tax liens, and performs seizures and sales of delinquent taxpayer assets.
Revenue Officer Compliance Sweeps	An assignment of work strategy used by IRS Field Collection to support compliance initiatives. The purpose of a Revenue Officer Compliance Sweep is to address an increase in unassigned high-priority inventory aligned to a compliance initiative, <i>e.g.</i> , egregious employment tax cases, high-income nonfilers, or specialty program, in each area or program due to current field compliance staffing or to support a compliance initiative.
Social Security Number	A nine-digit number issued to an individual by the Social Security Administration. The IRS uses this number to process tax documents and returns.
Sports Betting	Sports betting encompasses all sports wagering activity, both in-person and online, including daily fantasy sports.
Substitute for Return	Tax returns prepared by the IRS, based on I.R.C. provisions, when taxpayers appear to be liable for taxes but have not voluntarily filed their returns.
Tax Gap	The estimated difference between the amount of tax that taxpayers should pay, and the amount paid voluntarily and on time.
Tax Year	A 12-month accounting period for keeping records on income and expenses used as the basis for calculating the annual taxes due. For most individual taxpayers, the tax year is synonymous with the calendar year.
Taxpayer Delinquency Investigation	An account for which it appears a tax return has not been filed by a taxpayer.

The IRS Could Collect Over a Billion Dollars in Taxes From Unreported Wagering Income

Term	Definition
Taxpayer Identification Number	A nine-digit number assigned to taxpayers for identification purposes. Depending upon the nature of the taxpayer, it can be an Employer Identification Number, a Social Security Number, or an Individual Taxpayer Identification Number.
Total Positive Income	The sum of all positive amounts shown for the various sources of income reported on the individual tax return and, therefore, excludes losses.

Appendix V

Abbreviations

AGA	American Gaming Association
CY	Calendar Year
DCW	Data Center Warehouse
FY	Fiscal Year
GGR	Gross Gambling Revenue
IMF CCNIP	Individual Master File Case Creation Nonfiler Identification Process
IRA	Inflation Reduction Act of 2022
I.R.C.	Internal Revenue Code
IRS	Internal Revenue Service
SB/SE	Small Business/Self-Employed
TDI	Tax Delinquency Investigation
TIGTA	Treasury Inspector General for Tax Administration
TIN	Taxpayer Identification Number
TY	Tax Year



**To report fraud, waste, or abuse,
contact our hotline on the web at www.tigta.gov or via e-mail at
oi.govreports@tigta.treas.gov.**

**To make suggestions to improve IRS policies, processes, or systems
affecting taxpayers, contact us at www.tigta.gov/form/suggestions.**

Information you provide is confidential, and you may remain anonymous.