

CRANBERRY MAGNETITE CORP. '
Post Office Box 188
Pounding Mills, Virginia 24637, '

STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

Taxpayer, '

DOCKET NOS. INC. 95-371
S. 95-372
WITH. 96-402

v. '

STATE OF ALABAMA
DEPARTMENT OF REVENUE.

FINAL ORDER
ON APPLICATION FOR REHEARING

The Final Order entered on April 14, 1997 dismissed the wager winnings withholding tax final assessment in issue (Docket No. Inc. 95-371) because the Department failed to prove that the \$5,000 plus payouts by the Taxpayer were "winnings subject to withholding" as defined at Code of Ala. 1975, ' 40-18-90 and 26 U.S.C. ' 3402. Rather, the evidence established that the payouts were from bingo, which is specifically excluded from withholding at 26 U.S.C. ' 3402(q)(5). The Department timely applied for a rehearing.

Certain wager winnings are subject to Alabama withholding tax. See, ' 40-18-90. "Winnings subject to withholding" is defined for Alabama purposes the same as for federal purposes at 26 U.S.C. ' 3402. See, ' 40-18-90(3). Section 3402(q)(5) specifically excludes from withholding all winnings from bingo.

As indicated, the Taxpayer operated bingo games in Piedmont during the subject period. The Department argues, however, that because the bingo was not conducted in accordance with the Alabama Constitution and Piedmont ordinances, i.e.

was not "legal" bingo, it did not qualify as exempt bingo under ' 3402(q)(5), citing the definition of bingo at 26 U.S.C. ' 513. Specifically, ' 513(f)(2)(C) requires that bingo must be conducted in accordance with State and local laws.

I disagree with the Department's position that the ' 513 definition of bingo is applicable to ' 3402.

26 U.S.C. ' 511 levies an income tax on the unrelated business income of certain charities. Section 513 defines "unrelated trade or business" for purposes of the ' 511 tax. Section 513(f)(1) specifies that "unrelated trade or business" does not include bingo. Section 513(f)(2) then defines bingo games "for purposes of paragraph (1)."

The ' 513(f)(2) definition of bingo specifically relates only to the ' 511 tax on charities, and should not be read in *para materia* with ' 3402, as argued by the Department. Sections 511 and 3402 relate to different subjects entirely. Section 3402 does not refer to or adopt the definition of bingo at ' 513, and there is otherwise no statutory or logical reason why the limited definition of bingo at ' 513(f)(2) should apply to ' 3402.

Because ' 3402 does not define bingo, its commonly understood definition must apply. IMED Corp. v. Systems Engineering Assoc. Corp, 602 So.2d 344 (Ala. 1992).

Ironically, even if the ' 513 definition is used, the first step in determining if an activity constitutes bingo as defined at ' 513, is whether it fits the commonly understood and generally accepted definition of bingo. See, Julius M. Israel Lodge of B'nai B'rith v. C.I.R., 98 F.3d 190 (5th Cir. 1996). Only if the activity is bingo, as

commonly defined, is it then necessary to look at the specific definition of "bingo" at ' 513(f)(2). "Normally only after we have determined that a 'bingo game' is 'any game of bingo' (as generally defined) must we then look to the limiting factors upon such 'game of bingo' outlined in" Sections 513(f)(2)(A), (B) and (C). Julius M. Israel Lodge, 98 F.3d at 192. The Court in Julius M. Israel Lodge found that the activity in issue, Instant Bingo, was not bingo as commonly defined. There is no evidence to support such a finding in this case.

There is some general reference to "pull tabs" in the record, but the use of pull tabs apparently ceased early in the audit period. Importantly, there is no substantive evidence that the \$5,000 plus payouts on which the Department based its assessment were derived from any activity other than exempt bingo.

The Department also cites State v. Crayton, 344 So.2d 771 (Ala.Civ.App.), *cert denied*, 344 So.2d 775 (1977), for its position that bingo is a lottery, and thus is a wagering transaction subject to the wager winnings withholding tax at 26 U.S.C. ' 3402. I disagree.

The issue in Crayton was whether a bingo parlor was a "place of amusement or entertainment," and thus subject to the public amusement gross receipts sales tax levied at Code of Ala. 1975, ' 40-23-2(2). The Court of Civil Appeals correctly held that it was.

Although not necessary to its finding, the Court also stated as *dicta* that bingo was a lottery. However, Crayton was decided in 1977, before the Alabama

Constitution was amended to allow bingo in various counties. Legal bingo was first allowed in Jefferson County by Amendment 386 in 1980. Thus, all bingo was an illegal lottery in Alabama when Crayton was decided.

In any case, the analogy between bingo and a lottery in Crayton is clearly inappropriate in construing ' 3402. Certain lottery winnings are subject to withholding, but bingo winnings are specifically exempted. Consequently, bingo must be distinguished from a lottery for purposes of ' 3402. Otherwise, the exclusion for bingo provided at ' 3402(q)(5) would be meaningless.

The Department, on page 6 of its application for rehearing, argues that there is sufficient evidence to support the wager withholding assessment. I agree that there is ample evidence (the W-2Gs) from which the Department could compute a liability. However, what the Final Order held is that there is insufficient evidence that the \$5,000 plus payouts were from a taxable wagering transaction other than exempt bingo. There is no evidence from which I can reasonably find that the payouts qualified as "winnings subject to withholding" as defined at ' 3402(q)(3). Without a rational substantive basis, the final assessment must be dismissed. That finding is affirmed.

Finally, I do not understand the Department's argument that by dismissing the withholding tax assessment, "illegal" bingo is allowed preferential treatment over legal bingo. Anyone conducting bingo, whether it complies with State and local laws or

not, is required to comply with the tax reporting requirements established by federal and Alabama law. There is no advantage given to "illegal" bingo.

The above considered, the Department's application for rehearing is denied.

The Final Order is affirmed.

This Final Order on Application for Rehearing may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, ' 40-2A-9(g).

Entered August 6, 1997.

BILL THOMPSON
Chief Administrative Law Judge