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Now that we're in the midst of "March Madness," the annual NCAA basketball tournament, you may be checking your bracket regularly to see how you're faring in your office pool or other entries. If you're on track for a big payday, be aware that the IRS is entitled to collect its fair share. What's more, unbeknownst to many taxpayers, a winning bracket can also cause state income tax complications.

Start with the basic premise: Winnings from gambling activities are taxable on the federal level. This includes amounts resulting from wagers on the NCAA tournament, the Super Bowl or any other sporting event, as well as betting at racetracks, casinos and even church bingo games. If you're fortunate enough to hit the jackpot for $1,200

and lost. And the losses can come from different activities you've engaged in during the year. For example, if you win $5,000 in this month's NCAA pool, you can offset the tax with a $2,000 setback from several trips to the track and $3,000 in losses from a Las Vegas getaway. But you can't claim a loss in excess of your winnings.

Unlike other deductions for miscellaneous expenses, there is no floor based on your adjusted gross income (AGI). Only miscellaneous expenses in excess of 2 percent of AGI for the year are deductible, but gambling losses are fully deductible, subject to the limit discussed above.

For this reason, clients should be advised to keep detailed records of their gambling activities. The best approach is to maintain a log and collect any documentary proof that is available. A little legwork up-front can provide rewards at tax return time.

What about state income taxes? Here's where things can really get tricky. Each state has its own set of laws concerning gambling activities. In some states, like Nevada, gambling isn't taxed at all, while other states impose tax based on a flat percentage or a graduated scale.

Many states follow the federal tax rules, so you'll owe tax on the full amount of gambling income, but you can offset it with losses from gambling. Unfortunately, however, a handful of states don't allow any deduction for gambling losses. Thus, if you hit the jackpot, it's taxable in full.

The list of states where you can't deduct losses includes Connecticut, Illinois, Indiana, Kansas, Massachusetts, Michigan, Ohio, Rhode Island, West Virginia and Wisconsin. Residents in these states face this extra tax whammy. Others can rely on their records to offset winnings with losses.

Anyway, it's not a bad problem to have if your team makes it to the Final 4. Just remember that Uncle Sam and most state taxing authorities also have a rooting interest.

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