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Taxing Blue Jays, Marlins and Other Pro Athletes

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Paying tax in multiple states or countries and divvying up income might sound like a nice problem to have. But sometimes being taxed more than once really smarts. In fact, some professional athletes are so worried about taxes that they decline to play in certain locations. *See* Wood, "Like Mitt Romney, Usain Bolt Wants To Pay Only 13%," *Forbes.com* (8/17/12).

Foreign athletes must file U.S. income tax returns and face special withholding rules. They generally must pay U.S. income tax on their U.S.-source income. What is considered U.S.-source can be debated but includes pay for performances, endorsements, merchandise sales, and royalty or other income closely related to the event.

The IRS has a special program targeting foreign athletes and entertainers. Depending on an athlete's home country, treaty benefits may apply. Even so, disputes are common about how much income to allocate to particular countries and where endorsement earnings should be taxed.

For example, South African golfer Retief Goosen twice won the U.S. Open. His success rate wasn't quite as good in U.S. Tax Court. *See Goosen v. Comr.*[1] His case concerned what was U.S.-source income subject to tax by the IRS. *See* Wood, "IRS Sand Trap For Pro Golfers," *Forbes.com* (6/16/11).

Moving teams can also cause tax pain. Just consider five Miami Marlins traded to the Toronto Blue Jays, Josh Johnson, Mark Buehrle, Jose Reyes, Emilio Bonafacio, and John Buck (Buck has since traded to the New York Mets). Is this a move up in teams and cities? Sure, but taxes are another matter. See Costs, "These Marlins' Tax Bills Are Headed Way North," *Online.WSJ.com* (11/14/12). After all, Florida has no state income tax.

In contrast, moving to Ontario means Canadian taxes on top of U.S. taxes. What's more, Ontario is poised to impose a new high rate on the rich. An analysis by Robert Raiola of Fazio, Mannuzza, Roche, Tankel and LaPilusa claims the tax hit to the five players is a whopping $8.4 million. Even if that number turns out to be inflated, it shows taxes can figure hugely in an athlete's bottom line.

It's no wonder some athletes and managers plan aggressively.

There is often at least some flexibility, and that's where planning comes into play. Goosen treated only 7% of his total endorsement income as U.S.-sourced. The Tax Court held Goosen's endorsement fees and bonuses from Acushnet, TaylorMade and Izod were 50% personal services and 50% royalty income. The latter was effectively connected with a U.S. trade or business.

Goosen's royalty income from Rolex was 50% U.S.-source income not effectively connected with a U.S. trade or business. His royalty income from Upper Deck was 92% U.S.-source income not effectively connected with a U.S. trade or business. Goosen's royalties from Electronic Arts were 70% U.S.-source income not effectively connected with a U.S. trade or business.

Is it any wonder that successful professional athletes need professional advice? Cases of this sort demand careful planning and good documentation.

For more information, in the Tax Management Portfolios, see Bissell, 907 T.M., U.S. Income Taxation of Nonresident Alien Individuals, *and in Tax Practice Series, see ¶7150, U.S. Persons - Worldwide Taxation.*

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[1] 136 T.C. No. 27 (2011).