

**Table of Contents**

<b>Class of Income</b> .....	<b>2</b>
<b>Gambling and Lottery</b> .....	<b>2</b>
Gambling and Lottery Defined for Pennsylvania Personal Income Tax.....	2
Prizes – Cash, Noncash and Mixed .....	2
Consideration.....	2
Gratuitous Prizes .....	2
Door Prizes .....	2
<b>Taxable Winnings</b> .....	<b>3</b>
In General.....	3
Residents .....	3
Nonresidents .....	3
Pass-through Entities .....	3
Multistate Lotteries .....	3
Sale or Assignment of a Lottery Annuity .....	3
<b>Costs and Other Expenses</b> .....	<b>4</b>
Costs .....	4
Other Expenses .....	4
<b>Reporting</b> .....	<b>4</b>
<b>Withholding on PA Lottery Payments</b> .....	<b>4</b>

**CLASS OF INCOME**

Gambling and lottery winnings is a separate class of income under Pennsylvania personal income tax law. See 72 PA C.S. §7303(a)(7). Between July 21, 1983 and Dec. 31, 2015, all prizes of the Pennsylvania Lottery were excluded from this class of income. As a result of Act 84 of 2016, cash prizes of the Pennsylvania Lottery that are paid on or after Jan. 1, 2016, are included in this class of income.

**GAMBLING AND LOTTERY****Gambling and Lottery Defined for Pennsylvania Personal Income Tax**

Lottery is a game comprised of three elements:

- A prize to be won;
- Consideration; and
- The determination of a prizewinner primarily by the drawing of lots and only secondarily by skill and experience.

Gambling means a contest comprised of three elements:

- A prize to be won;
- Consideration; and
- The determination of the prizewinner primarily by chance and only secondarily by skill and experience.

**Prizes – Cash, Noncash and Mixed**

Prizes include cash, property or any advantage or inequality in amount or value that is offered in a contest of chance or lottery and accrues, or is expected to be given, to some, but not all, of the participants in such competition or contest. It includes the right or permission to compete in another competition for a prize or to strive for a prize in another contest of chance or the right to a discount.

- **Cash Prize**

A cash prize includes any prize paid in cash or cash equivalent (e.g. check, money order, electronic funds transfer or deposit). A cash prize also includes an annuity in which the annuity payments are paid in cash or a cash equivalent.

- **Noncash Prize**

A noncash prize is any prize other than a cash prize. It includes real property and personal property (tangible and intangible). A gift card to a specific store is also considered a noncash prize.

- **Mixed Prize**

A “mixed prize” is one that consists of both cash and noncash prizes. In some instances, a mixed prize may include the noncash prize plus taxes or fees paid on behalf of the prize winner. Such taxes and fees are considered a cash prize and are subject to Pennsylvania personal income tax as applicable even if the noncash prize may be excluded from tax.

**Consideration**

Consideration in this context means any valuable advantage or benefit that the person conducting a competition, contest of chance or lottery expects to realize as a result of conducting such competition, contest of chance or lottery. The term, therefore, may include, but is not limited to, bets or wagers of cash or property, making a purchase, being present at a drawing, giving a testimonial for a product of the donor of the prize, filling in an application or contest blank, following any rules; or expending time or personal effort. *Commw. v. Lane*, 242 Pa. Super. 283, 363 A.2d 1271 (1976); *Commw. v. Lund*, 142 Pa. Super. 208, 15 A.2d 839 (1940); and *Commw. v. Laniewski*, 173 Pa. Super. 245, 98 A.2d 215 (1953);

**Gratuitous Prizes**

A plan or system for gratuitously distributing money or property by direct gift or by lot or chance does not constitute a lottery or gambling. Money or property distributed under such plans or systems are not taxable gambling or lottery winnings.

**Door Prizes**

Prizes that are given in a competition or contest are not taxable gambling or lottery winnings if no advantage or inequality in amount or value is offered or striven for by any of the participants.

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**TAXABLE WINNINGS****In General**

For Pennsylvania and federal income tax purposes, winnings or proceeds from wagering transactions are not taxable until, and to the extent all of the following five conditions are satisfied:

- The amount of the prize is due;
- The amount of the prize is appropriated on the books of the obligor;
- The obligor is willing to pay the amount of the prize;
- The obligor is solvent; and
- The prizewinner has knowledge of the foregoing facts; or
- The amount of the prize is unconditionally and irrevocably paid into a fund or trust to be used exclusively for the prizewinner's sole benefit; or
- The prize becomes the equivalent of cash in hand because the prize is transferable at a discount not substantially greater than the generally prevailing premium for the use of money; or
- The amount of the prize is actually paid to the prizewinner or the prizewinner's designee.

**Residents**

Pennsylvania taxes resident individuals, estates or trusts on all gambling and lottery winnings from every source, except noncash winnings of the Pennsylvania Lottery, regardless of where the wager is placed.

**Nonresidents**

Pennsylvania taxes nonresident individuals, estates or trusts on gambling and lottery winnings derived from sources within Pennsylvania, other than noncash prizes of the Pennsylvania State Lottery. Gambling and lottery winnings are derived from sources within Pennsylvania by reason of a wager placed in this Commonwealth, the conduct of a game of chance, or other gambling activity located in this Commonwealth or the redemption of a lottery prize from a lottery conducted in this Commonwealth. These winnings must be included as taxable income.

Pennsylvania does not tax nonresident individuals, estates or trusts on gambling and lottery winnings by reason of a wager placed outside this Commonwealth, the conduct of a game of chance or other gambling activity is located outside this Commonwealth or the redemption of a lottery prize from a lottery conducted outside this Commonwealth. Nonresidents do not include these winnings as taxable income.

**Pass-through Entities**

Shareholders, partners, or members in pass-through entities receiving income from gambling or lottery activities are subject to personal income tax on their distributive share of those earnings. Resident shareholders, partners, or members are subject to tax on all gambling or lottery earnings, as stated in subsection B above. Nonresident shareholders, partners, or members are subject to tax only on Pennsylvania sourced gambling or lottery earnings, as stated in subsection C above.

**Multistate Lotteries**

Multistate lottery prizes, such as those from the Powerball and Mega Millions, awarded on tickets purchased through a licensed Pennsylvania state lottery ticket vendor are considered a prize awarded by the Pennsylvania State Lottery. Such prizes are considered Pennsylvania source income and both residents and nonresidents are subject to tax on such income if the prize is a cash prize. Multistate lottery prizes awarded on tickets purchased through a vendor in another state lottery are considered prizes awarded by that state lottery. Such prizes are not considered Pennsylvania source income and only residents are taxed on such income regardless of whether the prize is a cash or noncash prize.

**Sale or Assignment of a Lottery Annuity**

Whenever a Pennsylvania resident lottery winner, who originally elected to receive the winnings in the form of annuity payments, sells or assigns the entire interest in the rights to those winnings to a third party for purposes of receiving a lump sum payment from that third party, the proceeds (lump sum payment) received are taxable. The taxpayer's basis in the asset (the annuity) is the total cost of the winning wager. The transaction is recorded on Line 1 of PA Schedule D, Sale, Exchange or Disposition of Property. The net gain from Schedule D would be reported on Line 5 of the PA-40, Net Gain or Loss from the Sale, Exchange or Disposition of Property.

## **COSTS AND OTHER EXPENSES**

Gambling and lottery winnings income may be determined by taking total winnings and subtracting the total costs of wagers.

### **Costs**

The cost of wagers during a tax year including amounts paid for lottery tickets, bingo games or cards, raffle tickets, slot machines card allotments, etc. may be deducted from total winnings received during the same tax year.

- **PA Lottery Ticket Costs**

The cost of tickets for the Pennsylvania Lottery purchased on or after July 21, 1983, and before Jan. 1, 2016, may not be deducted from winnings. Tickets for the Pennsylvania Lottery purchased during tax years beginning on or after Jan. 1, 2016, may be deducted from winnings received during the same tax year.

- **Other Lottery Ticket Costs**

The cost of lottery tickets purchased in other states or countries or for other lotteries during a tax year, may be deducted from winnings received during the same tax year.

- **Proof of Costs**

Taxpayers must maintain detailed records to substantiate all costs of wagers. Taxpayers have the burden of proving all costs deducted. See 61 PA Code §103.17.

### **Other Expenses**

No expenses attributable to gambling and lottery income are deductible. Expenses such as: parking, postage, entry fees, meals and lodging or travel may not be deducted in arriving at gambling and lottery winnings.

## **REPORTING**

Resident and nonresident individuals use PA-40 Schedule T, Gambling and Lottery Winnings, to report amount(s) of gambling and lottery winnings. Estates and trusts use PA-41 Schedule A, Interest Income and Gambling and Lottery Winnings, to report gambling and lottery winnings. Partnerships, limited liability companies and S corporations use PA-20S/PA-65 Schedule T, Gambling and Lottery Winnings.

Act 46 of 2003, amended Section 335, requires that any person required to submit a federal Form W-2G, Certain Gambling Winnings to the Secretary of the Treasury of the U.S. regarding taxable gambling or lottery winnings from sources within the Commonwealth, must also file a copy with the Pennsylvania Department of Revenue by March 1 of each year or, if filed electronically, by March 31 of each year. This applies to taxable years beginning after Dec. 31, 2003.

<b>TYPE OF RETURN</b>	<b>LINE ON RETURN</b>	<b>USE THIS SCHEDULE</b>
PA-40 Individual Income Tax Return	8	PA-40 Schedule T
PA-40 Nonresident Consolidated Income Tax Return	5	PA-40 Schedule T
PA-41 Fiduciary Income Tax Return	1	PA-41 Schedule A
PA-20S/PA-65 PA S Corporation/Partnership Information Return	8	PA-20S/PA65 Schedule T

## **WITHHOLDING ON PA LOTTERY PAYMENTS**

Act 84 of 2016 amended the personal income tax law to require withholding on Pennsylvania Lottery prize payments that are paid by the Pennsylvania Lottery or by a person making a Pennsylvania State Lottery prize payment in the form of an annuity. Pennsylvania withholding is required on such prize payments whenever tax is required to be withheld for federal income tax purposes. The tax is required to be withheld at the Pennsylvania personal income tax rate in effect at the time the prize payment is made. The withholding requirement is in effect for prize payments made after July 12, 2016 and is reported to winners on federal Form W-2G, Certain Gambling Winnings. Withholdings are reported by resident and nonresident taxpayers on PA Schedule T, Gambling and Lottery Winnings.