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Taxation Is the Name of the Game for Professional Athletes

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Professional athletes' high salaries—and publicly available team travel schedules—make them a prime target for state tax authorities, but athletes can minimize their state income taxes with careful tax planning, says Michael B. Weicher of Marcum LLP.

"Taxes! Plain and simple. I'm not going to lie," said former New York Islanders Head Coach Barry Trotz when asked why he moved from New York to Tennessee.

The Islanders fired Trotz last May with one year left on his contract, so he is being paid $4 million not to coach this NHL season. When Trotz bought a home in Nashville, people speculated that he was trying to get a management position with the team that gave him his start as a head coach, the Nashville Predators. Apparently, Trotz was just making a sound financial decision, saving himself most likely over $300,000 moving from New York, a high tax state, to Tennessee, a state without an individual income tax.

In general, people who earn a living by providing services are subject to tax in the state where they provide those services as well as in their resident state. Professional athletes, as well as the coaches, trainers, and other personnel traveling with the team, must allocate their salary to the various states where the team plays or practices.

Bonuses, which are paid separately from salary and are not conditioned on the performance of services, are generally allocable only to the recipient's resident state. Endorsement income requiring a player to appear in a specific location will be subject to tax in that state, while endorsement income merely using the player's name, image, or likeness will be subject to tax only in the player's resident state.

Most states use the "duty days" method allocating the player's income based on the percentage of the total number of days the person works for the team, including games, practices, team meetings, and other team-related activities in the state versus total duty days everywhere. A few states use the games played method allocating a player's income based on the proportion of games played in the state versus the total games played. Although it varies by league, at least half of a player's salary will usually be subject to tax in the state that their team is based in because of the number of home games, practices, and meetings held there.

In addition to paying tax where they perform services, they are subject to tax on their entire income in their resident state. When you pay tax in multiple states, you will get a credit in your resident state for taxes paid to non-resident states. If your resident state has a lower tax rate than the rate in the non-resident states, your credit will be limited, and there is no tax credit if you live in a state without an income tax.

Because Trotz is going to be paid without having to perform any services for his former team, his income will only be subject to tax in his resident state. Accordingly, he acted prudently in moving to a state without an income tax.

Similarly, more free agents are considering state taxes when choosing which team to sign with. Many factors go into a free agent's decision about where to sign that next contract, including the lure of the big city with possibly big endorsement deals, playing time, the chance to win a championship, and how far away the team is from friends and family.

Today's professional athletes also have financial advisers and accountants who are telling them to consider state taxes in the net value of their contract offers. Tyreek Hill, for example, recently admitted he chose to sign with the Miami Dolphins over the New York Jets in part because Florida has no personal income tax and New York is a high tax state.

Establishing Residency

If a player decides to play for a team in a high tax state, they should be careful not to become a resident in that state, in which case their entire income will be subject to tax there. There are two separate ways to establish residency in a state. The first way, called statutory residency, is simply to have a permanent place of abode in a state and to spend more than 183 days in that state. The second way is to be domiciled in the state. Your domicile is where your primary residence is, or as the saying goes, "home is where your heart is." This is a facts and circumstances test, and states will examine five primary factors to determine domicile:

1. Home—if the individual owns more than one home, the state will compare the size, use, and other factors of the individual's homes;
2. Active business involvement—the state will look to see if the athlete has any business activity outside of playing and if so where they conduct it;
3. Time—the state will focus on where the athlete spends time in the off-season;
4. Personal items—where the individual keeps personal and sentimental items such as trophies and championship rings; and
5. Family—where does the athlete's immediate family live?

New York disputed Derek Jeter's claim that he was a Florida resident for tax years 2001 through 2003 when he was playing for the New York Yankees. New York argued that Jeter was "immersed in the New York community" and kept his personal items in his New York

City apartment. In addition, the state said Jeter spent holidays and had business interests outside of Florida. Jeter reached an undisclosed settlement with New York and sold his Manhattan apartment when he retired from baseball.

It's not hard to imagine other athletes having residency challenges, given that their incomes allow them to buy expensive homes in the cities they play in and bring their families to live with them. Professional athletes' high salaries and publicly available team travel schedules make them a prime target for state tax authorities. Athletes must file returns in all of the jurisdictions where they play that have an income tax. Careful tax planning can minimize an athlete's state income tax, but for many athletes, there are more important things in life than minimizing taxes.

Author Information

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