STATE OF WISCONSIN

TAX APPEALS COMMISSION

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**JEFFREY AND REBECCA GRUNDAHL,** **DOCKET NO. 08-I-173**

Petitioners,

vs. **DECISION AND ORDER**

**WISCONSIN DEPARTMENT OF REVENUE,**

Respondent.

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**THOMAS J. MCADAMS, COMMISSIONER**:

This case comes before the Commission for decision after a trial was held in this matter in Madison, Wisconsin on September 30, 2009. The Petitioners, Mr. and Mrs. Jeffrey Grundahl of Reedsburg, Wisconsin, are *pro se* in this matter and have filed a post-trial brief. The Respondent in this matter (also referred to in this decision as "the Department") is represented in this matter by Attorney Peter D. Kafkas, of Madison, who has also filed a post-trial brief. The legal issue in this case is if the Petitioners have proved that Mr. Grundahl was a professional gambler in the years 2004 and 2006 such that they may deduct the cost of his wagers against his winnings.

Based on the evidence received at trial, the Commission finds, concludes, and orders as follows:

## FINDINGS OF FACT[1]

### A. Jurisdictional Facts

1. The Department issued the assessment for $10,239.63 against the Petitioners on February 22, 2008 for a period that covers 2004, 2005, and 2006. Of that amount, $8,230.00 was for the income tax, and $2,009.63 was for interest. The explanation section of the Department's assessment form states that "Based on information submitted, you do not qualify as a professional gambler." Respondent's Exhibit 1.

2. On March 28, 2008 the Petitioners filed a Petition for Redetermination with the Department, claiming that during the relevant period Mr. Grundahl was a "probability analyst." Exhibit 2.

3. The Department denied the Petition for Redetermination by way of the notice of action the Department issued on September 17, 2008. Exhibit 3.

4. The Petitioners filed a timely Petition before the Tax Appeals Commission on November 10, 2008. In the petition, Mr. Grundahl wrote as follows:

> This Petition is to declare my appeal of denial of my status as a professional gambler. The Department states I was a recreational gambler which could not be further from the truth. I have complete records and documentation of all machines played... My taxes were filed correctly and all other tax matters were found in my favor...

Exhibit 4.

[1] The findings of fact are taken from the trial testimony and the exhibits.

**B. Material Facts**

1. During the period in question, the Petitioners resided in Reedsburg, Wisconsin, and Mr. Grundahl went to the Ho-Chunk casino in Baraboo between 48 and 60 hours per week in 2004 and in 2006. He would go there around 11:00 a.m. and come home at around 9:00 p.m. On Saturdays, he would go in at 8:00 a.m. and remain there until around 1:00 p.m. Transcript at 27.

2. At the beginning of the week, Mr. Grundahl would take $1,000 of the Petitioners' money to the casino in his pocket to gamble with. At the end of the week, Mr. Grundahl would count how much was in his pocket to determine his winnings and his losses and then enter the number in his spiral notebook. *Id.*

3. Mr. Grundahl played the dog track in the 1990's. Transcript at 31.

4. In 2004, the Petitioners made an alleged gross profit of $17,160 at the casino. *Id*.

5. Mr. Grundahl played hundreds of quarter and dollar slot machines each day he went to the casino. Transcript at 32.

6. Mr. Grundahl had criteria for the slot machines[2] he would play, only playing machines he thought were in an "advantageous mode." The slot machines that have the advantageous mode are also called top box bonus machines. Transcript at 37.

[2] Slot machines as referred to herein are casino gaming devices that spin reels---whether the reels are moving parts or images on a video screen---to determine the outcome of a wager. When we use the term "slot machines" in this opinion, video poker is not included.

7. Mr. Grundahl had no other occupations during 2004 and supported his wife and five children by gambling. Transcript at 38.

8. Mr. Grundahl did not gamble professionally in 2005 as there was construction at the casino. Instead, the Petitioners attempted to get a sales business started on E-Bay.com. Transcript at 39.

9. In 2006, Mr. Grundahl went back to gambling (in addition to internet sales) and made $9,423 at the casino. This included a gross amount of $26,000 in winnings from which the Petitioners subtracted expenses of $16,973. *Id.* and p. 47.

10. Mr. Grundahl played both traditional slot machines and video poker. Transcript at 62.

11. Mr. Grundahl's training for this line of work consisted of reading one book, Mr. Charles W. Lund's *Robbing the One Armed Bandits: Finding and Exploiting Advantageous Slot Machines* (RGE Publishing, 1st edition, 1999). ("Lund Book"). Transcript at 44.

12. Mr. Grundahl reviewed a computer program for his training at video poker entitled *Bob Dancer Presents WinPoker, version 6.0.* Transcript at 57.

13. In 2007, the casino replaced the machines Mr. Grundahl believed were advantageous and Mr. Grundahl stopped gambling. Transcript at 72.

14. Mr. Grundahl worked as an auditor for a number of hotels after he was graduated from college. Transcript at 49.

15. Mr. Grundahl's record keeping was limited to two small notepads based on weekly tallies of purported wins or losses. The notepads of his winnings and

losses for 2004 and 2006 do not record the types of wagers made or games played on any particular date. The amounts written in the notepads are typically in $5 or $10 denominations. Exhibits A and B.

16. The Petitioners listed Mr. Grundahl as a "professional gambler" on their 2004 Schedule C. Exhibit 5.

17. The Petitioners did not keep or submit any receipts or casino player's club records or receipts. Exhibit 10 and Transcript at 56.

18. Mr. Grundahl took courses in accounting after he finished college. Transcript at 46.

19. The following description appears in the Lund book the Petitioners submitted into evidence:

> The machine must enter a state or condition different from the previous state or condition in that the expected profits from slot play are on average more valuable than the credits being expended during the slot play.
>
> This condition is generally accomplished through a system called banking. In banking as it relates to slot machines, credits, symbols, or some privilege is held in abeyance as a reward or bonus for continued slot play and this may be based on the previous play. The bonus is then awarded when a certain semi-difficult feat is accomplished on the slot machine.
>
> As described above, banking is a technique that has been developed by slot manufacturers to encourage slot players to remain at a particular machine and continue to play. It was well known that many slot players often left a machine when they had lost a certain amount, e.g. the twenty dollar bill initially inserted. Studies showed that banking often encouraged some of these losing players to insert additional funds and remain at the slot machine. In the course of a

> year, inducing additional play among only a fraction of the vast numbers of players could generate substantial additional gaming revenues.
>
> * * *
>
> Now, it often happens that a player on a banking machine will leave while the machine is in a state of increased value and advantageous to continue playing. This departure may be based on ignorance, or some pressing engagement, or possibly a lack of funds to continue playing, or any number of obscure reasons. But when this does occur, any person who recognizes the potential value of the machine can begin advantageously playing that very machine with the proper strategy.
>
> A player will generally be better off financially if, instead of playing various slot machines in the hope of being lucky, he spends his time walking through the casino looking for a machine that has been vacated while in an advantageous condition.[3]

Exhibit K.

20. The Petitioners filed a Wisconsin income tax return for each of the years at issue with an attached copy of their Form 1040 U.S. Individual Income Tax Return for each respective year. Exhibit 5.

*21.* On line 1 of their 2004 Schedule C for 2004, the Petitioners reported receipts from gambling in the amount of $61,368. The Petitioners subtracted $4,680 for vehicle expenses and $44,208 for the cost of wagers, reporting a net profit on line 31 of $12,480. *Id.*

[3] Charles W. Lund, *Robbing the One-Armed Bandits: Finding and Exploiting Advantageous Slot Machines* (RGE Publishing, 1st edition, 1999). The introduction to the book states that Mr. Lund has a Ph.D. in statistics.

22. The Petitioners' Federal gross income as reported on line 1 of their 2004 Wisconsin Income Tax return was $13,535. On line 3, the Petitioners reported a capital gain of $2,500. On line 13, the Petitioners declared $16,035 as their total Wisconsin income. The Petitioners claimed 2 exemptions for themselves and 5 deductions for their children. On line 52, the Petitioners reported that they owed no Wisconsin income tax for 2004. *Id.*

23. On their 2005 Schedule C, the Petitioners listed "Internet Sales (collectibles)" as their principal business or profession. The Petitioners listed their Wisconsin income on line 13 as a loss of $6,148 and paid no income tax for that year. Exhibit 6.

24. On their 2006 Wisconsin income tax return, the Petitioners listed $16,378 as their Wisconsin income on line 13. The Petitioners attached two Schedule Cs, one listing "Internet sales" as a business or profession and the other leaving the box blank. The latter form reported a gross income on line 7 of $26,396.50. In part V, the Petitioners claimed $15,973.50 as the cost of wagers. The Petitioners reported on line 31 a net profit of $9,423. On line 50 of their Wisconsin income tax return, the Petitioners requested a refund of $1,944 for 2006. Exhibit 7.

25. Mr. Grundahl started going to the casino in 2003 after someone told him about this opportunity. Mr. Grundahl noticed that he was making money playing the machines in 2003, but he kept no records. That same year, Mr. Grundahl decided to pursue gambling full time going into 2004. Transcript at 25.

## DECISION

The Petitioners[4] in this case report winning $61,368 at a casino in Wisconsin Dells in 2004 and $26,396 at that same casino in 2006. These amounts included jackpots of $57,735 on July 11, 2004 and $14,941 on May 4, 2006.[5] For income tax purposes, the Petitioners seek to net out their alleged expenditures against those winnings, meaning that they would pay nothing to the State in income tax for 2004 and 2006. In order to net their losses against their winnings, however, the Petitioners must show that Mr. Grundahl was a professional gambler, as Wisconsin does not allow recreational gamblers to deduct their losses from their winnings. First, we will summarize the applicable law. Next, we will discuss why Mr. Grundahl meets the applicable tests for determining status as a professional. Last, we will show how the Petitioners have failed to substantiate their alleged losses and expenses.

### A. APPLICABLE LAW

This case is about whether or not Mr. Grundahl can prove that for the two years in question he was a professional gambler and, if so, whether he can substantiate his claimed losses and expenses. The first two parts of this section will discuss the burdens of proof and statutes associated with this case. The third part will apply the test used by the United States Supreme Court to determine if someone is a professional gambler. The next section will summarize the Commission's recent case law on gambling.

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[4] The evidence presented in this case was that only Mr. Grundahl gambled.

[5] Casinos issue W-2s to taxpayers for winnings over certain dollar amounts. Mr. Grundahl testified that almost all of the W-2s in this case relate to video poker. Transcript at 60.

### 1. Burdens of Proof

Assessments made by the Department are presumed to be correct, and the burden is upon the Petitioners to prove by clear and satisfactory evidence in what respects the Department erred in its determination. *Edwin J. Puissant, Jr. v. Dep't of Revenue,* Wis. Tax Rptr. (CCH) ¶202-401 (WTAC 1984). Tax exemptions, deductions, and privileges are matters of legislative grace and will be strictly construed against the taxpayer. *Hall Chevrolet Co., Inc. v. Dep't of Revenue*, 81 Wis. 2d 477, 484, 260 N.W.2d 706 (1978). Petitioners thus have the burden of establishing that the Department erred in rejecting Petitioners' characterization of their gambling activities as a trade or business and, thereby, denying their deductions for gambling losses. Whether a taxpayer engages in an activity with the primary purpose of making a profit is a question of fact to be resolved based on all of the facts and circumstances in a particular case. *John F. and Esther K. Chow v. Commissioner*, T.C. Memo 2010-48.

### 2. Applicable Statutes

For income tax purposes, Wisconsin generally follows federal law. *Donna Ring v. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶401-130 (WTAC 2008). Income derived from wagering transactions or gambling is includible in gross income under provisions of Section 61 of the Internal Revenue Code. I.R.C. § 165(d) provides that losses from gambling shall be allowed only to the extent of the gains from such transactions.

On the federal level, gambling winnings and losses are reported on Form 1040 in one of two ways. If the taxpayer is engaged in the business of gambling, the taxpayer files Schedule C with Form 1040 and reports the business income or loss from

gambling on line 12 of Form 1040. If the taxpayer is not a professional gambler, the taxpayer reports gambling winnings on line 21 of Form 1040 and files Schedule A with Form 1040 in order to itemize deductions attributable to gambling losses to the extent of gambling winnings.

Prior to the year 2000, Wisconsin's itemized deduction credit allowed taxpayers to add the amounts allowed as itemized deductions under the Internal Revenue Code (I.R.C.), with certain exceptions, in calculating the itemized deduction credit. *See* Wis. Stat. § 71.07(5) (1987-88)-(1997-98). Miscellaneous itemized deductions, including gambling losses, were allowed under I.R.C. § 165(d), and they were not one of the exceptions delineated under § 71.07(5). In other words, Wisconsin taxpayers were allowed to deduct gambling losses from their income as an itemized deduction credit at that time.

However, effective January 1, 2000, the Wisconsin legislature chose to except from its itemized deduction credit the miscellaneous itemized deductions that a taxpayer may claim under the I.R.C. *See* Laws of Wisconsin 1999, Act 9, § 1711. Thus, gambling losses, which are allowed as a federal miscellaneous itemized deduction, are no longer allowed in computing the Wisconsin itemized deduction credit. *See Calaway v. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶400-856 (WTAC 2005). The only way gambling losses can be deducted from gambling winnings in Wisconsin is if the taxpayer is engaged in the trade or business of gambling.

Section 162 of the Internal Revenue Code (I.R.C.) allows deductions for "all the ordinary and necessary expenses paid or incurred during the taxable year in

carrying on any trade or business." The I.R.C. does not define trade or business for purposes of Section 162. However, as discussed below, the United States Supreme Court has provided some guidance. "[I]f one's gambling activity is pursued full time, in good faith, and with regularity, to the production of income for a livelihood, and is not a mere hobby, it is a trade or business." *Commissioner v. Groetzinger*, 480 U.S. 23, 35 (1987). "[T]o be engaged in a trade or business, the taxpayer must be involved in the activity with continuity and regularity and[] the taxpayer's primary purpose for engaging in the activity must be for income or profit." *Id*. An activity that is sporadic, a mere hobby, or an amusement diversion does not qualify. *Id.*

**3. The U. S. Supreme Court's Decision in *Groetzinger***

*Groetzinger* is the leading case in this area and in this section we will describe the relevant facts.[6] In *Groetzinger*, the United States Supreme Court determined in a case involving the alternative minimum tax that Mr. Groetzinger was a professional gambler in pari-mutuel wagering, primarily on greyhound races. Mr. Groetzinger spent 48 weeks gambling during the year at issue.[7] *Groetzinger*, 480 U.S. at 24. He "spent a substantial amount of time studying racing forms, programs, and other materials" and "devoted from 60 to 80 hours each week to these gambling-related endeavors." *Id*. Mr. Groetzinger "kept a detailed accounting of his wagers and every day noted his winnings and losses in a record book." *Id*. at 25. In holding that Mr. Groetzinger was engaged in the trade or business of gambling, the Court noted

[6] It does not appear that the U.S. Supreme Court has decided another case involving gambling since *Groetzinger*. No appellate court in Wisconsin has cited to *Groetzinger.*

[7] There was no testimony in this case concerning vacations or off days.

"[c]onstant and large-scale effort on his part was made. Skill was required and was applied." *Id*. at 36.

For several reasons, we believe the Petitioners here meet the *Groetzinger* test. First, the time commitment was substantial. The testimony at the trial was that Mr. Grundahl went to the casino 6 days a week, for a period of between 48 and 60 hours.[8] The Department concedes this, but points out that some of the period had to be recreational. There is no direct support for that in the record, however, and self-serving though it may be, Mr. Grundahl testified at his deposition that he "despised slots."[9] Second, skill was applied, although at a low level. According to the Lund book, a slot player could choose a machine that was operating in a mode (the "advantageous mode") that would give a player higher odds of winning. Thus, the primary skill involved here was choosing a machine that was in the advantageous mode, which one would do by looking at a row of lights at or near the top of the machine.[10] The Respondent did not present evidence directly contradicting the claims made in the Lund book on this point, so the Petitioners' evidence on this point remains uncontroverted. Finally, Mr. Grundahl did at some level prepare himself for this work by reading or studying, although not nearly at the level Mr. Groetzinger did.

We must acknowledge, however, there is a split among various

[8] A taxpayer who spent just 35 hours a week at a horse track after losing his job as a salesman and who was seeking a new sales job qualified as a professional gambler for purposes of section 162. *Rusnak v. Commissioner*, T.C. Memo. 1987-249.

[9] The deposition transcript was marked and received into evidence at the trial.

[10] This is important because it is generally accepted that a slot machine player cannot reasonably expect to profit over time. *Orr*.

jurisdictions over whether slot playing can constitute a trade or business. A number of cases hold, or assume, that it can. For example, in *Hoyt M. and Helen J. Orr v. Commissioner,* T.C. Summary Opinion 2010-55 (Apr. 26, 2010) Mrs. Orr won a jackpot of $1.2 million dollars at a casino as a recreational gambler and then decided to try to make a living gambling when she had trouble trying to find a job. When she realized she could not make a living at blackjack or poker, she then focused on slot machines. In the context of the Section 165(d) limitation, the U.S. Tax Court in a summary opinion stated "To hold that playing a slot machine is not gambling would be an absurd interpretation of the word 'wagering'." Also, in the *Chow* case cited above, Ms. Chow and her husband, Dr. Chow, operated a medical practice. After Dr. Chow underwent surgery in 2003, Ms. Chow began playing slot machines extensively, gambling on 124 days in 2004 and 176 days in 2005. In all, she had gambling winnings of $283,072 and gambling losses of $339,832 in 2004. In 2005, she had gambling winnings of $1,079,292 and gambling losses of $1,232,005. The I.R.S. calculated the losses using a "session-based analysis", i.e., by netting wins and losses per slot machine session, but regardless of the methodology used, the losses exceeded the winnings in each year. While acknowledging that there seem to be no recognizable standards for a businesslike approach to slot machine gambling, the U.S. Tax Court found that a preponderance of the evidence favored Ms. Chow's claim that during 2004 and 2005 she pursued slot playing with a profit objective.[11] Finally, in *Estelle Busch v. Comm'r of Revenue*, Minn.

[11] The Tax Court did point out that under Treas. Reg. § 1.183-2(a) the expectation of profit is subjective and need not be reasonable. The Tax Court also wrote in the body of its opinion that based on the record before it that the Petitioners "would be prudent to abandon gambling as a potential source of income."

Tax Rptr. (CCH) ¶ 203-214, 713 N.W.2d 337 (Minn. 2006), the Supreme Court of Minnesota reversed the Minnesota Tax Court in an alternative minimum tax case, holding that the taxpayer's slot machine gambling did, in fact, constitute a trade or business. In *Busch*, the Minnesota Tax Court had found that the taxpayer considered playing slot machines to be her job and that she spent from 40 to 60 hours per week at a casino for over a two-year period.[12] Upon reaching 65 years of age in 1999, Ms. Busch quit her prior occupations, which had included being a teacher, a police dispatcher, and a landlord.

On the other hand, there are recent decisions of the Commission that will be discussed below which support the position that slot playing cannot be a trade or business. Clearly, the absence of skill is problematic and that has led to findings that slot playing cannot be a trade or business, as the taxpayer has essentially no chance of making a profit over time. About the issue of skill, the *Busch* court wrote the following:

> A Professional Gambler is one who has attained a certain level of skill in a gaming activity whereby he or she makes their living off of the net winnings in the business. Professional gamblers exist only in activities where skill is a factor in winning, not only the luck of the game. Such activities include black jack, poker (where legal),[13] and thoroughbred horse racing. On the other hand, games such as bingo, pull-tabs, scratch-offs and slot machines are simply games of chance with no skill factor to provide higher odds

[12] In *Busch*, the IRS had previously determined that the taxpayer's gambling constituted a trade or business. The facts of the case were essentially undisputed and one of the findings of the trial court was that Ms. Busch chose slot machines as a method of gambling because "it didn't take a great deal of knowledge to play a slot machine."

[13] Video poker allows a gambler to choose which digital cards to hold and which to discard, receiving new cards in return. Kurt Eggert, *Truth in Gaming: Toward Consumer Protection in the Gambling Industry,* 63 Md. L. Rev. 217 (2004).

of winning.

The Wisconsin appellate courts have considered issues related to the definition of gambling in the context of Chapter 945 of the Wisconsin Statutes. For example, in *State v. Hahn,* 203 Wis. 2d 450, 553 N.W.2d 292 (Ct. App. 1996), the defendant was prosecuted under Wis. Stat. § 945.03(5) after he collected proceeds from video poker machines, which he had placed in three Jefferson County taverns. *Id.* at 452, 553 N.W.2d 292. The issue presented to the court of appeals was whether Hahn's video poker machines were "gambling machines" under Wis. Stat. § 945.01(3). *Id.* at 454, 553 N.W.2d 292. The court held that a video poker machine is a "gambling machine" only if it affords a successful player an opportunity to obtain something of value, even if the machine itself does not award the prize. *Id.* at 457-458, 553 N.W.2d 292. Unfortunately, *Hahn* and the other cases under Wis. Stat. § 945 provide little or no guidance here.

This case is distinguishable from all of those cases, however, because the testimony in this case established that Mr. Grundahl had a particular method of picking and playing the machines. That testimony concerning the advantageous mode was supported by the Lund book, which is quoted above in the statement of facts, and by other authorities.[14] For example, the following passage appears in a book written by columnist John Grochowski:

> On some bonus games, any player can gain an edge if he knows what he's seeking. What he's seeking are bonuses that are banked---that is, the bonuses build in increments, and just how far the machine has gone toward the next

[14] *See id* at 271. ("Some slot machines have countdown systems, which notify players that they must play a certain number of coins to receive a point good toward the redemption of "comps," and thus encourage players to stay at the slot machine until they have received enough points.").

> bonus determines whether the situation is profitable.
>
> Look for individual machines that players have left with those bonuses partly completed. With a head start to the bonus, you can get there without the investment it would take if you started from scratch.
>
> Why do casinos and manufacturers offer banked bonuses if they can offer players an edge? Because players like them. They like to see they're making progress toward an extra payoff. Banked bonuses keep players in their seats---they'll try a few extra spins to try to get the bonus.
>
> The casino doesn't really lose any money off banked bonuses. The bonuses are going to be paid; they're a normal part of play. The question is who's going to get them. And the answer is that a large share of bonuses are going to go to players who know to watch for them.
>
> Having the edge does not insure that you're going to come out ahead in any one session. There are no guarantees at any game of chance. You're still bucking the normal house edge on the reel spins, and as we know, the player can have losing streaks on any slot machine. In the long run, the right bonus situations will outweigh the house edge on the basic game.

John Grochowski, *The Slot Machine Answer Book* 115 (Bonus Books 1999). This case, unlike *Calaway*, lacked expert testimony or exhibits to disprove that there is a skill involved here. Thus, we see no *per se* bar here such that this type of slot playing cannot be a trade or business.

**4. The Regulations**

Guidance for determining whether an activity is engaged in for profit is provided in Treasury Regulations § 1.183-2. Consistent with other cases using the *Groetzinger* standard, we analyze Mr. Grundahl's gambling activities with regard to the

regulations promulgated under Section 183 to identify activities not engaged in for profit.[15] *See, e.g., Hastings v. Commissioner*, T.C. Memo 2009-69; *Merkin v. Commissioner*, T.C. Memo 2008-146. Deductions are not allowable under § 162 for activities which are "carried on primarily as a sport, hobby or for recreation." Treas. Reg. § 1.183-2(a). "The determination whether an activity is engaged in for profit is to be made by reference to objective standards, taking into account all of the facts and circumstances of each case." *Id*. Although a reasonable expectation of a profit is not required, the taxpayer's profit objective must be actual and honest. *Dreicer v. Commissioner,* 665 F.2d 1292 (D.C. Cir. 1981); sec. 1.183-2(a), Income Tax Regs. Whether a taxpayer has an actual and honest profit objective is a question of fact to be answered from all of the relevant facts and circumstances. *Hastings v. Commissioner,* T.C. Memo. 2002-310; sec. 1.183-2(a), Income Tax Regs. Further, "[i]n determining whether an activity is engaged in for profit, greater weight is given to objective facts than to the taxpayer's mere statement of his intent." *Id*. The regulation states specifically as follows:

> **b) Relevant factors.** In determining whether an activity is engaged in for profit, all facts and circumstances with respect to the activity are to be taken into account. No one factor is determinative in making this determination. In addition, it is not intended that only the factors described in this paragraph are to be taken into account in making the determination, or that a determination is to be made on the basis that the number of factors (whether or not listed in this paragraph) indicating a lack of profit objective exceeds the number of factors indicating a profit objective, or vice versa...

[15] Treas. Reg. § 1.183-2 dates back to at least 1972, but never mentions gambling. The *Groetzinger* court never references Treas. Reg. § 1.183-2.

Treasury Regulations § 1.183-2(b) goes on to provide a non-exhaustive list of factors to consider when determining whether an activity is engaged in for profit: (1) the manner in which the taxpayer carries on the activity; (2) the expertise of the taxpayer or his advisors; (3) the time and effort expended by the taxpayer in carrying on the activity; (4) the expectation that assets used in the activity may appreciate in value; (5) the success of the taxpayer in carrying on other similar or dissimilar activities; (6) the taxpayer's history of income or losses with respect to the activity; (7) the amount of occasional profits, if any, which are earned; (8) the financial status of the taxpayer; and (9) elements of personal pleasure or recreation.

**5. Commission Cases That Apply the Regulation**

The Commission has applied the regulation on three recent occasions since the law change in 2000 and we will explain each case in detail to provide context to our decision here. In brief, Wisconsin taxpayers have had a more difficult time proving they are professional gamblers than taxpayers in the federal system. For example, in *Calaway v. Dep't of Revenue,* Wis. Tax Rptr. (CCH)¶400-856 (WTAC 2005), the taxpayer in 1996 won $3,794,525 in casinos in Las Vegas, Atlantic City, and Green Bay and had losses of $3,7069,925. In 1996, Mr. Calaway played about 40 percent slot machines, and the remaining 60 percent was split evenly between roulette and blackjack. Mr. Calaway testified that between 1993 and 1997, when he was not gambling in other states, he gambled at the Oneida Casino in Green Bay five to six times per week, three to ten hours a day. Mr. Calaway's bankruptcy petition listed loans to seven separate family members totaling more than $1.2 million dollars. In a

criminal complaint filed in Nevada in 1999, Mr. Calaway was charged with 22 counts of drawing and passing without sufficient funds, with checks ranging in amount from $10,000 to $75,000.

One of the issues in the case, like here, was substantiation. Mr. Calaway did not have records for the hands of blackjack he played in Las Vegas, and he had no records of his roulette playing. He did, however, have a player's card from some of the out-of-state casinos which tracked how much coin went in and out of a slot machine for player's club privileges.[16] The card could also be presented at the tables to track table play. Mr. Calaway testified that for some of the years at issue, he called the out-of-state casinos where he gambled the vast majority of the money, and requested "year-end information." Mr. Calaway also substantiated his gambling activities at Oneida by submitting a letter from an Oneida table games shift supervisor and the letter stated that the supervisor had observed Mr. Calaway playing blackjack approximately four to five times per week and that Mr. Calaway used the basic strategy rules of Blackjack to his advantage while he played.

Applying Treas. Reg § 1.183-2(b), the Commission had the following to say about the manner in which Mr. Calaway carried on the business:

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[16] The web site for the Ho Chunk casino states the following about its player's club membership:

> You can earn slot points by inserting your Rewards Club Card into the reader box of your favorite slot machine. When you insert your Rewards Club Card the reader box will welcome you and display your name along with your point total. To ensure your points are accumulating be sure to keep your Rewards Club Card inserted until you are finished playing. To earn table game comps simply present your Rewards Club Card to the table game supervisor, comps will be earned based on your play.

*available at* http://www.ho-chunkgaming.com/wisconsindells/rewards.html (last visited on August 15, 2010).

> Petitioner did not carry on his gambling activities in a businesslike manner. Petitioner would have no records at all if it were not for the casinos tracking him, either through their IRS reporting requirements, which do not require them to report all winnings, or through petitioner's use of his player's cards, which petitioner did not always use. The W-2G's generated in these cases are only for petitioner's slot machine play. Moreover, petitioner had no records at all from Oneida, where he stated he gambled five to six times per week and three to ten hours per day when he was not at casinos in other states. Thus, he has no records to substantiate either his winnings or amounts spent at one of the locations where he claims to have conducted a substantial portion of his time gambling. Similarly, petitioner admitted that he did not keep track of every hand played at the casinos, or even record his overall winnings and losses at any time, much less on a regular and consistent basis.

As to Mr. Calaway's specific activities, the Commission wrote the following:

> Nor were the specific gambling activities petitioner engaged in conducted in a businesslike manner. Slot machines -- which petitioner testified constituted 10 percent of his gambling activities in 1994, 35 percent in 1995, and 40 percent in 1996 -- involved no skill other than pressing a button. Regarding blackjack -- which petitioner testified constituted 90 percent of his gambling activities in 1994, 60 percent in 1995, and 30 percent in 1996 -- petitioner did not present any evidence that he engaged in any strategies to maximize or even earn a profit. Rather, he stated only that he played basic strategy and did not count cards, which Dr. Hannum[17] testified would produce a negative value in the long run, even if petitioner had played under a perfect application of basic blackjack strategy. With respect to roulette -- which petitioner played only a little in 1995 and 30 percent of the time he gambled in 1996 -- petitioner's only strategy was to bet on a block of eight numbers covering one-fourth of the wheel. He presented no evidence that such an approach was sound, successful or based on research or

[17] Footnote 2 in the *Calaway* decision states that Dr. Hannum is an expert in gambling and a professor of statistics and computer science at the University of Denver.

> other reliable information. Dr. Hannum testified that, from a mathematical perspective, petitioner's method of roulette play would produce a negative return over the long run.
>
> Petitioner's funding for his gambling activities was likewise not conducted in a businesslike manner. After spending his own money, he proceeded to spend money lent to him primarily by family members, for which no promissory note, interest or payment plan was generated. Petitioner did not keep a separate bank account for his gambling activities.
>
> In fact, Petitioner has not demonstrated that any aspect of his gambling activities was conducted in a businesslike manner.

The Commission after reviewing all of the evidence held as follows:

> On balance, application of the nine factors set forth in Treas. Reg. 1.183-2(b) undermines petitioner's argument that he was a professional gambler. Petitioner emphasizes his investment of time in gambling. This is not surprising, as it is one of the few factors arguably operating in his favor. However, that factor is somewhat ambiguous due to the unique character of gambling and the aspects of petitioner's behavior that suggest he had a gambling problem. Even if the time factor were free from ambiguity, however, it does not outweigh the other factors which show that petitioner was not conducting his gambling activities in a businesslike manner or in a way that would support his subjective hope of earning a profit.

In sum, the decision in *Calaway* shows several things that are relevant here. First, a taxpayer's burden to document his or her gambling is substantial. Second, the time commitment element is less significant where problem gambling is present. Third, a true business plan is needed.

The Commission next applied Treas. Reg. § 1.183-2 in *Merlin and Ali Voss v. Dep't of Revenue,* Wis. Tax Rptr. (CCH)¶401-028 (WTAC 2007). In the *Voss* case, the

taxpayers sought treatment as professional gamblers. Merlin Voss had retired in 1985 and during the relevant period, the Vosses played only slot machines. The Vosses played during all times of the day and every day of the week because of Ali's flexible work schedule. The Vosses entered wins, losses and time expended on gambling activities on Ali's computer on a daily basis. The Vosses calculated their losses from gambling activities by counting cash they started with, with additions and winnings, and cash they ended with. The Vosses did not count ATM charges, check cashing charges or interest paid on credit card accounts in the calculation of winnings and losses. The Vosses had engaged in gambling as a recreational activity in years prior to the year under review. The Vosses had several sources of income during the year under review and did not intend to support themselves solely from their gambling activities. For each year the Vosses reported gambling activities (1997, 1998, 1999 and 2000), the winnings reported were the same as or less than the losses reported, netting out to zero. The Vosses traveled from their home in Verona to the casino at Baraboo and several others. The Vosses used checks, Automatic Teller Machines, credit cards and casino cashiers to obtain cash for gambling.

The Vosses' "business plan" was to go into debt so that they could obtain funds to turn a profit from gambling. The "business plan" was not in any written form. The Vosses were going to gain expertise in the field by reading trade journals, watching videos and television to learn the intricacies of playing slots. The Vosses mixed gambling and non-gambling expenditures in their checking accounts and credit card accounts. The Vosses obtained the monies to pursue their gambling activities from

refinancing their house and obtaining cash advances from credit cards. The Vosses participated in slot machine tournaments at casinos and on cruises.

The Commission held that the Taxpayers in *Voss* failed to present clear and satisfactory evidence that the Department erred in rejecting Voss' characterization of their gambling losses as business losses. The Commission wrote as follows:

> Petitioners carried on their gambling activities in a minimally businesslike manner, at best. They did keep track of where, when and for how long they played slot machines during the year. They also kept track of the total wins and losses for both Ali and Merlin on each day they played the slot machines. However, this is the extent of their record keeping.
>
> It does not appear that petitioners kept business records that could accurately show their net income from gambling activities. They failed to keep track of any expenses directly related to gambling (other than losses), such as travel expenses, interest from loans and finance charges for credit card balance carryovers and cash advances for gambling. Moreover, they did not keep separate bank accounts for gambling activities for record keeping purposes. Instead, they commingled their gambling funds with their personal funds.
>
> Petitioners did not withdraw from any other occupation in order to pursue gambling. Ali continued her occupation during the year under review and Merlin had been retired for several years and was receiving social security benefits.
>
> In petitioners' favor, however, the record reflects that they spent a great deal of time playing slot machines. Undoubtedly, devotion of a substantial amount of time makes it more likely that one is engaged in the trade or business of gambling than it would be if such a time commitment were absent. However, while petitioners appear to have devoted a great deal of time to gambling there is no evidence indicating that they expended much

> effort towards improving their skills at or results from gambling, as noted above.
>
> Petitioners did win $4,080 more than they lost playing slot machines during the year under review. This is a profit over the losses and this would be a factor in favor of showing that petitioners were engaged in the business of gambling.
>
> However, this profit does not necessarily show petitioners' net income from gambling activities during the year under review. Petitioners never took into account any expenses directly relating to their gambling activities (other than losses) such as service charges for loans and cash advances (even though it was their plan to borrow money to finance the gambling activities) or mileage (even though all gambling activities involved some traveling expenses.)

Several lessons emerge from the Commission's decision in *Voss.* First, a profit in a particular year does not guarantee trade or business status. Second, lack of detail in records can be fatal to a claim of being a professional. Third, strong recreational components can negate trade or business status. Finally, it is difficult, if not impossible, to be a professional gambler playing traditional slots.[18]

The Commission last considered Treas. Reg. § 1.183-2 in *Donna Ring v. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶401-130 (WTAC 2008). In that case, a taxpayer challenging a Wisconsin personal income tax assessment failed to establish that the

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[18] One writer said the following about slots players:

> Slot machine players account for a distressing percentage of problem gamblers. Studies estimate that up to 70% of treatment-seeking pathological gamblers identify electronic gaming machines as their primary, if not exclusive, problem form of gambling. Worse yet, slot machine players are among the fastest to 'bottom out' and reach the depths of full problem or pathological gambling. One study indicated that the onset of pathological gambling occurred in a third of the time, on average, for machine gamblers compared to traditional gamblers.

Eggert, *supra* note 10 at 227.

Department of Revenue erred in disallowing gambling losses that she claimed on Schedule C of her federal income tax return. The Commission's review of the relevant factors indicated that the taxpayer was not a professional gambler and did not conduct her gambling activities in a way that suggested she was engaged in a trade or business. Further, the taxpayer had previously conceded to an IRS determination that her gambling was not a trade or business during one of the years at issue.[19] On her Schedule C's for each of the three years at issue, Ms. Ring reported receipts from gambling that matched the cost of goods sold, resulting in a reported zero net profit.

Like Mr. Grundahl, Ms. Ring gambled at the Ho-Chunk Casino in the Wisconsin Dells. The taxpayer testified that she maintained a diary showing her gains and losses from gambling for 2001 and 2002, and she submitted a copy of the diary to the Department and the Commission. Ms. Ring testified that she maintained a diary showing her gains and losses from gambling for 2003, but was unable to locate a copy of that diary. Ms. Ring testified that she prepared the diary of her 2001 and 2002 gambling gains and losses contemporaneously with her activities during that period, and that she provided the diary to her accountant to help prepare her tax returns for those years. Ms. Ring's diary for 2001 and 2002 provides a record of her total daily gambling gains and losses, but does not identify her specific gains and losses from slot machines and blackjack. During the Department's audit, the Department's auditor concluded that Ms. Ring's diary of her gambling gains and losses during 2001-2002 did

[19] The amount was small and the taxpayer wrote a note stating that because of the small amount, she would not contest the finding.

not appear to have been prepared contemporaneously, but rather appeared just to list cash withdrawals from bank accounts and credit card charges. Ms. Ring testified that she did not maintain a separate account for her gambling activities. Ms. Ring testified that she funded her gambling activities with the proceeds from settlements in two lawsuits and credit card charges during the period at issue. Ms. Ring testified that she also played the lottery, but did not maintain any records of her lottery winnings and losses.

To improve her profits from gambling, the Ms. Ring testified that she would change her gambling methods by going to the casino at different times of the day, playing different slot machines, varying her bets, and sometimes playing blackjack before the slot machines. Ms. Ring's efforts to improve her skills at blackjack consisted of learning from dealers and other players, playing computer-based gambling games at home and reading unnamed books and magazines on gambling, which she stated she no longer had in her possession. Mr. Ring stated that she attempted to learn how to count cards while playing blackjack, but did not state that she was successful. Ms. Ring testified that she played in two or three blackjack tournaments during the period at issue, but did not win any money. Ms. Ring testified that she gambled as a way to deal with stress in her life during at least part of 2001, which was caused by the deaths of loved ones. Regarding her reasons for gambling, Ms. Ring testified: "It was like an escape from reality for a while. It was a place where I had been before where I had made some money and I knew all the people at the casino. I knew the staff. They were helpful to me."

The Commission wrote as follows:

> Petitioner did not carry on her gambling activities in a businesslike manner. Petitioner's records are at best incomplete, and her 2001-2002 diary of gains and losses does not show petitioner's wagers or the different games played on any particular date.
>
> Nor were the specific gambling activities petitioner engaged in conducted in a businesslike manner. Slot machines, which petitioner testified constituted a significant portion of her gambling activities during the period in question, require no skill to play. The Commission has previously held that, as a matter of law, gambling in the form of playing slot machines cannot constitute a trade or business. *Calaway, supra.* Petitioner's other main gambling activity involved playing blackjack, but petitioner presented no evidence showing that she engaged in strategies to maximize or earn a profit.
>
> The statements included in petitioner's petition for redetermination and her testimony support a different interpretation of her gambling activities. That document refers to petitioner's "gambling problem" which resulted in her filing for bankruptcy in 2002. Due to petitioner's financial situation, her daughter became her "protective payee." Petitioner testified that gambling provided her with a form of escape from her problems. These statements suggest that petitioner suffered from a harmful addiction, not that she pursued gambling in a businesslike manner.

The Commission's decision in *Ring* shows two things. First, it shows that problem gambling is not a trade or business.[20] Second, the decision shows the importance of detailed, contemporaneous records.

### B. Applying the regulation here

#### 1. The Petitioners' arguments

In their post-hearing brief, the Petitioners argue that they have provided the Commission at the trial with concrete evidence that playing Video Poker and Bonus Slot Machines was what Mr. Grundahl did as a business for the years 2004 and 2006. In support of this argument, the Petitioners state that they have exact records of profits and losses on the machines and the numbers of the machines played. In the Petitioners' view, this business was based only on profit and loss and no other record-keeping was necessary. As he worked the same hours, it would have been redundant to write down the hours every day in a journal. The Petitioners also deny Mr. Grundahl was a

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[20]The following quote appeared in the Maryland Law Review:

> As more states have legalized more forms of gambling, the amount of problem and pathological gambling appears also to have increased. The number of people who gamble excessively is, of course, difficult to measure precisely, especially given disagreement over what constitutes excessive gambling. Essential elements of problem gambling are the difficulty in resisting gambling and the damage caused by gambling on the lives of gamblers, including their jobs, family, or personal lives. Pathological gambling is a step beyond problem gambling. Pathological gambling is classified by the American Psychiatric Association as "an impulse control disorder" and it "describes 10 criteria to guide diagnoses, ranging from 'repeated unsuccessful efforts to control, cut back, or stop gambling' to committing 'illegal acts such as forgery, fraud, theft or embezzlement' to finance gambling." A recent meta-analysis of 120 studies of problem gambling rates concluded that about 3.85% of Americans will be problem gamblers during their lifetime, that 1.6% will be probable pathological gamblers during their lifetime, and that 2.8% are currently (past-year) problem gamblers while 1.14% are current (past-year) probable pathological gamblers.

Eggert, *supra* note 13, at 224.

recreational gambler, as he studied his trade through practice on computer software and he read publications. The Petitioners point out that when the machines Mr. Grundahl played were taken out of the casino in 2007, he immediately quit and he was not in the casino in 2008 or 2009.

In his rebuttal filing, the Petitioner points out that the Department produced no evidence at trial that Mr. Grundahl engaged in any other occupation during the relevant time period. In conclusion, the Petitioners assert that Mr. Grundahl was a full-time probability analyst[21] in 2004 and 2006 and, as such, his business losses are deductible against his business profits.

**2. The Respondent's Arguments**

The Department offers several arguments in support of its position. First, the Department posits that the Petitioners' slot machine business cannot constitute a trade or business, distinguishing this case from *Groetzinger*. Second, the Department alleges that the Petitioner's gambling does not meet the standards under Section 183 for a trade or business, in particular the nine factors listed in Reg. § 1.183-2(b). Specifically, the Department takes issue with the way the Petitioner carried on the activity in that slot machines cannot constitute a trade or business. The Department notes the Petitioner lacked expertise and the advice of advisors. While the Department concedes that the record reflects that the Petitioner likely spent a great deal of time gambling, the Department points out that the Petitioner did not keep daily records of hours worked.

[21] Mr. Grundahl has continually referred to himself as a "probability analyst," apparently to contrast his activities from that of a gambler, recreational or professional. We see little merit in this distinction for two reasons. First, we are bound to apply the same body of statutes and case law regardless of the preferred title. Second, the Petitioner has not been consistent in the use of the title.

Finally, the Department points out that the hours the Petitioner was at the casino are not consistent with a business purpose.

**3. The 9 Criteria in Treas. Reg. § 1.183-2(b).**

Our analysis of the evidence here is thus guided by the case law and Treas. Reg. § 1.183-2(b). We will go through each of the relevant factors below:

***(1) Manner in Which the Taxpayer Carries On the Activity***

Carrying on an activity in a businesslike manner, maintaining complete and accurate books and records, conducting the activity in a manner substantially similar to comparable businesses which are profitable, and making changes in operations to adopt new techniques or abandon unprofitable methods suggest that a taxpayer conducted an activity for profit. Treas. Reg. § 1.183-2(b)(1). Complicating this analysis is the fact that there seem to be no recognizable standards for a businesslike approach to slot machine gambling. *Chow*.

Two factors do support the Petitioners here. First, the Petitioners did attempt to keep track of how much cash Mr. Grundahl had remaining at the end of the week. However, this is virtually the extent of their record keeping, which we will discuss further below in connection with substantiation. Second, the Petitioners did deduct vehicle expenses on their Schedule C, but no other expenses. The factors that do not support the Petitioners here are the absence of a formal business plan and the lack of any attempts to emulate a successful similar business. In our view, the manner in which Mr. Grundahl performed this activity is a neutral factor in deciding whether he was a professional gambler.

### *(2) The Expertise of the Taxpayer or the Taxpayer's Advisors*

Preparation for the activity by extensive study of its accepted business, economic, and scientific practices, or consultation with those who are expert therein, may indicate that a taxpayer has a profit objective. Treas. Reg. § 1.183-2(b)(2). A taxpayer's failure to obtain expertise in the economics of an activity indicates that he or she lacks a profit objective. *Burger v. Commissioner*, 809 F. 2d 355, 359 (7th Cir. 1987).

In this case, the Petitioners learned of a method to make a profit playing these machines and followed up on that conversation by reading a book which verified the information they had received. At a certain low level, Mr. Grundahl gained expertise in playing one type of slot machine in one particular fashion.

As discussed above, there is something of a split on whether or not slot machines involve a skill generally. *See Calaway v. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶ 400-856 (WTAC 2005). The testimony in this case, however, indicates that Mr. Grundahl had a specific way to play slot machines which, in our view, makes this case unique. On a different factual record, this Commission noted that playing slots involves no skill other than pressing a button, but we do not view that as controlling here. The Petitioners have met their burden on this issue because the evidence they produced as to the skill involved went uncontroverted.

### *(3) Taxpayer's Time and Effort*

The fact that a taxpayer devotes much time and effort to an activity, particularly if the activity does not have substantial personal or recreational aspects, may indicate that he or she has a profit objective. Treas. Reg. § 1.183-2(b)(3). A

taxpayer's withdrawal from another occupation to devote most of his energies to the activity may also be evidence that the activity is engaged in for profit. *Id.*

In Petitioners' favor, the record reflects that Mr. Grundahl spent a great deal of time playing slot machines. Undoubtedly, devotion of a substantial amount of time makes it more likely that one is engaged in the trade or business of gambling than it would be if such a time commitment were absent. Clearly, under *Groetzinger*, this was no hobby or sporadic activity. Mr. Grundahl does not appear to have spent his time doing any other work, at least not in 2004. Further, at his deposition Mr. Grundahl contended that he despised playing slots and there is no evidence in this record that Mr. Grundahl was a problem gambler or that he gambled for recreation. When the favorable machines were removed, Mr. Grundahl stopped going to the casino. This factor works in the Petitioners' favor.

***(4) Expectation that Assets Used in the Activity Will Appreciate in Value***

This factor is inapplicable, as the Petitioners did not have assets which they used in the business, other than perhaps a book and a computer program.

***(5) Taxpayer's Success in Other Similar or Dissimilar Activities***

This factor is inapplicable since there is no evidence that the Petitioners have engaged in similar activities for profit in the past, other than the fact that the Mr. Grundahl alleged that he spent some period in the past betting on dogs.

### *(6) Taxpayer's History of Income or Losses*

A history of substantial losses may indicate that the taxpayer did not conduct the activity for profit. Treas. Reg. § 1.183-2(b)(6). In this case, however, the Petitioners made money each year. As the regulation states:

> A series of years in which net income was realized would of course be **strong evidence** that the activity is engaged in for profit.

*Id.* [emphasis added].

### *(7) Amount of Occasional Profits, If Any, Which Are Earned*

As mentioned above, the Petitioners made money all of the years Mr. Grundahl gambled.

### *(8) Financial Status of the Taxpayer*

The fact that the taxpayer does not have substantial income or capital from sources other than the activity may indicate that an activity is engaged in for profit. Conversely, substantial income from sources other than the activity, especially if the losses from the activity generate large tax benefits, may indicate that the taxpayer does not intend to conduct the activity for profit. Treas. Reg. § 1.183-2(b)(8).

While examination of the returns shows that the taxpayers here sold some stocks in 2004, there is nothing in the record which indicates that the Petitioners actually supported themselves during the three relevant years in any way other than gambling.[22]

[22] The evidence was that Mrs. Grundahl made a small amount of money working outside of the home as a church organist.

### *(9) Elements of Personal Pleasure*

The presence of recreational or personal motives in conducting an activity may indicate that the taxpayer is not conducting the activity for profit. Treas. Reg. § 1.183-2(b)(9). In this case, there is no evidence of a recreational motive on the part of the Petitioners.

In sum, our review of the nine factors leads us to the conclusion that Mr. Grundahl was a professional gambler in 2004 and 2006. The factors that weigh heavily in his favor are his study and preparation, the time that he put in at the casino and the profit that he made both of the relevant years. We also note the absence of a recreational motive and the fact that Mr. Grundahl was not a problem gambler.

## C. SUBSTANTIATION

Having determined that Mr. Grundahl's activities during 2004 and 2006 meet the *Groetzinger* test does not end our inquiry, however. As the Department points out, the taxpayer here also has the burden to substantiate his expenses and deductions. It is long-settled law that deductions are a matter of legislative grace. *Fall River Canning Co. v. Dep't of Taxation,* 3 Wis. 2d 632, 637, 89 N.W.2d 203 (1958). Based on the evidence received at trial, we hold that the taxpayers have not substantiated their claimed deductions.

There are numerous problems with the records introduced here. First, they are minimal, in that Mr. Grundahl allegedly made one tabulation by way of a handwritten notation in a 3'' x 5'' spiral notebook at the end of each week, and did not

record each wager or even the machines he played.[23] We are not ready to say each wager of $1 or $5 must be listed, but we are ready to say these records are inadequate. The records here do not even break down the numbers by what type of game Mr. Grundahl played, slot machines or video poker. Second, there is no corroboration for the amounts the Petitioners claim Mr. Grundahl spent on wagers.[24] As *Calaway, Voss,* and *Ring* show, it is possible to corroborate the cost of wagers by way of a player's card.[25] It may have even been possible to use a credit card or write checks in order to

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[23] There are occasional notations in the record tied to the serial numbers of various machines, but no detail linking wager amounts to the various machines.

[24] One observer wrote the following in 2004:

> Casinos have already begun to keep extensive information about their customers through the use of what are called "slots clubs." Slot clubs are the method by which casinos track the gambling of individual slots bettors and determine how much they play, win, and lose...
>
> Slot clubs, on the other hand, track players with less expense and intrusiveness and with more accuracy. Upon joining a slot club, a player is issued a plastic card which looks much like a credit card with a magnetic strip on the back. Slot machines have readers that are able to decode the information about the player contained on the magnetic strip. As soon as the player slides the slot club card into the slot machine's reader, the slot machine is able to record how much that particular player bet and the player's wins or losses.

Eggert, *supra* note 13, at 270.

[25] The U.S. Tax Court has considered a taxpayer's reliance on a player's club card statement as a record of winnings and losses on several occasions. *See Hardwick v. Commissioner,* T.C. Memo. 2007-359; *Lutz v. Commissioner,* T.C. Memo. 2002-89; *Merkin v. Commissioner*, T.C. Memo. 2008-146("Petitioners were misguided to assume that Dr. Merkin's Players Club card would keep a complete business record of his activities at a casino and that this record would absolve them of the duty to maintain business records. See sec. 6001. It is the taxpayer's duty, and not that of the casino, to maintain such records. Sec. 6001. In short, his lack of records and accountability for his activities illustrates to us that Dr. Merkin did not carry on his video poker playing in a businesslike manner.")

have some documentation.[26] One would have expected to see at least a separate bank account. While an individual taxpayer reserves the right to run his business as he sees fit, by adopting such a minimalist cash-based accounting system Mr. Grundahl ran the risk that this alleged system would be found unacceptable.[27] Third, as the Department points out, the numbers Mr. Grundahl puts forth are not internally consistent.[28] Fourth, it is doubtful that this system accurately reflected income in that no other expenses other than perhaps vehicle expenses were accounted for. In sum, the Petitioners have not proved their claimed deductions.

**CONCLUSION**

The evidence the Petitioners introduced at trial shows that in 2004 and 2006 Mr. Grundahl went to the casino six days a week, playing top box bonus slot machines and video poker. Each of the two years in question, Mr. Grundahl made

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[26] Mr. Grundahl's testimony as to the effort he put into this endeavor was credible. Mr. Grundahl's testimony, however, that he supported his spouse and their five children on his claimed income was not credible.

[27] The Seventh Circuit wrote the following in connection with a "trade v. hobby" case:

> Moreover, a taxpayer need not maintain a sophisticated cost accounting system. What a taxpayer should use is some cost accounting techniques that, "at a minimum, provide the entrepreneur with the information he [or she] requires to make informed business decisions. Without such a basis for decisions affecting the enterprise, the incidence of a profit in any period" would be wholly fortuitous, and losses would be expected. *Burger,* 50 T.C.M. (CCH) at 1271. *See also Feldman v. Commissioner,* 51 T.C.M. (CCH) 1412, 1416 (1986). Consequently, a taxpayer must show that he or she has instituted some methods for controlling expenses, and if losses are mounting, methods to control those losses.

*Burger v. Commissioner*, 809 F.2d 355, 359 (7th Cir. 1987).

[28] The Department argues persuasively in its brief that the alleged cost of wagers is essentially a made up number, as the weekly totals in the notepads would not have supplied the information. The Department also points out that even using this method, the Petitioners listed different figures on a Schedule C for "cost of wagers" and "other expenses." Respondent's Brief at 5.

money using his particular system and had no other occupations that supported his spouse and their five children. Unlike the Petitioners in *Calaway, Voss*, and *Ring*, Mr. Grundahl was neither a problem gambler nor is there any evidence he was a recreational gambler. When the casino replaced the advantageous machines in 2007, Mr. Grundahl quit gambling. His activities, therefore, meet the test in the Treas. Reg. § 1.183-2 for determining if one is engaged in a trade or business. The Petitioners, however, failed to keep adequate records and receipts to support their claimed deductions for the cost of wagers and, therefore, the Commission finds for the Department.

**ORDER**

Based on the evidence received at trial, the Department's action on the Petition for Redetermination is affirmed.

Dated at Madison, Wisconsin, this 25th day of August, 2010.

**WISCONSIN TAX APPEALS COMMISSION**

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David C. Swanson, Chairperson

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Roger W. Le Grand, Commissioner

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Thomas J. McAdams, Commissioner

ATTACHMENT: **"NOTICE OF APPEAL INFORMATION"**