**JOCK TAX: REDUCING THE TAX LIABILITY OF PROFESSIONAL ATHLETES: FARINESS IN APPORTIONMENT**

*This is the first-post in a multi-part series dealing with the income tax imposed on professional athlete earnings. This post reveals the value in questioning and sometimes challenging the apportionment formula methodologies employed by states and municipalities in application to non-resident professional athletes.*

**Here’s the hypothetical:** I’m a professional athlete, live in Florida and travel for games. When I travel to another state or municipality for work, they frequently impose an income tax on my earnings. I’m neither afforded an exemption nor is there an applicable reciprocal agreement between my state and the places I visit. What can I do to reduce my SALT exposure in these foreign jurisdictions?

All but nine states impose an income tax on wage earnings.[[1]](#footnote-1) Generally, non-resident taxpayers are afforded an exemption[[2]](#footnote-2) from those taxes (or fly under the audit radar), but professional athletes receive special attention from the taxing authorities. Publicized high-salaries and travel schedules reveal to tax authorities a professional athlete’s travel schedule and earnings, making it easy to determine whether they’ve accurately reported. Since the players are audit targets, every traveling-member of a team including coaches, trainers, broadcasters and referees are targets as well.[[3]](#footnote-3) Making the issue worse for professional athletes, the Tax Cuts and Jobs Act now limits the itemized deduction for state and local taxes to $10,000.00. Without question, tax planning for athletes is necessary to avoid overpaying on both the federal and state and local levels. Now that the SALT deduction is capped, professional athletes and team members should examine and if possible, further reduce their SALT exposure.

There are a few issues that should be at the top of any SALT tax professional’s list when tax planning on behalf of a professional athlete. One main consideration is where an athlete chooses to live. The choice of legal domicile or permanent-residence can dramatically reduce an athlete’s overall effective tax liability. For example, Florida has no income tax – when a professional athlete is domiciled in Florida and never leaves, then they will have no foreign state and local tax exposure. Of course, most professional athletes must travel, but when the majority of their work activities take place in their state of domicile and non-tax jurisdictions, they are able to substantially reduce their non-resident tax exposure. Exemptions and reciprocal agreements[[4]](#footnote-4) can provide a substantial amount of tax relief as well, but when they are unavailable, we have to seek other ways to reduce their non-resident tax exposure. *In some cases, challenging the apportionment formula methodologies employed by states and municipalities in application to non-resident professional athletes could further reduce their non-resident tax exposure.*

Multiple methods exist for apportioning income on the state and local level. The two main approaches employed by states and municipalities distinguish between unitary business and non-business income. With regard to unitary business income, various apportionment formulas are applied, while nonbusiness income must usually be more specifically allocated to that place where the particular increment of income is earned.[[5]](#footnote-5)

The formulas used by states and municipalities to apportion a professional athletes’ income to that state, among others, include the “games played” and “duty days” methods. The games played method is based on the number of games played in a state or municipality, over the total number of games played. The duty days method is based on earnings in a state or municipality from services performed under a contract from the beginning of an official preseason activity until the last game played, over the total of the same. Both the games played and duty days formulas produce a ratio which is multiplied by the total amount of the players games or compensation resulting in the amount of an athlete’s income sourced to the jurisdiction.

The application of a different formula to the same person can result in different amount of taxes owed to different jurisdictions, even when they spend an identical amount of time in jurisdictions with the same tax rate. Complexity, the cost of compliance and sometimes huge differences in effective tax rates would seem to warrant challenging a state or local income tax on the basis of their choice of method. As a general rule, unless an application of the method is found to be unconstitutional, challenging the legitimacy of an apportionment methodology on its face is challenging at best.

The federal definition of wages does not specifically address how to apportion or allocate income; barring a U.S. Constitutional challenge, this leaves it up to the state’s broad authority to adopt an apportionment methodology proper for that jurisdiction. States generally follow the same protocol with their municipalities – unless a “provision of state law expressly imposes the restriction” [on apportionment], municipalities enjoy like-kind home-rule authority.[[6]](#footnote-6) In English, that means states and localities are generally free to come up with their own formulas, **but this is not without limitation as in application, a formula may effectively violate Due Process.** In the most recent Ohio Supreme Court case on point, the games-played method was successfully challenged by two NFL players as a violation of the Due Process Clause.[[7]](#footnote-7)

In Hillenmeyer v. Cleveland Board of Review, the court found that “the games-played method of determining the tax base fails to afford due process when applied to [non-resident] NFL players” because it reached a portion of the non-resident’s compensation that was not connected with the municipality, in this case, Cleveland. To satisfy Due Process, the taxpayer must have a “definite link, some minimum connection” to a state[[8]](#footnote-8) ***and*** “the income attributed to the State for tax purposes must be rationally related to ‘values connected with the taxing State.’ ”[[9]](#footnote-9) Due process requires an allocation that reasonably associates the amount of compensation taxed with work the taxpayer performed within the…[state or municipality].”[[10]](#footnote-10) The games played method effectively allocated 5% of the players’ income to Cleveland on the basis of two-days spent in Cleveland; whereas, applying the duty days method, resulted in a 1.25% allocation based on the same two-days. Although the games played formula has not been struck down as a violation of Due Process on its face, **its application** in this case allowed Cleveland to reach extraterritorial income; a clear violation of Due Process which afforded the athletes an opportunity to apply the more reasonable method (and file amended returns for the last three-years to recoup those overpayments).

To begin with, it seems worthwhile to take a look at each and every taxing state and municipality’s apportionment methodology as compared to others, to determine whether the formula *as applied* seems reasonable. If not, a player may be paying more than their fair-share of tax to the state or locality in question.

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1. <https://taxfoundation.org/toolkit-sources-state-local-tax-collections/>. Tennessee and New Hampshire tax income from interest and dividends. However, subsection (d) invalidates the exemption for professional athletes. [↑](#footnote-ref-1)
2. Ohio Rev. Code § 718.011(B)(1) allows for an exemption to municipal taxes for non-residents doing business in the municipality for 20 days. [↑](#footnote-ref-2)
3. Sports Illustrated https://www.si.com/nfl/2016/02/06/super-bowl-50-california-jock-tax-cam-newton. [↑](#footnote-ref-3)
4. https://tax.thomsonreuters.com/blog/accounting-audit-payroll/payroll/state-by-state-reciprocity-agreements/. [↑](#footnote-ref-4)
5. Peters and Miller, *Apportionability in State Income Taxation: The Uniform Division of Income for Tax Purposes Act and Allied-Signal*, 60 Tax Lawyer 57 (2006). [↑](#footnote-ref-5)
6. Hillenmeyer v. Cleveland Bd. of Rev., 144 Ohio St.3d 165 2015-Ohio-1623 (p. 9). [↑](#footnote-ref-6)
7. United States Constitution, 14th Amendment. [↑](#footnote-ref-7)
8. Quill Corp. v. North Dakota, 504 U.S. 298, 306, 112 S.Ct. 1904, 119 L.Ed.2d 91 (1992). [↑](#footnote-ref-8)
9. Norfolk & W. Ry. Co. v. Missouri State Tax Comm., 390 U.S. 317, 325, 88 S.Ct. 995, 19 L.Ed.2d 1201. [↑](#footnote-ref-9)
10. Id. [↑](#footnote-ref-10)