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Kathryn Kisska-Schulze

Adam Epstein

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Article

THE CLAIM GAME: ANALYZING THE TAX IMPLICATIONS OF STUDENT-ATHLETE INSURANCE POLICY PAYOUTS

KATHRYN KISSKA-SCHULZE* & ADAM EPSTEIN**

I. INTRODUCTION

Prior to the 2016–2017 college football season, quarterback Deshaun Watson accepted a pair of \$5 million disability insurance policies paid for by Clemson University to protect against a catastrophic career-ending injury and potential loss-of-value he might suffer in the National Football League (NFL) draft if he sustained an injury while playing for the Tigers.¹ Watson is not the only student-athlete who has ever accepted disability insurance coverage paid for by their university, and it turned out to be an astute decision as Watson was a back-to-back Heisman Trophy finalist who entered the 2017 NFL Draft as a top overall pick.²

For the small number of elite student-athletes whose athletic prowess garner professional draft potential, enrolling in the National Collegiate Athletic Association's (NCAA) Exceptional Student-Athlete Disability Insurance ("ESDI") and loss-of-value ("LOV") insurance programs may be a crucial step in protecting against career-ending injuries and loss of future earnings as professional athletes.³ Recognizing that these student-athletes might,

* J.D., LL.M., Assistant Professor, College of Business, School of Accountancy, Clemson University.

** J.D./M.B.A., Professor, Department of Finance and Law, Central Michigan University.

1. See Brett McMurphy, *Tigers QB Deshaun Watson Takes out \$5 Million Insurance Policies*, ESPN (Aug. 17, 2016), http://www.espn.com/college-football/story/_/id/17328331/clemson-tigers-qb-deshaun-watson-takes-5-million-insurance-policies [<https://perma.cc/PU6C-NPMB>].

2. See Alex Kirshner, *2016 Heisman Trophy Finalists: Lamar Jackson Joined by 4 Others*, SB NATION (Dec. 6, 2016), <https://www.sbnation.com/college-football/2016/12/5/13837236/heisman-trophy-finalists-2016-list> [<https://perma.cc/DBE3-Z5WY>] (noting that Watson was finalist for Heisman Trophy for second consecutive year). See also Adam Wells, *Top Reaction After Texans Trade up to Draft Deshaun Watson in 2017 NFL Draft*, BLEACHER REPORT (Apr. 27, 2017), <http://bleacherreport.com/articles/2698765-top-reaction-after-texans-trade-up-to-draft-deshaun-watson-in-2017-nfl-draft> [<https://perma.cc/23LN-CR9S>] (reporting that Watson was the 12th overall pick by the Houston Texans in the 2017 NFL draft).

3. See *Student-Athlete Insurance Programs*, NCAA, <http://www.ncaa.org/about/resources/insurance/student-athlete-insurance-programs> [<https://perma.cc/>]

however, forfeit their remaining years of collegiate eligibility to sign with an agent and enter a professional draft, some universities are selectively paying the premiums for ESDI and LOV insurance policies to entice star student-athletes to stay at the institutions for another season.⁴ In a big-money industry where twenty-seven schools now top the \$100 million revenue mark from their athletic departments, universities have a vested interest in retaining top players for whom these policies are purchased.⁵

A curious question regarding ESDI and LOV premiums paid for by universities is whether an injury-related payout to a student-athlete-beneficiary amounts to a taxable event at the federal level. From its origination in the U.S. Constitution granting Congress the power to “lay and collect taxes,” a major justification of the federal government’s taxing power is to raise revenue.⁶ To help meet revenue needs, Internal Revenue Code (“IRC”) § 61 dictates that gross income include “all income from whatever source derived.”⁷ This rule carries numerous exceptions, including amounts received from disability payouts when an individual pays the entire cost of a health or accident insurance plan out of their own pocket.⁸ However, the Internal Revenue Service (IRS) generally requires that insurance payouts received through accident or health plans paid for by an *employer* be reported as income to the beneficiary.⁹ Because the IRS and the American legal system have thus far not characterized student-athletes as employees of their academic institutions, and because the Code and Treasury Regulations (“Treas. Regs.”) provide no guidance on the tax consequences of payouts received from insurance policies purchased by non-employers, analyzing the

MU5G-LFAC] (last visited Jan. 4, 2018) [hereinafter *Student-Athlete Insurance Programs*]. See also *Loss-of-Value Insurance Information*, NCAA, <http://www.ncaa.org/about/resources/insurance/loss-value-insurance-information> [<https://perma.cc/3XCN-CXPY>] (last visited Jan. 4, 2018) [hereinafter *Loss-of-Value Insurance Information*].

4. See Marc Tracy, *Insurance Doesn’t Eliminate Risk for Top College Athletes Who Forgo Draft*, N.Y. TIMES (May 8, 2015), <http://www.nytimes.com/2015/05/09/sports/ncaafotball/insurance-doesnt-eliminate-risk-for-top-college-athletes-who-forgo-draft.html> (documenting various college athletic programs that have paid for loss-of-value insurance policies on behalf of star student-athletes, including Florida State, Texas A&M, and University of Georgia).

5. See Cork Gaines, *The 27 Schools That Make at Least \$100 Million in College Sports*, BUS. INSIDER (Nov. 25, 2017), <http://www.businessinsider.com/schools-most-revenue-college-sports-texas-longhorns-2017-11/#27-university-of-virginia-1006-million-1> [<https://perma.cc/U6NC-UCZ8>].

6. U.S. CONST. art. I, § 8, cl. 1.

7. 26 U.S.C. § 61(a) (2012).

8. See *id.* § 104(a)(3). See also Treas. Reg. § 1.104-1(d) (2017).

9. 26 U.S.C. § 105(a). See also Treas. Reg. § 1.105-1(a).

taxability of ESDI and LOV payouts when the premiums are paid for by universities provides an important addition to academic and practitioner literature.¹⁰

This article focuses on two scenarios to determine whether injury payouts received by student-athletes are taxable at the federal level when their universities pay for the insurance premiums. We first explore the tax consequences of payouts if the premium payments are either purchased individually by the student-athlete or financed through a private loan from a third party. Second, we examine the taxability of payouts when a college or university pays the cost of the premium for the benefit of the select student-athlete. We surmise that to best ensure a tax-free payout from an ESDI or LOV insurance policy following injury, a student-athlete should purchase the policy individually. We also conclude that treating premium payments as a loan provides a sound opportunity to minimize or eliminate tax imposition on payouts received following a catastrophic injury so long as the loan is structured properly. We finally conclude that the IRS is unlikely to impose a tax on disability payouts made to student-athletes when their college or university pays the premium on their behalf.

Our analysis is based on ambiguity in the IRC and the premise that the IRS has historically been reluctant to impose taxes on student-athletes, as well as the college sports industry in general. However, because the language of the IRC does not specifically address the tax consequences of a non-employer paying the cost of disability insurance premium on behalf of a third party, we further recommend that the IRS publish a Revenue Ruling to address the taxability of proceeds received from disability insurance policies purchased for student-athletes by their universities to clarify whether or not universities are considered employers in this context, provide uniformity in applying the IRC to disability insurance policies paid for by universities, and confirm whether the IRS intends to continue its historically favorable tax treatment of student-athletes by excluding their benefits from falling under the umbrella of taxable income.¹¹

10. As of the date of this article, no situation has been publicized where proceeds have been distributed to an injured student-athlete under a disability insurance policy that was purchased by a university on behalf of the student-athlete. However, as will be discussed in this article, there have been instances where proceeds have been distributed to injured student-athletes under policies purchased by the beneficiary himself or herself.

11. See, e.g., JOHN A. KOSKINEN, U.S. DEP'T OF TREAS.: IRS, No. 2014-0016 (Apr. 9, 2014), <https://www.irs.gov/pub/irs-wd/14-0016.pdf> [<https://perma.cc/35YH-CYSH>] (letter from John A. Koskinen to Senator Richard Burr (R-N.C.)). This

To better understand the parameters of our analyses and conclusions, Part I discusses ESDI and LOV insurance policies as supported by the NCAA. Part II analyzes the federal tax consequences of insurance policy payouts as imposed by the IRC. Part III dissects policy arguments surrounding the imposition of tax and employment litigation in the college sports industry. Part IV examines the taxability of ESDI and LOV insurance policies based on whether premiums are paid for by student-athletes individually, financed through a loan agreement with a third party, or purchased outright by a university on behalf of its student-athlete-beneficiary. Finally, Part V offers conclusions to help address the ambiguities surrounding the tax implications of disability insurance policy payouts when covered student-athletes suffer career-ending injuries.

II. DISABILITY AND DRAFT PROTECTION INSURANCE FOR TOMORROW'S PROFESSIONAL ATHLETES

In 1990, the NCAA enacted the ESDI Program to protect elite student-athletes against future lost earnings as professional athletes due to disabling injuries or sicknesses that may occur during their college career.¹² To qualify for ESDI benefits, the injury or illness sustained must be career-ending, thereby preventing the player from ever competing as a professional athlete.¹³ Distinguishable from ESDI insurance, LOV coverage is typically purchased the year leading up to professional draft eligibility, attempting to shield student-athletes' professional contract value from falling below a certain draft-rank threshold due to the significant injury or illness.¹⁴

letter is Koskinen's response to Burr's March 28, 2014 letter to Koskinen, Commissioner of the IRS until November 12, 2017, in which Burr requested confirmation of the current federal tax treatment of college athletic scholarships. *Id.* In his response to that letter, Koskinen stated that "[i]t has long been the position of the Internal Revenue Service that athletic scholarships can qualify for exclusion from income under section 117." *Id.* The letter further states with regard to the 1977 Revenue Ruling 77-263, 1977-2 C.B. 47, that "the athletic scholarship awarded by the university is primarily to aid the recipients in pursuing their studies and, therefore, is excludable under section 117." *Id.*

12. See *Student-Athlete Insurance Programs*, *supra* note 3 (offering that the inaugural NCAA ESDI insurance program was only available to elite men's football and basketball players). The program was later expanded in 1991 to include elite baseball players, in 1993 to include men's ice hockey, and again in 1998 to include women's basketball. *Id.*

13. See Daniel J. Kain et al., *Draft Protection Insurance: Elite Athlete Loss-of-Value Policies and the Emerging Wave of Coverage Litigation*, 4 JEFFREY S. MOORAD SPORTS L.J. 217, 233 (2017).

14. *Loss-of-Value FAQs*, NCAA, <http://www.ncaa.org/about/resources/insurance/loss-value-faqs> [https://perma.cc/5M6A-XAH8] (last visited Jan. 4, 2018).

Recently, LOV insurance has generated interest following former student-athletes Christian McCaffrey's (Stanford University) and Leonard Fournette's (Louisiana State University) decisions to skip the 2016 college bowl games for fear of injuries that could have diminished their 2017 professional football draft rankings and athletic careers.¹⁵ Also recently, Michigan tight end, Jake Butt, who suffered a torn ACL in the 2016 Orange Bowl, entertained media blitz in 2017 following announcements that he would collect on a LOV policy he had purchased prior to the start of the season.¹⁶

Although some student-athletes have successfully collected ESDI payouts after sustaining injuries, only a handful of college athletes have collected payouts arising from LOV policies.¹⁷ Several lawsuits, however, have been filed since 2015 involving former college athletes who were denied claims under LOV policies following injury.¹⁸

While student-athletes generally have access to various insurance options depending on their NCAA Division (I, II, III), their sport, and their status as an elite athlete, access to ESDI and LOV insurance policies are the critical focus of this article.¹⁹ The remainder of this section explains in detail both (a) permanent total

15. See Dennis Dodd, *Jaylon Smith's Insurance Payout Could Lead to More Players Skipping Bowl Games*, CBS SPORTS (Mar. 23, 2017), <http://www.cbssports.com/college-football/news/jaylon-smiths-insurance-payout-could-lead-to-more-players-skipping-bowl-games/> [https://perma.cc/6BVN-3GJB].

16. Penn Collins, *College Athletes Are Now Protecting Themselves with 'Career Protection' Insurance Policies*, GOOD SPORTS (May 4, 2017), <https://sports.good.is/articles/college-athletes-insurance> [https://perma.cc/W7CL-ZNNM].

17. See Richard C. Giller, *Lawsuits Involving Former USC Football Stars Shine a Light on the Murky World of Loss-of-Value Insurance*, POLSINELLI, <http://www.polsinelli.com/~media/Intelligence%20Documents/gillerlossofvalueinsurancefinalauthcheckdam> (last visited Jan. 4, 2018) (noting that some athletes have successfully collected permanent total disability payouts, but that no athletes have reportedly been successful in collecting LOV payouts). See also Dodd, *supra* note 15 (documenting that Jaylon Smith (Notre Dame), Ifo Ekpre-Olomu (Oregon), E.J. Bibbs (Iowa State), and Silas Redd (University of Southern California (USC)) have received LOV payouts following injuries).

18. See Giller, *supra* note 17. See also Kain et al, *supra* note 13, at 220 (citing to *Lee v. Certain Underwriters at Lloyd's London*, 2:15-cv-01614-ODW-JC (C.D. Cal. Mar. 4, 2015); *Breslin v. Amtrust at Lloyd's Ltd.*, 2:15-cv-00330-R-AS (C.D. Cal. Jan. 15, 2015); *Breslin v. Univ. of S. Cal.*, No. BC592870 (Cal. Super. Ct. Aug. 28, 2015)).

19. Insurance options allowable by the NCAA include personal medical insurance coverage for expenses arising from injuries sustained while participating in a covered athletic event, and disability insurance coverage which includes catastrophic and ESDI insurance. For more information, see NCAA, 2017-18 NCAA DIVISION I MANUAL, art. § 3.2.4.8 [hereinafter 2017-18 NCAA MANUAL], available at <https://www.ncaapublications.com/p-4511-2017-2018-ncaa-division-i-manual-august-version-available-august-2017.aspx> [https://perma.cc/XAD6-H64U]. See also *Student-Athlete Insurance Programs*, *supra* note 3.

disability and (b) draft protection insurance coverage options that are available to elite student-athletes.

A. Permanent Total Disability Insurance

The traditional purpose of disability insurance is to “protect a person from a loss of income during a period of incapacity for work.”²⁰ Disability insurance is generally offered in one of two forms: permanent (an injury resulting in perpetual loss of work) and temporary (an injury resulting in short-term loss of work).²¹ The NCAA sponsors two types of disability insurance programs for student-athletes: Catastrophic Injury Insurance and Exceptional Student-Athlete Disability.²² Each of these policy programs is discussed separately below.

1. *Catastrophic Injury Insurance Program*

Effective August 1, 2005, the NCAA Division I Bylaws (“Bylaws”) require that member institutions certify that every student-athlete have personal medical insurance coverage for expenses arising from injuries sustained while participating in a covered athletic event.²³ The Bylaws further require that any medical expenses exceeding \$90,000 be covered by the NCAA Catastrophic Injury Insurance Program (“CIIP”).²⁴

The CIIP covers student-athletes who are “catastrophically injured while participating in a covered intercollegiate athletic activity.”²⁵ This program, which insures student-athletes at any of the

20. Glenn M. Wong & Chris Deubert, *The Legal & Business Aspects of Career-Ending Disability Insurance Policies in Professional and College Sports*, 17 VILL. SPORTS & ENT. L.J. 473, 482 (2010) (quoting BLACK’S LAW DICTIONARY 816 (8th ed. 2004)).

21. *See id.*

22. *See Student-Athlete Insurance Programs, supra* note 3.

23. *See* 2017–18 NCAA MANUAL, *supra* note 19, at art. § 3.2.4.8 (“An active member institution must certify insurance coverage for medical expenses resulting from athletically related injuries sustained by the following individuals while participating in a covered event: A student-athlete participating in a covered-event in an intercollegiate sports as recognized by the participating institution.”). *See also id.* at art. § 3.2.4.8.3 (“Covered Event”) (defining the expression to include team travel, competition, practices, and conditioning sessions during playing season, as well as any authorized practice and conditioning sessions organized during off season).

24. *Id.* at art. § 3.2.4.8.1 (“Amount of Coverage Insurance”) (requiring that coverage “be of equal or greater value than the deductible of the NCAA catastrophic injury insurance program”). Currently, that deductible stands at \$90,000. *Id.*

25. *Student-Athlete Insurance Programs, supra* note 3. *See also* NCAA Catastrophic Injury Insurance Program Benefit Summary for the Period 8/1/17 through 7/31/20, NCAA [hereinafter NCAA Catastrophic Injury Insurance Program Benefit Summary], http://www.ncaa.org/sites/default/files/2018_17-20%20Cat%20Benefit%20Summary_20180105.pdf [https://perma.cc/MMS5-JUQL] (last visited Mar. 19, 2018) (offer-

active member NCAA institutions, applies when one of two types of claims is filed: (1) a serious injury occurs that results in or may result in a disability, or (2) an injury occurs that is likely to exceed the NCAA CIIP deductible.²⁶ The premium for the CIIP is paid for by the NCAA itself, and allows for maximum benefits of \$20 million with a \$90,000 deductible.²⁷

Three categories of benefits are available under the CIIP, including medical, disability, and death.²⁸ Medical benefits are available to insured persons who incur expenses in excess of the deductible as a result of an injury sustained during a covered event.²⁹ Disability benefits are available to individuals who are totally or partially disabled while participating in a covered event.³⁰ Although the expression “catastrophic injury” is not specifically defined by the NCAA, it includes injuries that have or may result in a disability, including severe injuries to the head or spinal cord.³¹ Total disability includes irrecoverable loss of speech, hearing, sight, use of limbs, or severely diminished mental capacity due to brain or other neurological injury.³² In addition to monetary subsidy, other benefits available include vocational rehabilitation and college edu-

ing that coverage is also available to student coaches, student managers, student trainers and student cheerleaders).

26. *NCAA Catastrophic Injury Insurance Program Frequently Asked Questions*, NCAA, http://www.ncaa.org/sites/default/files/2018_Cat%20FAQs_20180105.pdf [<https://perma.cc/YE73-XZ5G>] (last visited Mar. 19, 2018) (applying to 8/1/2017 to 7/31/2020 Policy Period). The NCAA defines “disability” as follows:

The condition of a disability can be determined when the following criteria have been met: (1) The student-athlete’s disability results from an injury or sickness, (2) The student-athlete’s injury or sickness occurs while the policy is in force, (3) The student-athlete is under the regular care of a qualified physician, (4) The student-athlete is unable to engage in sporting activity at the professional level, (5) The applicable elimination period has elapsed, and (6) The student-athlete’s total disability prevents him or her from signing any employment contract with any professional team as a professional athlete in his or her sporting activity.

Student-Athlete Insurance Programs, *supra* note 3.

27. *See NCAA Catastrophic Injury Insurance Program Benefit Summary*, *supra* note 25 (noting that deductible decreases to \$75,000 for institutions that participate in NCAA Group Basic Accident Medical Program).

28. *See id.*

29. *See id.*

30. *See id.*

31. *See id.*

32. *See NCAA Catastrophic Injury Insurance Program Frequently Asked Questions*, *supra* note 26.

cation.³³ Finally, a \$25,000 death benefit is payable for death resulting from an accident or injury occurring during a covered event.³⁴

While the purpose of the CIIP is to provide a form of disability insurance to all its covered student-athletes, for a small number the CIIP is not monetarily protective enough to cover the potential loss in wages and other income that might affect professionally-bound elite student-athletes who are injured. For a finite group, including star basketball player, Miles Bridges (Michigan State University), who in April 2017 announced his intent to return to MSU for his sophomore year in lieu of entering the National Basketball Association (NBA) draft, the additional protection offered by ESDI played a key role in his decision to play another season for the Spartans.³⁵

2. *Exceptional Student-Athlete Disability Insurance*

The ESDI Program was created to insulate student-athletes projected to be top-round draft picks by the professional leagues.³⁶ To be eligible for coverage, the student-athlete must be expected to be a draftee in either the first two rounds of the NFL or National Hockey League (NHL) draft, or a first round draft pick in the NBA, Major League Baseball (MLB), or Women's National Basketball Association (WNBA).³⁷ ESDI policies are available through either the NCAA or private insurers, and they protect against potentially career-ending injuries.³⁸

33. See *NCAA Catastrophic Injury Insurance Program Benefit Summary*, *supra* note 25.

34. See *id.* See also 2017–18 NCAA MANUAL, *supra* note 19, at art. § 3.2.4.8.3 (“Covered Event”) (defining expression to include team travel, competition, practices, and conditioning sessions during playing season, as well as any authorized practice and conditioning sessions organized during off season).

35. See Graham Couch, *Couch: Miles Bridges Is a Millionaire-in-Waiting, Thanks to Insurance*, LANSING ST. J. (Apr. 19, 2017, 1:25 PM), <http://www.lansingstatejournal.com/story/sports/columnists/graham-couch/2017/04/19/miles-bridges-insurance-policy-couch-column/100638812/> [<https://perma.cc/SKM7-NH8W>].

36. See Adam Epstein & Paul M. Anderson, *The Relationship Between a Collegiate Student-Athlete and the University: An Historical and Legal Perspective*, 26 MARQ. SPORTS L. REV. 287, 295 (2016). See also *Student-Athlete Insurance Programs*, *supra* note 3 (noting that in 1990, the program was available only to exceptional student-athletes in the sports of football and men's basketball. In 1991, the program expanded to include baseball, in 1993 men's ice hockey became eligible, and in 1998 the program expanded to include women's basketball).

37. See *Student-Athlete Insurance Programs*, *supra* note 3 (noting that exceptional student-athletes in other sports who have demonstrated a strong likelihood of a professional career in their sport may be eligible for coverage on a case-by-case basis).

38. Jill Wieber Lens & Joshua Lens, *Insurance Coverage for Elite Athletes*, 84 MISS. L.J. 134, 137 (2014) (noting the insurance can be purchased through the NCAA or private insurers).

ESDI offers permanent total disability (“PTD”) coverage that gives student-athletes protection against “future loss of earnings as a professional athlete due to a disabling injury or sickness that may occur during [their] collegiate career.”³⁹ In addition, ESDI protects student-athletes’ interests against sports agents who might otherwise encourage them to sign up for representation, forfeit their “amateur” status, and leave college early with remaining eligibility to instead pursue the professional leagues.⁴⁰ While maximum coverage limits vary by sport, the amount of coverage available to any eligible student-athlete is based on their prospective status in the upcoming draft.⁴¹ The ESDI payout is a one-time occurrence and contingent on the premise that the student-athlete will never be eligible to play professional sports due to their injury.⁴²

Unlike the CIIP premiums that are paid for by the NCAA, student-athletes or their institutions must purchase ESDI coverage on their own and at their own expense.⁴³ If personal funds are unavailable to cover the costs of the premiums, the NCAA allows student-athletes to take out loans for this purpose.⁴⁴ As ESDI premium costs run between \$10,000 and \$12,000 for each \$1 million dollar in coverage, securing loans to pay these premiums is commonplace.⁴⁵ Thus, to further incentivize elite student-athletes to return to college play rather than forego their remaining collegiate eligibility to enter the professional draft, the NCAA allows them to take out personal loans against their future earnings without jeopardizing their amateur status.⁴⁶

39. *Student-Athlete Insurance Programs*, *supra* note 3.

40. *See* Wong & Deubert, *supra* note 20, at 506.

41. *See Student-Athlete Insurance Programs*, *supra* note 3.

42. *See* Lens & Lens, *supra* note 38, at 138.

43. *See Student-Athlete Insurance Programs*, *supra* note 3.

44. *See* 2017–18 NCAA MANUAL, *supra* note 19, at art. § 12.1.2.4.4 (“Exception for Insurance Against Disabling Injury or Illness, or Loss of Value”) (“An individual may borrow against his or her future earnings potential from an established, accredited commercial lending institution exclusively for the purpose of purchasing insurance (with no cash surrender value) against a disabling injury or illness that would prevent the individual from pursuing a chosen career or for the purpose of purchasing loss-of-value insurance, provided a third party (including a representative of an institution’s athletics interests) is not involved in arrangements for securing the loan.”). *See also* Glenn M. Wong et al., *Going Pro in Sports: Providing Guidance to Student-Athletes in a Complicated Legal & Regulatory Environment*, 28 CARDOZO ARTS & ENT. L.J. 553, 569 (2011).

45. *See* Wong et al., *supra* note 44, at 569 (discussing cost of premiums). *See also* Lens & Lens, *supra* note 38, at 145 (noting that the high cost of ESDI premiums equates to loans being necessary).

46. *See* 2017–18 NCAA MANUAL, *supra* note 19, at art. § 12.1.2.4.4 (“Exception for Insurance Against Disabling Injury or Illness, or Loss of Value”). *See also* Lens & Lens, *supra* note 38, at 153–57.

While the NCAA and private insurers offer disability insurance loans to qualifying elite student-athletes, some universities have chosen to pay the cost of these high premiums on behalf of their star athletes.⁴⁷ The NCAA allows schools to use the NCAA Student Assistance Fund (“SAF”) to purchase these policies on behalf of student-athletes.⁴⁸ As noted, Clemson purchased a \$5 million insurance policy to cover any career-ending injury that Deshaun Watson might have suffered while playing his final year at the university.⁴⁹

Whether university funds, student-athlete resources, or private loans are used to secure the price of ESDI premiums, this program provides some measure of financial security to those premier student-athletes interested in postponing their entry into the professional draft.⁵⁰ Approximately eighty to one hundred student-athletes participate in the ESDI program each year, of which 75% are considered first-round draft picks in the NFL and NBA.⁵¹ For top collegiate athletes in recent years including Johnny Manziel (Texas A&M), Jadaveon Clowney (University of South Carolina), and Andrew Luck (Stanford University), securing disability insurance policies to protect against career-ending injuries was critical in

47. See Joseph Stuart Knight, *Tackling Problems with the NCAA’s Exceptional Student-Athlete Disability Insurance Program*, 1 MISS. SPORTS L. REV. 157, 162 (2012) (noting that NCAA offers low interest rate loans to pay for premium). See also *Student Athlete Disability Insurance*, PETERSEN INT’L UNDERWRITERS, <https://www.piu.org/athlete-disability-insurance/draft-protection> [<https://perma.cc/ML85-E489>] (last visited Jan. 4, 2018) (providing disability coverage options for elite student-athletes).

48. See NCAA, *Loss-of-Value FAQs, How Can Coverage Be Paid for?*, <http://www.ncaa.org/about/resources/insurance/loss-value-faqs> [<https://perma.cc/6H7L-VXUJ>] (last visited Apr. 18, 2018).

49. See Mandrallius Robinson, *Clemson Buys \$5 Million Insurance Policy for Deshaun Watson*, GREENVILLE NEWS, <http://www.thestate.com/sports/college/acc/clemson-university/article96498222.html> [<https://perma.cc/C64Z-TD4C>] (last updated Aug. 19, 2016, 3:50 PM).

50. See, e.g., Mike Herndon, *NCAA Insurance Program Protects Elite Athletes, Future Earnings Against Injury*, AL (Aug. 1, 2010, 6:03 AM), http://www.al.com/sports/index.ssf/2010/08/are_you_in_good_hands.html [<https://perma.cc/U5PC-4P44>] (noting various student-athletes who have postponed their draft dates due to protection afforded by ESDI policies). See also Ross Dellenger, *Collins Invests in Insurance Policy; Peveto Contract Revealed*, ADVOC. (July 6, 2014, 5:43 PM), http://www.theadvocate.com/baton_rouge/sports/lsu/article_470a2f19-b439-5537-8fa9-98f60167d225.html [<https://perma.cc/X5JT-THJ8>] (discussing LSU left tackle La’el Collins’ decision to pass on NFL draft and return to LSU for his senior year due to insurance protection); Nick Ironside, *Irish’s Smith Takes Advantage of Insurance Options*, 247SPORTS (Jan. 5, 2016), <http://notredame.247sports.com/Article/Irish-Smith-takes-advantage-of-insurance-options-42575472> [<https://perma.cc/8462-5YX5>] (documenting Notre Dame players who have purchased ESDI insurance policies).

51. See Wong & Deubert, *supra* note 20, at 507–08.

protecting the possible loss of future professional-athlete income.⁵² Still, professionally-bound student-athletes who opt to stay in college an additional year are also likely to consider securing draft-protection (i.e., LOV) insurance in conjunction with ESDI in order to protect their professional draft stock.

B. Draft Protection Insurance Coverage

Draft protection, or LOV insurance, protects against the risk that a student-athlete's draft stock might decrease below a prescribed threshold following a non-career-ending injury sustained during college play.⁵³ These policies, which must be purchased in conjunction with ESDI coverage, specify how far a student-athlete must fall in the professional draft before coverage is triggered.⁵⁴ Per NCAA recommendations, only those student-athletes projected to be a top fifteen NFL draft pick should consider purchasing LOV insurance.⁵⁵ Coverage limits are based on a student-athlete's anticipated draft position, and generally range between \$1 million and \$10 million.⁵⁶

Unlike ESDI disability insurance, the NCAA does not provide LOV insurance.⁵⁷ Instead, draft protection must be secured through private insurers, with premiums ranging from \$10,000 to \$95,000.⁵⁸ Similar to ESDI policies, student-athletes who are unable to afford the high cost of LOV premiums are permitted to take out personal loans against their future earnings.⁵⁹ The NCAA also allows member institutions to use money from their SAF to purchase LOV premiums.⁶⁰

52. See Kevin Fixler, *The \$5 Million Question: Should College Athletes Buy Disability Insurance?*, ATLANTIC (Apr. 11, 2013), <https://www.theatlantic.com/entertainment/archive/2013/04/the-5-million-question-should-college-athletes-buy-disability-insurance/274915/>.

53. See Lens & Lens, *supra* note 38, at 141. See also Kain et al., *supra* note 13, at 218; *Loss-of-Value Insurance Information*, *supra* note 3.

54. See Lens & Lens, *supra* note 38, at 141. See also *Loss-of-Value White Paper*, NCAA <http://www.ncaa.org/about/resources/insurance/loss-value-white-paper> [<https://perma.cc/E56H-PTVR>] (last visited Jan. 4, 2018).

55. See Kain et al., *supra* note 13, at 221.

56. *Loss-of-Value White Paper*, *supra* note 54.

57. See Lens & Lens, *supra* note 38, at 142.

58. See *id.* See also *Loss-of-Value White Paper*, *supra* note 54 (noting that the private insurance company Lloyd's of London writes the majority of LOV policies for student-athletes); Kain et al., *supra* note 13, at 222 (providing data on LOV premium cost range).

59. See 2017–18 NCAA MANUAL, *supra* note 19, at art. § 16.11.1.4 (“Insurance Against Disabling-Injury or Illness, or Loss of Value”).

60. See Kain et al., *supra* note 13, at 222.

The use of the SAF to purchase ESDI and LOV premiums gives universities a competitive advantage in recruiting and retaining elite student-athletes who might otherwise leave college prior to graduation to enter the professional draft.⁶¹ However, use of the SAF to retain top student-athletes has been a debatable issue within the NCAA and among academics.⁶² Although coaches and elite student-athletes may applaud the use of the SAF as a hedge against losing star athletes to the professional realm due to a largely unaffordable insurance market, others argue that use of the SAF to cover expensive insurance premiums for a few takes away from the use of these funds for the benefit of all other student-athletes.⁶³ Still, no less than fourteen universities have used their SAF funds to purchase ESDI and LOV insurance policies for select student-athletes, making a strong statement that schools want to retain their top talent in the billion-dollar college sports industry.⁶⁴

Media outlets have reported that most participants who purchase LOV insurance policies rarely receive payouts after sustaining injuries.⁶⁵ The NCAA notes that “the flood of student-athletes currently seeking loss-of-value coverage and pending Lloyd’s lawsuits for denied claims will impact this tenuous marketplace.”⁶⁶ Most recently, in May 2017, former Penn State linebacker, Nyeem

61. *See id.* at 224.

62. *See id.* (noting that while certain NCAA collegiate executives have expressed discomfort in member institutions using SAF money to fund LOV premiums, college coaches have noted that use of SAF funds allows institutions to remain professionally bound elite student-athletes for additional season). *See also* Lens & Lens, *supra* note 38, at 163 (discussing negative ramifications of using SAF to pay for insurance premiums).

63. *See* Lens & Lens, *supra* note 38, at 163–64.

64. *Id.* at 162 n.171 (citing Darren Rovell, *Georgia Paid to Insure Todd Gurley*, ESPN (Oct. 12, 2014, 11:17 AM), http://www.espn.com/college-football/story/_/id/11682691/georgia-bulldogs-paid-more [<https://perma.cc/KA4X-6E9X>]). *See also* William W. Berry III, *Employee-Athletes, Antitrust, and the Future of College Sports*, 28 STAN. L. & POL’Y REV. 245, 253 (2017) (noting that men’s college basketball and football have become billion dollar industries).

65. *See, e.g.*, Darren Rovell, *College Football Insurance Policies Are Big—but Complex—Business*, ESPN (Aug. 17, 2016), http://www.espn.com/college-football/story/_/id/17328541/college-football-insurance-policies-big-complicated-business [<https://perma.cc/N8UG-366H>]. *But see* Darren Rovell, *Jake Butt to Collect on Loss-of-Value Policy Following Torn ACL*, ESPN (Apr. 29, 2017), http://www.espn.com/nfl/draft2017/story/_/id/19271765/jake-butt-collecting-loss-value-policy-reach-2-million [<https://perma.cc/2MNH-ESCQ>] (reporting that Jake Butt (University of Michigan (“UM”)), Ife Ekpre-Olomu (University of Oregon) and Jaylon Smith (University of Notre Dame (“ND”)) all reportedly have collected on LOV insurance policies after falling in professional draft due to injuries).

66. *Loss-of-Value White Paper*, *supra* note 54. *See also* Lee v. Certain Underwriters at Lloyd’s London, 2:15-cv-01614-ODW-JC (C.D. Cal. Mar. 4, 2015); Breslin v. Amtrust at Lloyd’s Ltd., 2:15-cv-00330-R-AS (C.D. Cal. Jan. 15, 2015); Breslin v. Univ. of S. Cal., No. BC592870 (Cal. App. Dep’t Super. Ct. Aug. 28, 2015).

Wartman-White, filed a lawsuit against International Specialty Insurance Co., claiming the insurance provider reneged on a disability policy after a knee injury caused him to drop from NFL draft contention altogether.⁶⁷ Due to the questionable payout history and mounting litigation surrounding LOV policies, the NCAA has purposefully avoided offering LOV insurance through its ESDI program, instead leaving coverage accessibility solely to private insurers.⁶⁸

Even amid mounting legal claims, elite student-athletes continue to secure both LOV and ESDI insurance policies to help protect against risk of injury that could end their professional careers or impact their draft stock. For programs such as Clemson, Texas A&M, and Florida State University that have the financial means to purchase policies on behalf of their star athletes, exercising this option better secures institutions' retention of elite players for an additional season.⁶⁹

One question resonating from the spectrum of universities using the SAF to cover ESDI and LOV insurance premiums is whether any resulting payouts are taxable as income to the student-athlete. Neither the IRC nor Treas. Regs. specifically address the tax consequences of insurance policy payouts received when the premiums are paid for by non-employers on behalf of beneficiaries in general. Further, to date there is no published IRS Revenue Ruling addressing the taxability of payouts when student-athletes are listed as the beneficiaries of policies purchased by their universities. Thus, one can only speculate how the IRS will treat these types of payouts. To address this inquiry, it is helpful to understand the broader scope of federal tax rules encompassing insurance policy payouts. The following section provides a brief analysis of the taxation of disability income insurance benefits in the United States.

III. DISABILITY INSURANCE PLANS AND THE INTERNAL REVENUE CODE

Understanding the umbrella of federal tax law as applies to disability insurance plans is an important step in analyzing the taxability of ESDI and LOV insurance policy payouts. Although there are prescribed benefits to purchasing disability insurance policies, it is essential to address the tax implications that could arise following a

67. See *Whartman v. Int'l Specialty Ins., Inc.*, No. 4:17-CV-00871-MEM (M.D. Pa., May 17, 2017).

68. See *Kain et al.*, *supra* note 13, at 233.

69. See *Tracy*, *supra* note 4.

benefit payout. Generally, the tax impact on disability benefits comes down to one main question: who pays the cost of the premium?⁷⁰

The IRC and accompanying Treas. Regs. do provide some guidance with respect to the taxability of insurance policy benefits. As a starting point for assessing the imposition of federal taxation, taxpayers must first determine the amount of their gross income.⁷¹ The term ‘gross income’ includes “all income from whatever source derived,” including compensation for services rendered for fringe benefits.⁷² The IRS includes employer-provided accident and health benefits within the spectrum of *fringe benefits*, although certain exclusions apply.⁷³

In 1943, following the initiation of health insurance coverage in the United States, the IRS ruled that employees were not required to include the value of health insurance premiums paid for by their employers in their taxable income.⁷⁴ Congress later codified this decision with the addition of IRC § 106, which allows an employee to exclude from their gross income the cost of the premium paid for accident or health coverage when their employer is the party that pays the premium.⁷⁵ As a result, an employer can provide any health insurance it chooses without including the costs associated with the insurance in the employee’s income, while also allowing the employer to deduct the cost of health insurance from their own federal income tax base.⁷⁶ This favorable codification ul-

70. *How Taxes Can Impact the Benefits You Choose*, PRINCIPAL FIN. SERVS., INC., <https://secure02.principal.com/publicvsupply/GetFile?fm=GP58784&ty=VOP&EXT=VOP> [<https://perma.cc/A5RA-QSFY>] (last visited Jan. 4, 2018).

71. See 26 U.S.C. § 61(a)(1) (2012). See also Jonathan Barry Forman & Roberta F. Mann, *Making the Internal Revenue Service Work*, 17 FLA. TAX REV. 725, 731 (2015) (denoting gross income as the starting point for calculating the federal income tax).

72. § 61(a)(1). See also DEP’T OF TREAS.: IRS, PUBL’N 15-B, EMPLOYER’S TAX GUIDE TO FRINGE BENEFITS 5 (2018) [hereinafter IRS, *Publ’n 15-B*], available at <https://www.irs.gov/pub/irs-pdf/p15b.pdf> [<https://perma.cc/ZV3U-QKLL>]. A fringe benefit is a form of pay for the performance of services, and includes items such as an employer-provided automobile, a flight on an employer-provided aircraft, and an employer-provided membership in a country club. Treas. Reg. § 1.61-21(a)(3) (2017).

73. See IRS, *Publ’n 15-B*, *supra* note 72. See also 26 U.S.C. § 61(a)(1).

74. See Richard L. Kaplan & Dawson J. Price, *Change and Continuity in Fringe Benefit Taxation: Seeking Sense and Sensibility*, 59 N.Y.L. SCH. L. REV. 285, 292 (2014–2015). See also SPEC. RUL. 433 STANDARD FED. TAX SERV. CCH 6587 (Nov. 24, 1943).

75. See 26 U.S.C. § 106(a). See also Treas. Reg. § 1.106-1.

76. See Richard L. Kaplan, *Who’s Afraid of Personal Responsibility? Health Savings Accounts and the Future of American Health Care*, 36 MCGEORGE L. REV. 535, 543–44 (2005). See also 26 U.S.C. § 162(a)(1).

timately led to the development of widespread health insurance policies across the nation, as well as the predominant practice of employees participating in employer-sponsored insurance plans.⁷⁷

Another provision that excludes the taxation of health benefits is IRC § 104.⁷⁸ Section 104 exempts from gross income damages received due to personal injuries, unless those amounts are either paid for by an employer or are attributable to pre-tax employee contributions.⁷⁹ The key to understanding the foundation of IRC § 104 is identifying who pays for the coverage—the individual or their employer. Thus, self-employed persons and those who pay for health insurance in an individual capacity qualify for the more favorable tax treatment under IRC § 104, while distributions made from policies paid for by an employer do not qualify for the tax exclusion.⁸⁰

Treas. Reg. section 1.410(b)-9 only generically defines the term ‘employer’ as “the employer maintaining the plan,” making it unclear as to who qualifies as an employer for IRC § 104 purposes in the first place.⁸¹ However, if the sole contributor to an accident or health insurance policy is identified as an employer (however defined), or is the sole purchaser of the policy paid for on behalf of their employees, the tax exclusion allowed under IRC § 104 is unavailable.⁸² For instance, if an identified employer contributes \$1X per month to a disability plan and an employee later becomes disabled, receiving \$3X per month under the terms of the insurance policy, the entire \$3X per month must be included in the individual’s gross income under IRC § 104 because the employer was the sole contributor to the plan.⁸³

77. See Kaplan & Price, *supra* note 74, at 293.

78. See 26 U.S.C. § 104.

79. See *id.* § 104(a)(3). See also Treas. Reg. § 1.104-1(d); Robert W. Wood, *Are Insurance Bad Faith Recoveries Taxable?*, 53 ARIZ. ATT’Y 26, 30 (2017). The exclusion is premised on the requirement that coverage be purchased using after-tax dollars. ‘After-tax dollars’ is defined as the amount of money that an individual “has left over after all federal, state and withholding taxes have been deducted from taxable income.” *After-Tax Income*, INVESTOPEDIA, <http://www.investopedia.com/terms/a/aftertaxincome.asp?lgl=myfinance-layout-no-ads> [https://perma.cc/4TXB-PWAJ] (last visited Jan. 4, 2018).

80. See 26 U.S.C. § 104(a)(3).

81. Treas. Reg. § 1.410(b)-9.

82. Treas. Reg. § 1.104-1(d). If the employer and their employees each contribute to a fund or purchase insurance which pays accident or health benefits to employees, IRC § 104(a)(3) does not apply to amounts received by employees to the extent that such amounts are attributable to the employer’s contributions. *Id.*

83. Although the payout benefit is taxable to the employee in this instance, it should be noted that the cost of health care is less expensive for taxpayers when it is provided through their employer because it is paid with pre-tax dollars. See

Although amounts paid for by or on behalf of an employer for personal injury or sickness are not excludable from the employee's gross income under IRC § 104, they may be excludable under IRC § 105.⁸⁴ Section 105 reiterates the general rule that any amounts received by an employee through an employer-sponsored health or accident plan for personal injury are includable in the employee's gross income.⁸⁵ Receipt of disability payouts is therefore included in the gross income of an employee if their employer paid for all or part of the coverage premium on behalf of the injured person.⁸⁶ However, an important exclusion to this provision exists within IRC § 105(b) and (c), which allows taxpayers to exclude benefits they receive from employer financed accident or health plans for purposes of medical care and "permanent loss or loss of use of a member or function of the body" (i.e. disability) payments.⁸⁷

Treas. Reg. section 1.105-1 provides several examples to illustrate the taxability of amounts attributable to employer contributions under IRC § 105.⁸⁸ Outside the parameters of the IRC § 105(b) and (c) exclusions, if an employer maintains an accident or health plan where employees make no contributions to the plan and all benefits are paid by the employer (referred to as a noncontributory plan), any amounts received under such plan are includable in the employees' gross income.⁸⁹ Alternatively, if the annual premium for employee X is \$24, of which \$16 is paid by the employer, then 16/24 (or two-thirds) of all amounts received by X under the policy are subject to IRC § 105(a), while 8/24 (or one third) of the remaining amounts received are excludable from X's gross income under IRC § 104(a)(3).⁹⁰

Analyzing the taxability of disability insurance payouts under the entire framework of IRC §§ 104, 105, and 106 also requires an identification of whether insurance premiums are paid with pre-tax or post-tax dollars.⁹¹ If a taxpayer pays for the premium of a disability insurance policy using after-tax dollars, any benefits received are

Daniela De La Torre, Comment, *The Affordable Care Act: The Replacement for the Employer Sponsored Health Insurance Tax Exclusion*, 18 DUQ. BUS. L.J. 1, 6 (2016). Further note that "X" in the textual example represents any number of zeros.

84. See Treas. Reg. § 1.104-1(d). See generally 26 U.S.C. § 105.

85. 26 U.S.C. § 105(a). See also Treas. Reg. § 1.105-1(a).

86. 26 U.S.C. § 105(a). See also Treas. Reg. § 1.105-1(b)-(c).

87. 26 U.S.C. § 105(c). See also *id.* § 105(b). The term "medical care" is defined in 26 U.S.C. § 213(d).

88. See generally Treas. Reg. § 1.105-1.

89. See Treas. Reg. § 1.105-1(b), Example 1.

90. See *id.* § 1.105-1(d)(1).

91. See 26 U.S.C. § 104(a)(3).

excludable from gross income.⁹² Instead, if a taxpayer pays for the premium using pre-tax dollars, any benefits received are taxable.⁹³

Finally, if the cost of the insurance premium is split between an employer and employee, the portion of the benefit received relating to the employer-contribution will be taxable, while the tax consequences of the share of the benefit received relating to the employee-contribution will depend on whether the premium was paid using pre-tax or after-tax dollars.⁹⁴ Thus, in a hypothetical scenario where an employer contributes 60% towards an accident or health insurance policy premium and employee X contributes 40%, \$60 of any \$100 benefit received will be includable in the employee's gross income.⁹⁵ If employee X contributed to the premium using pre-tax dollars, the remaining \$40 is includable in gross income. However, if employee X contributed to the premium using after-tax dollars, then the \$40 will be tax-free.

The following chart attempts to summarize the general taxability of disability benefit rules as applicable under the IRC:⁹⁶

92. *See id.*

93. *See id.* Pre-tax dollars refers to the scenario where deductions are taken off an individual's gross income before income taxes are paid, resulting in taxes being calculated at a reduced salary. *See, e.g., What Does It Mean When You Have Pre-Tax Dollar Insurance Premiums Deducted from Your Pay*, EXTENSION (Nov. 26, 2013), <http://articles.extension.org/pages/42694/what-does-it-mean-when-you-have-pre-tax-dollar-health-insurance-premiums-deducted-from-your-pay> [<https://perma.cc/6E76-MWLC>] ("When you pay for benefits such as health insurance with pre-tax (also called before-tax) dollars, the deductions are taken off your gross income before income taxes are paid. Taxes are then calculated on the reduced salary amount. Having pre-tax dollar deductions results in less income tax paid than would otherwise be the case.").

94. *See* 26 U.S.C. § 104(a)(3); Treas. Reg. § 1.105-1(c)(1) ("In the case of amounts received by an employee through an accident or health plan which is financed partially by his employer and partially by contributions of the employee, section 105(a) applies to the extent that such amounts are attributable to contributions of the employer which were not includible in the employee's gross income.").

95. *See* Treas. Reg. § 1.105-1(c)(1).

96. *See* STANDARD INS. CO., GUIDE TO TAXATION OF EMPLOYEE DISABILITY BENEFITS 2 available at <https://www.standard.com/eforms/8461.pdf> [<https://perma.cc/8L7U-VR2U>] (last visited Jan. 4, 2018).

Payor of the Premium	Pre- or Post-Tax Dollars	Taxability of Benefit Received by Taxpayer	Percent of Benefit Taxable to Taxpayer
Employer	————	Taxable	100%
Split Between Employer & Employee	After-Tax Dollars (Employee)	Taxable	% of premium contributed by Employer (% of premium contributed by employee is tax-free)
Split Between Employer & Employee	Pre-Tax Dollars (Employee)	Taxable	100%
Individual	After-Tax Dollars	Not Taxable	0%
Individual	Pre-Tax Dollars	Taxable	100%

Based on the rules as outlined in the IRC and Treas. Regs. regarding the taxability of disability insurance plans, a legitimate question is how the IRS might categorize benefits received by student-athletes under ESDI or LOV insurance policy payouts. To date, the IRS has been reluctant to impose taxes on student-athletes and, to a great degree, on the college sports industry in general.⁹⁷ There is also no question that college athletic programs have a vested interest in protecting elite student-athletes and keeping them on the amateur playing field to help bolster program revenue. Analyzing the taxability of ESDI and LOV insurance premium payouts could prompt broader policy discussions among academic scholars in what is currently an under-theorized legal area. Therefore, a discussion regarding the IRS's historical stance on taxing student-athletes and the college sports industry, the national dialog over whether student-athletes should be paid to play, and the overlying quandary surrounding the movement toward the professionalization of college sports is helpful in gauging future policy solutions for taxing ESDI and LOV payouts.

97. See KOSKINEN, *supra* note 11.

IV. TAX POLICY IN THE BILLION DOLLAR COLLEGE SPORTS INDUSTRY

Academic literature has suggested that there can be “[n]othing . . . more professional than big-time college football and basketball teams.”⁹⁸ This sentiment is not without merit—it is estimated that the college sports industry generates more than \$11 billion in revenue annually based on “ticket sales, merchandise, sponsorships, and broadcasting rights.”⁹⁹ Even the NCAA, a non-profit organization under the federal tax laws, earned almost \$1 billion in revenue during its 2014 fiscal year.¹⁰⁰ However, the basic tenet of the NCAA continues to be the promotion and preservation of amateurism in college sports.¹⁰¹ Thus, any movement toward professionalization at the collegiate level would be hugely inconsistent with the ideal of the “student-athlete.”¹⁰²

Still, the debate over the movement to professionalize the college sports industry has gained traction in the past decade, prompting a volume of academic scholars weighing in on the pay-for-play model.¹⁰³ Simultaneously, recent litigation encompassing anticom-

98. See, e.g., Erik M. Jensen, *Taxation, the Student Athlete, and the Professionalization of College Athletics*, 1 UTAH L. REV. 35, 35 (1987).

99. See Marc Edelman, *From Student-Athletes to Employee-Athletes: Why a “Pay for Play” Model of College Sports Would Not Necessarily Make Educational Scholarships Taxable*, 58 B.C.L. REV. 1137, 1141 (2017); Kyle Obly, *It Is Time for NCAA Student-Athletes to Be Paid*, GAMBIT (Oct. 3, 2017), <http://auroragambit.wixsite.com/gambit/single-post/2017/10/03/It-is-time-for-NCAA-student-athletes-to-be-paid> [https://perma.cc/DCW8-EATD] (noting the reasoning behind the \$11 billion estimate).

100. See Steve Berkowitz, *NCAA Nearly Topped \$1 Billion in Revenue in 2014*, USA TODAY (Mar. 11, 2015), <https://www.usatoday.com/story/sports/college/2015/03/11/ncaa-financial-statement-2014-1-billion-revenue/70161386/> [https://perma.cc/H6XC-86QQ].

101. See 2017–18 NCAA MANUAL, *supra* note 19, at art. § 2.9 (“The Principle of Amateurism”).

102. See Jensen, *supra* note 98, at 36.

103. See, e.g., Christian Dennie, *He Shoots, He Scores: An Analysis of O’Bannon v. NCAA on Appeal and the Future of Intercollegiate Sports*, 93 N.C.L. REV. 90 (2015) (positing arguments about future of college sports following *O’Bannon* case); Roger M. Groves, *A Solution for the Pay for Play Dilemma of College Athletes: A Novel Compensation Structure Tethered to Amateurism and Education*, 17 TEX. REV. ENT. & SPORTS L. 101 (2016) (offering the creation of new NCAA rules that are consistent with the *O’Bannon* decision); Kathryn Kisska-Schulze & Adam Epstein, *Northwestern, O’Bannon, and the Future: Cultivating a New Era for Taxing Qualified Scholarships*, 49 AKRON L. REV. 771 (2016) (analyzing the possibility of taxing qualified scholarships should student-athletes be deemed employees of their universities); Josephine R. Potuto et al., *What’s in a Name? The Collegiate Mark, the Collegiate Model, and the Treatment of Student-Athletes*, 92 OR. L. REV. 879 (2014) (analyzing the movement from amateurism to professionalism in college sports); Joseph Davison, Note, *Throwing the Flag on Pay-for-Play: The O’Bannon Ruling and the Future of Paid Student-Athletes*, 11 WASH. J.L. TECH. & ARTS 155 (2015) (analyzing the impact of recent litigation on the premise of amateurism in college sports).

petitive behaviors, unionization efforts, and antitrust lawsuits have further capitalized on the running campaign that student-athletes should be given the opportunity to rise above their current amateur status.¹⁰⁴ Certainly, the metamorphosis from “amateur” athletics into a more professional-yet-collegiate model would not occur without considering the possible tax ramifications.¹⁰⁵

As mentioned, the IRS has been reluctant to impose income taxes on student-athletes with respect to their athletic scholarships, more formally known as athletic “grants-in-aid.”¹⁰⁶ Further, the college sports industry in general has enjoyed strikingly favorable tax positions over the past decades due to the tax-exempt status of colleges, athletic departments, and the NCAA itself.¹⁰⁷ Such historical protection could play an important role in identifying the potential tax effects of ESDI and LOV insurance policy payouts moving forward.

In conjunction, a slew of court decisions over the past sixty years have generally supported the notion that student-athletes are not yet considered employees of their institutions.¹⁰⁸ This distinction could also play a part in understanding the application of the IRC and Treas. Regs. to disability insurance policy payouts received by student-athletes. As such, this section provides a brief synopsis of

104. For examples of litigation concerning anticompetitive behavior, see *O'Bannon v. Nat'l Collegiate Athletic Ass'n*, 802 F.3d 1049 (9th Cir. 2015), and *In re NCAA Student-Athlete Name & Likeness Licensing Litig.*, 37 F. Supp. 3d 1126 (N.D. Cal. 2014). For an example of unionization efforts, see *Nw. Univ. Employer & Coll. Athletes Players Ass'n*, 13-RC-121359 (N.L.R.B.) (Mar. 26, 2014), *rev. dismissed* *Nw. Univ. Employer & College Athletes Players Ass'n*, 362 NLRB No. 167, 2-3, (Aug. 17, 2015). In February 2017, the NCAA and 11 major athletic conferences agreed to pay \$208.7 million to settle a federal class-action lawsuit filed by former college athletes who claimed the value of their scholarships was illegally capped. See Jon Solomon, *NCAA, Conferences Agree to Pay \$208.7 Million in Cost of Attendance Settlement*, CBS SPORTS (Feb. 4, 2017), <https://www.cbssports.com/college-football/news/ncaa-conferences-agree-to-pay-208-7-million-in-cost-of-attendance-settlement/> [<https://perma.cc/M65F-CUD2>].

105. See Jensen, *supra* note 98, at 37 (noting that the creation of an openly professional athletic team would have federal income tax consequences). See also Kathryn Kisska-Schulze & Adam Esptein, “*Show Me the Money!*”—*Analyzing the Potential State Tax Implications of Paying Student-Athletes*, 14 VA. SPORTS & ENT. L.J. 13 (2014) (documenting potential state tax implications of paying student-athletes).

106. See Gary C. Randall, *Athletic Scholarship and Taxes: Or a Touchdown in Taxes*, 7 GONZ. L. REV. 297, 299 (1972).

107. See Jensen, *supra* note 98, at 51 (noting that college sports hold “an exalted tax position”). See also William A. Drennan, *Taxing Commercial Sponsorships of College Athletics: A Balanced Approach*, 73 OHIO ST. L.J. 1353, 1373 (2012) (discussing that tax law has treated nonprofit athletic organizations and college athletic programs as being “integral part[s] of the tax-exempt college”).

108. For further discussion of court decisions regarding student-athletes’ status (or lack thereof) as employees, see *infra* notes 157–163.

(a) the IRS's historical reluctance to impose taxes on student-athletes and the college sports industry in general, and (b) the mounting litigation to characterize big-time college sports as professional rather than amateur.

A. IRS's Historical Reluctance to Tax the College Sports Industry

In 1954, Congress enacted IRC § 117 which governs the rules pertaining to taxing qualified scholarships.¹⁰⁹ A qualified scholarship includes “amount[s] received by an individual as a scholarship or fellowship grant” so long as the funds are “used for qualified tuition and related expenses.”¹¹⁰ Section 117 allows that any amount received as a qualified scholarship by an individual is excludable from gross income if that individual is a candidate for a degree at a qualified educational organization.¹¹¹ In general, qualified scholarships do *not* include amounts for incidental expenses including room, board, travel, and research.¹¹²

The IRC § 117 exclusion does not apply to amounts representing payments for teaching, research, or other services required as a condition of a student's scholarship.¹¹³ The U.S. Supreme Court held that any quid pro quo condition required in exchange for the receipt of scholarship or grant funds triggers a taxable event.¹¹⁴ In the landmark case *Bingler v. Johnson*,¹¹⁵ two Ph.D. students participated in a fellowship program that required both work-study and research obligations in exchange for receiving stipends.¹¹⁶ The Court, finding these stipends to be taxable, held that students who provide services in exchange for scholarship funds must include such amounts in their gross income.¹¹⁷

109. See 26 U.S.C. § 117. See also Kisska-Schulze & Epstein, *supra* note 103, at 782.

110. 26 U.S.C. § 117(b)(1). See also Treas. Reg. § 1.117-3(a). Qualified tuition and related expenses include “tuition . . . fees, books, supplies, and equipment” that are required in the specified course of instruction. 26 U.S.C. § 117(b)(2)(A)–(B).

111. See 26 U.S.C. § 117. See also Treas. Reg. § 1.117-1.

112. Treas. Reg. § 1.117-5(c)(1)(ii).

113. 26 U.S.C. § 117(c)(1).

114. *Bingler v. Johnson*, 394 U.S. 741, 757–58 (1969).

115. 394 U.S. 741 (1969).

116. See *id.* at 742–44.

117. See *id.* at 758 n.32 (finding that payments cannot be scholarships “where the recipient receives money, and in return provides a quid pro quo”).

The application of IRC § 117 has also been analyzed by the U.S. Tax Court multiple times.¹¹⁸ In *Bonn v. Commissioner*,¹¹⁹ the court held that funds received by a physician in exchange for services rendered to a Veterans Administration hospital under a fellowship program constituted taxable compensation for services rather than a fellowship grant.¹²⁰ Later, in *Zolnay v. Commissioner*,¹²¹ the U.S. Tax Court held that monthly payments received by a Ph.D. candidate who worked forty hours a week as a research assistant for the Ohio State University while being subject to supervision, planned schedules, and regular progress reports were taxable as compensation for services rendered rather than a fellowship excludable under IRC § 117.¹²² In *Proskey v. Commissioner*,¹²³ the Tax Court sustained a decision that a stipend received by a resident physician in exchange for his supervisory role over medical students, interns, and residents constituted taxable compensation for services rendered to the hospital.¹²⁴

In contrast, in *Smith v. Commissioner*,¹²⁵ the Tax Court found that funds received by a graduate assistant while completing her master's degree constituted a scholarship or fellowship grant.¹²⁶ This case is distinguishable from the court's prior cases in that the petitioner only studied during the funding period; the university granting the funds received no direct benefit from her research nor imposed any requirement that she teach or conduct university research projects or publish any findings during the period at issue.¹²⁷

118. See, e.g., *Smith v. Comm'r*, 51 T.C.M. (CCH) 1348 (1986); *Proskey v. Comm'r*, 51 T.C. 918 (1969); *Zolnay v. Comm'r*, 49 T.C. 389, 399 (1968); *Bonn v. Comm'r*, 34 T.C. 64 (1960).

119. 34 T.C. 64 (1960).

120. See *Kisska-Schulze & Epstein*, *supra* note 103, at 787–88. See also *Bonn*, 34 T.C. at 64–66, 73 (finding that the Veterans Administration hospital existed primarily for patient care, and that the fellowship program's adoption of a trainee program—which petitioner participated in—was incidental to the care and treatment of patients).

121. 49 T.C. 389 (1968).

122. *Id.* at 397–99.

123. 51 T.C. 918 (1969).

124. See *Kisska-Schulze & Epstein*, *supra* note 103, at 788. See also *Proskey*, 51 T.C. at 919–22 (finding as compensation for employment services—not a fellowship grant—when petitioner received annual stipends during his medical residency based on the number of years of service he provided as a resident. In return, petitioner supervised medical students, interns, and assistant residents. The U.S. Tax Court upheld this decision).

125. 51 T.C.M. (CCH) 1348 (1986).

126. See *Kisska-Schulze & Epstein*, *supra* note 103, at 789. See also *Smith*, 51 T.C.M. (CCH) at 1348.

127. *Smith*, 51 T.C.M. (CCH) at 1350.

Although the U.S. Supreme Court and Tax Court have applied the *quid pro quo* condition within the spectrum of research assistants and fellowship recipients for IRC § 117 purposes, such adherence has historically been dealt with differently for student-athletes receiving qualified scholarships.¹²⁸ In 1977, the IRS issued Revenue Ruling 77-263, which excludes athletic scholarships from the strict *quid pro quo* limitation of IRC § 117(c) because “the benefit to the university was incidental and the primary purpose of collegiate sports was educational.”¹²⁹ However, Revenue Ruling 77-263 is unclear and confusing. For example, it does impose the restriction that universities may not require student-athletes to participate in sports or other activities as a condition of receiving scholarship funds, and that universities may not cancel scholarships on the basis of student-athletes not participating in their sports.¹³⁰ In reality, when a student-athlete receives an athletic scholarship from an institution, it is a naturally expected, outright condition that the student-athlete participate in the sport itself unless the student-athlete voluntarily withdraws from the sport for personal reasons, provides fraudulent information to the school, engages in “serious misconduct,” or violates a condition of the financial aid agreement or policy of the school.¹³¹ The 1977 Revenue Ruling further provides that the value of an athletic scholarship “may not exceed expenses for tuition, fees, room, board and necessary supplies”¹³² Such language provides a broader exclusion than that generally afforded by the applicable Section 117 Treas. Reg. which does not allow for the exclusion of room and board costs from a scholarship recipient’s gross income.¹³³

Forty years later, the IRS has yet to challenge or re-examine its own tax treatment of athletic scholarships.¹³⁴ The only documenta-

128. See Jake Linford, *The Kidney Donor Scholarship Act: How College Scholarships Can Provide Financial Incentives for Kidney Donation While Preserving Altruistic Meaning*, 2 ST. LOUIS U.J. HEALTH L. & POL’Y. 265, 302 (2009).

129. See Rev. Rul. 77-263, 1977-2 C.B. 47, 1977 WL 43568 (1977); Justin Morehouse, *When Play Becomes Work: Are College Athletes Employees?*, TAX ANALYSTS (Sept. 22, 2014), <http://www.taxanalysts.org/content/when-play-becomes-work-are-college-athletes-employees> [https://perma.cc/6B8F-XXCE].

130. Rev. Rul. 77-263, 1977 WL 43568, at *1.

131. See 2017–18 NCAA MANUAL, *supra* note 19, at art. § 15.3.5.1 (“Reduction, Cancellation or Nonrenewal Permitted”).

132. Rev. Rul. 77-263, 1977 WL 43568, at *1. This “cap” enunciated by the 1977 Revenue Ruling is not entirely consistent given the holding in the noteworthy 2015 court decision in *O’ Bannon v. Nat’l Collegiate Athletic Ass’n*, 802 F.3d 1049 (9th Cir. 2015) that now allows cost of attendance (“COA”) payments to be paid to student-athletes above their athletic scholarships, discussed further *infra*.

133. See Treas. Reg. § 1.117-5(c)(1)(ii).

134. See Morehouse, *supra* note 129.

tion to come forward since the issuance of Revenue Ruling 77-263 regarding the federal tax treatment of athletic grants-in-aid is a 2014 letter from then IRS Commissioner, John A. Koskinen, to Senator Richard Burr (R-NC) rearticulating the agency's stance that athletic scholarships qualify for exclusion from gross income outside the exact spectrum of quid pro quo.¹³⁵ Legal scholars and commentators have argued that a quid pro quo relationship does in fact exist between universities and their student-athletes, but the IRS has not moved to participate in this discussion.¹³⁶ Thus, unless there is a clear-cut change in IRS policy, it remains stable that student-athletes will continue to enjoy highly favorable tax treatment by the IRS with respect to their scholarship funds moving forward and that athletic scholarships will continue to be non-taxable at the federal level.

Similarly, the college athletics arena in general has received amicable tax treatment by the IRS. Universities do "not pay federal tax on tuition and other income attributable to its educational activities."¹³⁷ Instead, colleges are taxed only on their unrelated business income ("UBI"), which is income from a trade or business that is carried on regularly, but is not "substantially related" to the institution's primary purpose.¹³⁸ As the primary purpose of a university is to educate students, institutions have successfully maintained their tax-exempt statuses with regard to their college athletic pro-

135. See KOSKINEN, *supra* note 11.

136. See, e.g., Randall, *supra* note 106 at 299–309 (1972) (arguing that athletic scholarships should be taxable under the Internal Revenue Code); Adam Hoeflich, Note, *The Taxation of Athletic Scholarships: A Problem of Consistency*, 1991 U. ILL. L. REV. 581 (1991) (examining the quid pro quo application to athletic scholarships); Thomas R. Hurst & J. Grier Pressly III, *Payment of Student-Athletes: Legal & Practical Obstacles*, 7 VILL. SPORTS & ENT. L. J. 55, 74 (2000) (noting that student-athletes are required to perform athletic services in exchange for scholarship money); and Daniel Nestel, Note, *Athletic scholarships: An Imbalance of Power Between the University and the Student-Athlete*, 53 OHIO ST. L. J. 1401, 1413 (1992) (providing that athletic scholarships create a quid pro quo relationship).

137. Jensen, *supra* note 98, at 44. But see TAX CUTS AND JOBS ACT, H.R. 1, 115th Cong. (2017–2018), which became Public Law No. 115-97 on Dec. 22, 2017. H.R. 1 will impact higher education, to include imposing a 21% excise tax on non-profit organization salaries in excess of \$1 million dollars per year if those salaries belong to any of the organization's five highest paid employees, including college football coaches. *Id.*

138. See Jensen, *supra* note 98, at 45, 47. An activity is an unrelated business (and thus subject to the unrelated business income tax) if it is: (1) a trade or business, (2) regularly carried on, and (3) not substantially related to the institution's exempt purpose. *Id.* at 45 (citing 26 U.S.C. § 512(a)(1)). See also Jeff K. Brown, *Issues Facing College Athletics: Compensation for the Student-Athlete: Preservation of Amateurism*, 5 KAN. J.L. & PUB. POL'Y 147, 150 (1996). See generally 26 U.S.C. §§ 511(a); 513(a).

grams.¹³⁹ In 1976, Congress passed an amendment to IRC § 501(c), which declared the fostering of “national or international amateur sports competition” as a charitable purpose.¹⁴⁰ Later, in 1983, the Tenth Circuit upheld a U.S. Tax Court decision finding that “the furtherance of recreational and amateur sports” continues to be a charitable activity.¹⁴¹

However, one year after Congress’s amendment to the IRC, the IRS attempted to impose a tax on revenue from radio and broadcasting rights from college bowl games based on the concept that such revenue was UBI.¹⁴² This divisive position was met with heavy opposition, and following intense protests, the IRS reversed its stance by issuing numerous technical advice memoranda stating it would not impose a UBI tax on revenue from broadcasting rights as it determined there is “no meaningful distinction between exhibiting the game in person to 100,000 people and exhibiting the game on television to a much larger audience.”¹⁴³ The IRS further highlighted the interconnection between college athletics and education, noting, “[a]n audience for a game may contribute importantly to the education of the student-athlete . . . and to the education of the student body and the community at large”¹⁴⁴

In 1991, the IRS again published a highly-debated technical advice memorandum (referred to as the “Mobil Cotton Bowl Letter”), imposing a tax on corporate sponsorship income received by tax-exempt organizations.¹⁴⁵ The memorandum stemmed from the IRS’s interest in sponsorship payments received by the Cotton Bowl

139. See Christopher W. Haden, *Foul! The Exploitation of the Student-Athlete: Student-Athletes Deserve Compensation for Their Play in the College Athletic Arena*, 30 J.L. & EDUC. 673, 678 (2001).

140. TAX REFORM ACT OF 1976, Pub. L. No. 94-455, § 1313(a), 90 Stat. 1520, 1730 (codified as amended at 26 U.S.C. § 501(c)(3)).

141. *Hutchinson Baseball Enters. v. Comm’r*, 696 F.2d 757, 762 (10th Cir. 1982).

142. See Jensen, *supra* note 98, at 51 (citing Bruce R. Hopkins, *THE LAW OF TAX-EXEMPT ORGS.*, APP. A., 887–88 (6th ed. 1992)). The subject of the subsequent IRS technical advice memorandum was the Cotton Bowl, hosted by the Cotton Bowl Athletic Association. See Nathan Wirtschafter, Comment, *Fourth Quarter Choke: How the IRS Blew the Corporate Sponsorship Game*, 27 LOY. L.A.L. REV. 1465, 1472–73 (1994).

143. *Id.* (citing I.R.S. Tech. Adv. Mem. 78-51-002; 78-51-004 (Aug. 21, 1978); 78-51-006). Two similar Revenue Rulings were also published in 1980. See Rev. Rul. 80-295, 1980-2 C.B. 194, 1980 WL 130283 (1980); Rev. Rul. 80-296, 1980-2 C.B. 195 (1980).

144. I.R.S. Tech. Adv. Mem. 78-51-004 (Aug. 21, 1978). See also Brown, *supra* note 138, at 151.

145. See I.R.S. Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991). The Technical Advice Memoranda was primarily directed at the Cotton Bowl Athletic Association.

Athletic Association from Mobil Corporation, one of its major corporate sponsors.¹⁴⁶ Following a barrage of letters to the IRS and Congressional lobbying after the publication of the memorandum, in 1993, the IRS once again changed its stance, issuing proposed Treas. Regs. granting significant leniency to corporate sponsorship¹⁴⁷

Similar to colleges and universities, the NCAA also garners great tax immunity.¹⁴⁸ With a membership exceeding 1,100 institutions, even the U.S. Supreme Court has recognized that virtually all public and private universities which conduct major athletic programs in the U.S. belong to the NCAA.¹⁴⁹ Like private universities, the NCAA relies on its tax-exempt status as an IRC § 501(c)(3) organization to maintain its favorable tax treatment with the IRS.¹⁵⁰ For years academic scholars have questioned how a billion dollar entity can continue to be recognized as a tax-exempt organization.¹⁵¹ Even Congress in 2006 demanded that the NCAA justify its position as a not-for-profit organization.¹⁵² Still, to date the NCAA has successfully defended its favorable tax status.¹⁵³

The above examples paint a history of the IRS's reluctance to tax student-athletes on their grants-in-aid, and the successful efforts by the college sports industry to maintain generally favorable tax treatment. Such rich history could ultimately influence the IRS's decision as to whether it should even consider taxing ESDI and LOV insurance policy payouts made to injured student-athletes in the future. Still, the growing movement to professionalize college sports in the U.S. continues to gain traction and attention. This movement, which exploded in the media in recent years due to

146. See Frank James Vari, *The Unrelated Business Income Tax and Its Effect upon Collegiate Athletics*, 9 AKRON TAX J. 111, 111 (1992).

147. See Wirtschafter, *supra* note 142, at 1466–67. See also Prop. Treas. Reg. § 1.513-4 (1983).

148. See John D. Columbo, *The NCAA, Tax Exemption, and College Athletics*, 2010 U. ILL. L. REV. 109, 133 (2010).

149. See W. Burlett Carter, *Student-Athlete Welfare in a Restructured NCAA*, 2 VA. J. SPORTS & L. 1, 6 (2000) (citing *NCAA v. Smith*, 525 U.S. 459 (1999); *NCAA v. Tarkanian*, 488 U.S. 179, 183 (1988)).

150. See Columbo, *supra* note 148, at 113.

151. See, e.g., Amy C. McCormick & Robert A. McCormick, *The Emperor's New Clothes: Lifting the NCAA's Veil of Amateurism*, 45 SAN DIEGO L. REV. 495 (2008); Amanda Pintaro, *Is the NCAA Fulfilling Its Tax-Exempt Status?*, ILL. BUS. L.J. (2010).

152. See Columbo, *supra* note 148, at 110.

153. See Elia Powers, *The NCAA Responds*, INSIDE HIGHER ED (Nov. 16, 2006), <https://www.insidehighered.com/news/2006/11/16/ncaa> [<https://perma.cc/894T-XYCY>] (referencing to the twenty-five page response drafted by Myles Brand, then-President of the NCAA) to Capitol Hill defending the NCAA's status as a tax-exempt organization).

multiple legal actions being filed by former and current student-athletes, could ultimately prompt a closer examination by the IRS as to the taxability of the college sports industry as a whole. Thus, a brief history of the evolution of attempts to professionalize college sports by characterizing student-athletes as *employees* and their universities as *employers* should be considered when evaluating how the IRS could treat ESDI and LOV payouts moving forward.

B. The Mounting Litigation to Professionalize College Athletics

The conflict that exists between the educational archetype that embraces the “student” in the NCAA’s ideal of student-athlete, and the realities of college football and basketball is not a recent anomaly.¹⁵⁴ Studies have found that a student-athlete’s personal salient identity as being identified as an athlete first during their college career is largely influenced by the proportion of time spent with coaches, teammates, and others in the athletic arena.¹⁵⁵ Additionally, the increasing gap between student-athletes and the educational side of their institutions stems from the enormous revenue that universities generate from their athletic departments.¹⁵⁶ The growing divide has prompted litigation for more than six decades querying whether student-athletes should be treated as employees of their universities.¹⁵⁷

The earliest cases addressing the employer-employee characterization of student-athletes arose almost entirely within the context of state workers’ compensation claims.¹⁵⁸ In *University of Denver v. Nemeth*,¹⁵⁹ a Colorado court held that a college football player who was also employed and compensated by the university in exchange for his participation on the football team qualified for work-

154. See Jensen, *supra* note 98, at 39.

155. See Lydia F. Bell, *Examining Academic Role-Set Influence on the Student-Athlete*, J. ISSUES IN INTERCOLLEGIATE ATHLETICS 19, 22 (2009), http://csri-jiiia.org/old/documents/publications/special_issues/2009/sp_02_Making_of_the_Athlete-Student.pdf [<https://perma.cc/C9MZ-BFMV>] (analyzing the role of salience in student-athletes, and offering that a quarterback who becomes a campus hero after leading a team to victory in a championship game may see ‘athlete’ as his most salient identity at the close of the season).

156. See Jensen, *supra* note 98, at 41.

157. See, e.g., *Univ. of Denver v. Nemeth*, 257 P.2d 423 (Colo. 1953); *State Comp. Ins. Fund v. Indust. Accident Comm’n*, 314 P.2d 288 (Colo. 1957); *Van Horn v. Indus. Accident Comm’n*, 33 Cal. Rptr. 169 (Dist. Ct. App. 1963); *Taylor v. Wake Forest Univ.*, 191 S.E. 2d 379 (N.C. Ct. App.), *cert denied*, 192 S.E. 2d 197 (N.C. 1972); *Rensing v. Indiana State Univ. Bd. of Trs.*, 444 N.E. 2d 1170 (Ind. 1983); *Coleman v. W. Michigan University*, 336 N.W. 2d 224 (Mich. Ct. App. 1983); and *Waldrep v. Texas Emp’rs Ins. Ass’n*, 21 S.W.3d 692 (Tex. Ct. App. 2000).

158. See Epstein & Anderson, *supra* note 36, at 294.

159. 257 P.2d. 423 (Colo. 1953).

ers' compensation after being injured during practice.¹⁶⁰ Four years later, however, the Supreme Court of Colorado denied workers' compensation benefits to the widow of player who died after suffering an injury during a football game, finding no contractual obligation to play football between the player and university.¹⁶¹ Then, more than two decades later, in *Coleman v. Western Michigan University*,¹⁶² the Michigan Court of Appeals found no employment contract existed between a university and student-athlete which would rise to the level of being eligible for workers' compensation.¹⁶³

Some states have specifically rejected the characterization of student-athletes as employees.¹⁶⁴ In *Waldrep v. Texas Employers Insurance Ass'n*,¹⁶⁵ the Texas Court of Appeals emphasized that there was no intent on the part of Texas Christian University or Kent Waldrep that his scholarship constitute payment for his football services or that any employment relationship existed.¹⁶⁶ Similarly, in the 1983 case *Rensing v. Indiana State University Board of Trustees*,¹⁶⁷ the Indiana court ruled that no employment relationship existed between a football player and his university.¹⁶⁸

160. *See id.* at 430.

161. *State Comp. Ins. Fund v. Indus. Accident Comm'n*, 314 P.2d 288, 290 (Colo. 1957). The court technically did not overturn the *Nemeth* decision four years earlier, but rather distinguished *Nemeth* by finding that his (Nemeth's) employment "depended wholly on his playing football and it is clear that if he failed to perform as a football player he would lose the job provided for him by the University." *Id.*

162. 336 N.W.2d 224 (Mich. Ct. App. 1983).

163. *See id.* at 228 (Mich. Ct. App. 1983). In 1979, the hearing referee denied compensation to Coleman, noting he "was not an employee of defendant" but instead "a scholarship-student athlete." *Id.* at 225. The Court of Appeals affirmed and rejected the argument that college football is integral to a university's primary business of education and research. *Id.* at 227.

164. *See State Comp. Ins. Fund*, 314 P.2d at 574; *Rensing v. Ind. St. Univ. Bd. of Trs.*, 444 N.E.2d 1170, 1173 (Ind. 1983) (holding no evidence of an employer-employee relationship).

165. 21 S.W.3d 692 (Tex. App. 2000).

166. *See id.* at 699-700 (emphasizing no intent on the part of Texas Christian University (TCU) or football player Kent Waldrep that his athletic scholarship should create an employer-employee relationship that would fall under workers' compensation statutes).

167. 444 N.E.2d 1170 (Ind. 1983).

168. *See id.* at 1175 (holding no evidence of an employer-employee relationship amounting to workmen's compensation for permanent total disability). The two outlying cases that have established employment within the context of student-athlete qualifying for workers' compensation did so based on facts substantiating that the student-athletes were each separately employed by their universities outside the scope of sports, and that such employment was required in order to maintain their status on the football team. *See Epstein & Anderson, supra* note 36, at 294-95. *See also Van Horn v. Indus. Accident Comm'n*, 33 Cal. Rptr. 169 (1963)

In recent years, challenges about whether student-athletes should be compensated as employees or, alternatively, for the use of their names, images, and likenesses stem not from workers' compensation claims, but from antitrust and right-of-publicity arguments. In 2009, Sam Keller and Ed O'Bannon merged separately-filed lawsuits into a unified suit against the NCAA, labeled the *In re NCAA Student-Athlete Name & Likeness Licensing Litigation*.¹⁶⁹ Keller, O'Bannon, and other former and current Division I student-athletes claimed that the characteristics of the players in the NCAA Electronic Arts ("EA") Sports' video games mirrored theirs, thus violating their rights of publicity and image.¹⁷⁰ The *O'Bannon v. NCAA*¹⁷¹ lawsuit claimed the NCAA was violating antitrust law in preventing student-athletes from capitalizing on their names and likenesses.¹⁷²

In 2014, Senior District Judge Claudia Wilken ruled in favor of O'Bannon in his antitrust lawsuit against the NCAA.¹⁷³ At the time, Judge Wilken allowed for payment to student-athletes of up to \$5,000 in deferred compensation by NCAA schools, resulting in an immediate appeal by the NCAA which remained adamant that student-athletes should not be paid or characterized as employees.¹⁷⁴

(holding that a college football player at California Polytechnic State University, San Luis Obispo, could be the college's 'employee' for workers' compensation purposes after the widow of a college football player killed in an airplane crash following a football game sued under California law); *Univ. of Denver v. Nemeth*, 257 P.2d. 423 (Colo. 1953). *But see* *Shephard v. Loy. Marymount Univ.*, 125 Cal. Rptr. 2d 829, 832 (Cal. Ct. App. 2002) (referencing *Van Horn* and offering that as a direct result of that decision, California's "Labor Code section 3352, subdivision (k) excludes a student athlete receiving an athletic scholarship from the term 'employee'").

169. 724 F.3d 1268 (9th Cir. 2013). *See also* Kisska-Schulze & Epstein, *supra* note 105, at 22.

170. *See In re NCAA Student-Athlete Name & Likeness Licensing Litigation*, 724 F.3d at 1271–73. *See also* Kisska-Schulze & Epstein, *supra* note 105, at 22.

171. 7 F. Supp. 3d 955 (N.D. Cal. 2014), *aff'd in part, vacated in part*, 802 F.3d 1049 (9th Cir. 2015).

172. *See O'Bannon*, 7 F. Supp. 3d at 962–63. *See also* Kisska-Schulze & Epstein, *supra* note 103, at 778.

173. *See O'Bannon*, 7 F. Supp. 3d at 1008. Wilken's ruling, though short-lived by the appellate decision referenced *infra*, held that the NCAA could cap compensation at \$5,000 per year above the value of full college scholarships. *Id.*

174. *See* Tom Farrey, *Ed O'Bannon: Ruling is Tip of Iceberg*, ESPN (Aug. 10, 2014, 10:09 AM), http://espn.go.com/espn/otl/story/_/id/11332816/ed-obannon-says-antitrust-ruling-only-beginning-change [https://perma.cc/H6ZJ-9KCF] (noting that the *O'Bannon* decision is a significant start towards the outright rejection of the NCAA's amateurism model). *See also* Rick Maese, *O'Bannon v. NCAA Ruling Could Set Up Larger Arguments over College Sports, Experts Say*, WASH. POST (Aug. 9, 2014), http://www.washingtonpost.com/sports/colleges/obannon-v-ncaa-ruling-could-set-up-larger-arguments-over-college-sports-experts-say/2014/08/09/5338ae4c-1fe2-11e4-9b6c-12e30cbe86a3_story.html (detailing that in the aftermath

The Ninth Circuit Court of Appeals affirmed Judge Wilken's decision, in part, but rejected and vacated the part of her ruling allowing schools to offer deferred compensation in exchange for the use of players' likenesses.¹⁷⁵

Most recently, in 2017, former Ohio State University linebacker, Chris Spielman, filed a similar lawsuit against IMG College, LLC, Ohio State University, and others for unlawfully conspiring under antitrust law to deny payment to current and former Ohio State football players for the unlawful use of their names, images, and likenesses.¹⁷⁶ The complaint alleges that Honda corporate-sponsored banners hung during home football games at the Buckeyes' stadium depicted Spielman and other student-athletes who never agreed to appear on the banners and were never paid for such appearances.¹⁷⁷ Spielman's complaint demands that the U.S. District Court for the Southern District of Ohio enjoin Ohio State and others from continuing to use players' identities for profit without negotiating these rights with players, and to compel the defendants to pay monetary damages to former players for the historic use of their images and likenesses.¹⁷⁸

It also must be noted, however, that a 2014 ruling from Region 13 of the National Labor Relations Board ("NLRB") involving a unionization attempt by the Northwestern University football team

of the *O'Bannon* decision, the NCAA "has given no indication it is eager to embrace any form of pay-for-play model").

175. See *O'Bannon*, 802 F.3d at 1079 (vacating the district court's judgment (Wilken) and ordering a permanent injunction insofar as requiring the NCAA to allow its member schools to pay student-athletes up to \$5,000 per year in deferred compensation).

176. See Michael McCann, *Chris Spielman's Lawsuit Against Ohio State Could Set Monumental Precedent*, SPORTS ILLUSTRATED, <https://www.si.com/college-football/2017/07/16/chris-spielman-ncaa-ohio-state-football-img-college-ed-obannon-honda-nike> [<https://perma.cc/F8Y3-YMDP>] (July 16, 2017). See also Class Action Complaint, *Spielman v. IMG College, LLC*, No. 2:17-cv-00612-MHW-KAJ, 2017 WL 3015658 (S.D. Ohio July 14, 2017).

177. See Class Action Complaint, *supra* note 176, at 8–9. The complaint also alleges that Ohio State, in collaboration with Nike, produced "Legends of the Scarlet and Gray" vintage Ohio State jerseys that depicted Spielman and other former Ohio State athletes without providing compensation. *Id.* at 6.

178. *Id.* at 34. Spielman's case sets the groundwork for having a greater judicial impact than even the *O'Bannon* case, which was denied certiorari on appeal from the Ninth Circuit to the U.S. Supreme Court in 2016. Should it go to trial and be appealed to the Sixth Circuit Court of Appeals, resulting in a possible conflict with the Ninth Circuit's ruling in *O'Bannon*, the U.S. Supreme Court may ultimately be faced with a request for certiorari premised on a conflict of federal antitrust law interpretation between circuits. Although there is no guarantee that the U.S. Supreme Court would grant certiorari on any grounds for appeal, the Spielman filing provides the springboard for unified federal precedent to be established in the area of antitrust law as applies to former and current student-athletes.

which held that select student-athletes should be allowed to unionize under the National Labor Relations Act (“NLRA”) may have been the most significant step forward—though short lived—in the movement to characterize student-athletes as employees.¹⁷⁹ That decision and opinion by Hon. Peter Sung Ohr authoring that football players at Northwestern should indeed be considered employees under the law and be allowed to vote to unionize was ultimately overruled and vacated by the full NLRB, holding that the Region 13 NLRB did not have jurisdiction to hear the case from the outset.¹⁸⁰ Then, in 2016, the Seventh Circuit Court of Appeals, in *Berger v. NCAA*,¹⁸¹ held that former track and field student-athletes at the University of Pennsylvania were not employees and therefore not covered under the Fair Labor Standards Act (“FLSA”), the federal minimum wage law.¹⁸²

Each of these challenges, cases, and decisions—from early Colorado workers’ compensation to present—have helped shape the debate over whether student-athletes should be paid or characterized as employees. It is clear, however, that the judicial system has thus far generally not conceded to the will of plaintiffs who claim that student-athletes are employees of their institutions, *per se*. This assessment, in conjunction with the NCAA’s firm adherence to the fundamental principle of amateurism in college sports, pro-

179. Nw. Univ. Employer & Coll. Athletes Players Ass’n, 13-RC-121359 (N.L.R.B.) (Mar. 26, 2014). *See also* Kisska-Schulze & Epstein, *Northwestern University, The University of Missouri, and the “Student-Athlete”: Mobilization Efforts and the Future*, 26 J. LEGAL ASPECTS OF SPORT 71, 94 (2016). Regional Director, Peter Sung Ohr, determined that grant-in-aid scholarship football players at Northwestern University were ‘employees’ under Section 2(3) of the NLRA and could therefore hold a unionization election. *Id.*

180. Nw. Univ. Employer & Coll. Athletes Players Ass’n, 362 N.L.R.B. No. 167, *7 (Aug. 17, 2015) (noting that even if it were to find that scholarship student-athletes were employees, “it would not effectuate the policies of the Act to assert jurisdiction,” because, due to the nature of NCAA Division I Football Bowl Subdivision (FBS) football and the fact that there are so few private universities who are members, “it would not promote stability in labor relations to assert jurisdiction in this case”).

181. 2016 U.S. App. LEXIS 21642 (7th Cir. 2016).

182. *Id.* at *1–*2 (referencing the relevant statutory framework throughout beginning with 29 U.S.C. § 201 et seq., “Fair Labor Standards Act of 1938”). The Berger court stated, “Simply put, student-athletic ‘play’ is not ‘work,’ at least as the term is used in the FLSA. We therefore hold, as a matter of law, that student-athletes are not employees and are not entitled to a minimum wage under the FLSA.” *Id.* at *12. However, in a concurring opinion in this decision, Circuit Judge David F. Hamilton cautioned the court by saying that he felt that “revenue sports” such as Division I men’s basketball and the Football Bowl Championship Subdivision (FBS) might be looked at differently someday given that “[t]hose sports involve billions of dollars of revenue for colleges and universities.” *Id.* at *13 (Hamilton, J., concurring).

motes the position that student-athletes are not employees of their institutions. Such a standard, along with the IRS's historical reluctance to tax student-athletes, sustains the importance of analyzing the potential tax implications of ESDI and LOV payouts. As the IRC and Treas. Regs. do not provide rules governing the taxability of disability payouts when the payor of the premium is neither the individual taxpayer nor their employer, the next section offers practical solutions to address the tax treatment of disability insurance policy payouts while taking into account the aforementioned historical perspectives.

V. PROPOSALS FOR THE TAX TREATMENT OF ESDI AND LOV PAYOUTS

As the IRS has been historically averse to imposing taxes on student-athletes and the college sports industry in general, and as the American legal system has not generally characterized student-athletes as employees of their academic institutions, the Code and Treas. Regs. offer no clear guidance regarding the taxability of ESDI and LOV payouts. Evaluating the potential tax consequences of these payouts is an important addition to the minimal academic literature currently available regarding insurance policy coverage for student-athletes.¹⁸³ An analysis of the taxability of these payouts is also timely due to the fact that the first recorded LOV insurance policy payout only occurred in 2015.¹⁸⁴ Given the increasing num-

183. See generally Kain et al., *supra* note 13 (discussing the increasing arena of LOV litigation); Lens & Lens, *supra* note 38 (discussing the insurance options available to elite student-athletes); Wong, et al., *supra* note 44 (providing a section on disability policies for student-athletes); Michael D. Randall, Note, *Even I Can't Cover Me: Examining the NCAA's Effective Prohibition on "Loss of Value" Insurance for Its Student-Athletes*, 21 CONN. INS. L.J. 521 (2015) (analyzing the NCAA prohibition on student-athletes exploring outside insurance to cover loss-of-value).

184. One of the earliest media records regarding ESDI or LOV insurance policy payouts emerged in 2015. Before the start of his senior year at the University of Oregon, cornerback, Ifo Ekpre-Olumu, purchased a LOV insurance policy. See Xandria James, *Ifo Ekpre-Olumu Collects \$3M on Loss of Value Policy*, SPORTS ILLUSTRATED (Oct. 19, 2015), <https://www.si.com/nfl/2015/10/19/cleveland-browns-ifo-ekpre-olumu-three-million-insurance-policy> [<https://perma.cc/AGD3-EXTK>]. At that time, he was projected as a top twelve pick in the first round of the 2015 NFL draft. *Id.* However, during practice Ekpre-Olumu tore his ACL, resulting in him falling to the seventh round, 241st pick in the NFL draft. *Id.* This injury and subsequent drop in his NFL draft stock resulted in an insurance payout totaling \$3 million. *Id.* Ekpre-Olumu has been cited as the first college football player to ever collect on a LOV insurance policy. *Id.* See also Andy Staples, *Man Coverage: How Loss-of-Value Policies Work and Why They're Becoming More Common; Punt, Pass & Pork*, SPORTS ILLUSTRATED (Jan. 18, 2016), <https://www.si.com/college-football/2016/01/18/why-loss-value-insurance-policies-becoming-more-common> [<https://perma.cc/3NZA-DXVE>]; Chase Goodbread, *Silas Redd First to Collect from Loss-of-Value Insurance Policy*, NFL (Oct. 5, 2015, 2:13 PM), <http://www.nfl.com/news/story/>

ber of elite student-athletes who are listed as beneficiaries of ESDI and LOV insurance policies, it is important to evaluate the potential tax consequences of insurance payouts when a student-athlete is listed as a beneficiary on a policy that (1) they individually purchase or finance, or (2) is purchased by the university they play for.¹⁸⁵

A. Student-Athlete-Beneficiary of a Policy They Individually Purchase or Finance

Adopting the language of the IRC, when a student-athlete purchases an ESDI or LOV insurance policy, any resulting payout following injury is generally going to result in a tax-free transaction. The key to this foundation is in the identification of the actual payor of the premium—the individual or their employer. As previously noted, IRC § 104 exempts from gross income damages received from personal injuries unless those amounts are paid for by an employer.¹⁸⁶ IRC §§ 105 and 106 reiterate this premise.¹⁸⁷

Similar to self-employed persons and those who pay for health insurance premiums out-of-pocket, student-athletes who personally pay for insurance premiums will qualify for the more favorable tax treatment allowed under the IRC should an injury payout occur.¹⁸⁸ However, IRC § 104 requires the additional element of identifying whether the insurance premiums are paid for with pre-tax or after-tax dollars to fully secure a tax-free transaction.¹⁸⁹ Thus, student-athletes who purchase ESDI or LOV premiums using after-tax dollars will qualify for the tax exclusion.¹⁹⁰

Similarly, a student-athlete who takes out a personal loan to finance the cost of an ESDI and LOV insurance policy should also receive favorable tax treatment on any resulting payouts. Although IRC § 61 defines gross income as “all income from whatever source derived,” taxpayers are not required to report personal loans as income nor pay income tax on the receipt of such loans.¹⁹¹ Such

0ap3000000550500/article/silas-redd-first-to-collect-from-lossofvalue-insurance-policy [https://perma.cc/37PH-YDGE] (reporting that Redd, formerly of USC, may have collected on a LOV payout prior to Ekpre-Olomu).

185. See Staples, *supra* note 184 (noting increasing number of elite student-athletes who are listed as beneficiaries of ESDI and LOV insurance policies).

186. See 26 U.S.C. § 104(a)(3). See also Treas. Reg. § 1.104-1(d).

187. See 26 U.S.C. §§ 105(a), 106(a).

188. See *id.* § 104(a)(3).

189. See *id.*

190. See *id.*

191. Phillip J. Closius & Douglas K. Chapman, *Below Market Loans: From Abuse to Misuse—a Sports Illustration*, 37 CASE W. RES. 484, 487 (1987) (quoting 26 U.S.C. § 61(a)).

exclusion is based on the premise that an income tax is only imposed on a gain or increase in income.¹⁹² As the receipt of loan proceeds is offset by an obligation to repay the loan, the transaction does not result in gain.¹⁹³ However, if the proceeds of a loan are not required to be repaid by the borrower, the transaction will result in taxable gain at the point when the offsetting liability is discharged.¹⁹⁴

A central requirement in assessing the taxability of loan proceeds is to ensure that the loan is bona-fide. For a loan to be recognized as bona-fide indebtedness for tax purposes, there must be evidence of an unqualified obligation to pay a sum certain at a reasonably fixed maturity date.¹⁹⁵ Such mandate obliges the borrower to make a promise to repay a substantial portion of the advanced funds in order to reap the benefits of entering into a tax-free transaction.¹⁹⁶ It is also important to ensure that any loan entered into between a third-party creditor and debtor is at arms-length. Loans with below-market interest rates may be taxable to the extent of the foregone interest that the debtor should have paid at the applicable federal rates (“AFR”).¹⁹⁷

Based on the language of the IRC, we believe that student-athletes who receive injury payouts from ESDI or LOV insurance policies that they purchase themselves should not have to pay any federal tax on such proceeds. Additionally, student-athletes who take out personal loans to finance disability insurance policies should also be successful in avoiding any federal tax consequences following an injury payout. As the NCAA allows student-athletes to take out loans to purchase ESDI and LOV policies without jeopardizing their amateur status, such loans can be secured through private insurers or via their universities’ NCAA SAF.¹⁹⁸ To successfully

192. See Glenn E. Coven, *Redefining Debt: Of Indianapolis Power and Fictitious Interest*, 10 VA. TAX REV. 587, 600 (1991).

193. See *id.* at 601.

194. See *id.* (citing *United States v. Kirby Lumber Co.*, 284 U.S. 1, 2–3 (1931); Treas. Reg. § 1.61-12(a)).

195. See Kevin J. Liss, *Options as Disguised Financings: The Demise of an Urban Tax Legend*, 27 VA. TAX REV. 907, 921 (2008) (citing *Gilbert v. Comm’r*, 248 F.2d 399, 402 (2d. Cir. 1957)); *id.* at 721 n.22 (quoting *Gilbert*, 248 F.2d at 402 (“The classic debt is an unqualified obligation to pay a sum certain.”)); *Id.* (quoting I.R.S. Notice 94-47, 1994-1 C.B. 357) (“listing as first among several factors in determining whether an instrument is debt ‘whether there is an unconditional promise on the part of the issuer to pay a sum certain.’”).

196. See *id.* at 721.

197. See 26 U.S.C. § 7872.

198. See 2017–18 NCAA MANUAL, *supra* note 19, at art. § 12.1.2.4.4 (“Exception for Insurance Against Disabling Injury or Illness, or Loss of Value”). See also

avoid taxation on payouts, these loan agreements should evidence an obligation by the student-athlete to repay the loan at the point of a prescribed date or occurrence of a specified event, and include an arms-length rate of interest based on the AFR.¹⁹⁹ Since evidence of a lender's discharge of indebtedness will automatically trigger taxable gain, universities must ensure that loans entered into with elite student-athletes to finance ESDI and LOV insurance policies not be discharged or forgiven or the entire amount of the loan will be taxable to the student-athlete.

B. Student-Athlete-Beneficiary of a Policy Purchased By Their University

If a student-athlete receives an injury payout from a disability insurance policy paid for by their university, it could trigger a taxable event. This presumption is based on the language of the IRC which allows that damages received due to personal injuries be exempt from gross income unless those amounts are paid for by an employer.²⁰⁰ Because the Treas. Regs. only provide a generic definition for the term 'employer' as "the employer maintaining the plan . . .," a university that maintains and ultimately pays for ESDI and LOV insurance plans could debatably fall within the spectrum of this definition.²⁰¹

Imposing a tax on disability payouts when universities pay the cost of the insurance premiums would somewhat correlate with the IRC requirements that payouts received by injured parties are taxable when their employers pay the price of the premium, since the payor of the policy in this instance would definitely *not* be the individual taxpayer.²⁰² Applying the language of IRC sections 104, 105, and 106 to universities that choose to pay the cost of ESDI and LOV premiums would provide uniformity in understanding the tax consequences of elite student-athletes across the country who are beneficiaries of such policies. However, adopting this posture is subject to debate since the term 'employer' in the Treas. Regs. is so vague.

id. at art. § 16.11.1.4 ("Insurance Against Disabling-Injury or Illness, or Loss of Value").

199. Every month, the IRS publishes various prescribed rates for federal income tax purposes, known as the Applicable Federal Rates (AFRs). See *Index of Applicable Federal Rates (AFR) Rulings*, IRS, <https://apps.irs.gov/app/picklist/list/federalRates.html> [<https://perma.cc/4JT9-LT5J>] (last visited Jan. 4, 2018).

200. See 26 U.S.C. §§ 104(a)(3), 105(a), 106(a). See also Treas. Reg. §§ 1.104-1(d), 1.105-1(a), 1.106-1.

201. See Treas. Reg. § 1.410(b)-9.

202. See 26 U.S.C. §§ 104(a)(3), 105(a) and accompanying Treasury Regulations.

Because American courts have consistently held that student-athletes are not employees of their universities, the ambiguity of the term ‘employer’ could result in varied interpretations of whether the exemptions allowed in the IRC apply to student-athletes when their universities pay the cost of ESDI and LOV premiums.²⁰³

IRC sections 104 and 105 do not specifically address the tax consequences of a non-employer (university) paying the cost of the premium on behalf of a non-employee (student-athlete) of a health or disability insurance policy. In conjunction with the NCAA’s adherence to the principle of amateurism, the rather unified findings in the American court system that student-athletes are not employees of their institutions could set the stage for a credible argument that the language embedded in the IRC with respect to employers paying disability insurance premiums does *not* directly apply to student-athletes who receive payout benefits from policies purchased by their universities.

This argument, however, is not entirely telling of how the IRS would legitimately characterize the relationship between student-athletes and their institutions for disability insurance purposes. While judicial precedent may provide a compelling argument to suggest that no employment relationship exists between institutions and their student-athletes, it is important to consider the possibility that such relationship does in fact exist from a purely tax perspective. When evaluating the existence of an employment relationship from a tax standpoint, the IRS and most government agencies generally rely on the application of the Right-To-Control Test.²⁰⁴

1. *The Right To Control Test*

The Right-To-Control Test requires an evaluation of the contractual intent of workers in conjunction with the employers’ right to control in determining whether an employer-employee relationship exists.²⁰⁵ Evidence must indicate that the employing party re-

203. See, e.g., Epstein & Anderson, *supra* note 36, at 297 (“[T]he courts have been consistent in finding that student-athletes are not recognized as employees under any legal standard, whether bringing claims under workers’ compensation laws, the NLRA or FLSA.”).

204. See Pamela A. Izyanariu, *Matters Settled but Not Resolved: Worker Misclassification in the Rideshare Sector*, 66 DEPAUL L. REV. 133, 142 (2016) (noting that the IRS and most government agencies rely on some rendition of the common law test for employment).

205. See Kisska-Schulze & Epstein, *supra* note 103, at 795. See also E.E.O.C. v. Sidley Austin Brown & Wood, 315 F.3d 696, 705 (7th Cir. 2002) (noting that “the court stated that the most important factor in deciding whether a worker was an employee or an independent contractor was the employer’s right to control the worker’s work” while also employing an economic realities test”); Justin C. Vine,

serve the right to control how the worker performs their duties.²⁰⁶ Factors considered as part of this analysis include contractual intent, “the exercise of control [over the worker], the method of payment, the furnishing of equipment, and the right to terminate the worker.”²⁰⁷

Although the IRS adopts its own “Twenty-Factor Test” to evaluate the existence of an employment relationship, the focal point of that test relies on the identification of control and includes an evaluation of the degree of supervision and control over a worker, the regularity of training, and the continuity of the relationship between worker and employer.²⁰⁸ This test has been met with some skepticism due to its relative inefficiency and subjectivity.²⁰⁹ However, the common law Right-To-Control Test continues to be the most dominant test employed by courts when examining the existence of an employment relationship.²¹⁰

Note, *Leveling the Playing Field: Student Athletes Are Employees of Their University*, 12 CARDOZO PUB. L. POL’Y. & ETHICS J. 235, 246–47 (2013).

206. See Izyanariu, *supra* note 204, at 142 (documenting that under common law control test, it must be shown that rideshare companies reserve right to control rideshare workers).

207. Timothy Davis, *Intercollegiate Athletics: Competing Models and Conflicting Realities*, 25 RUTGERS L.J. 269, 286 (1994). See also *Rensing v. Ind. St. Univ. Bd. of Trs.*, 444 N.E.2d 1170, 1173 (Ind. 1983) (involving the case of a collegiate football player who suffered a debilitating injury resulting in his claim for recovery under workmen’s compensation). In *Rensing*, the court noted, “[i]t is clear that while a determination of the existence of an employee-employer relationship is a complex matter involving many factors, the primary consideration is that there was an intent that a contract of employment, either express or implied, did exist.” *Id.*

208. See Rev. Rul. 87-41, 1987-1 C.B. 296 (codified at Treas. Reg. § 31.3121(d)-1 (LEXIS through Oct. 28, 2015 issue of the Fed. Register)). See also Izyanariu, *supra* note 204, at 142 (noting that the IRS Twenty Factor Test primarily focuses on the control factor); Kisska-Schulze & Epstein, *supra* note 103, at 796 (noting the IRS’s use of a derivative of the common law test); Izyanariu, *supra* note 192, at 142 (noting that the IRS Twenty Factor Test primarily focuses on the control factor).

209. See Kisska-Schulze & Epstein, *supra* note 103, at 798 (citing Alexandre Zucco, Note, *Independent Contractors and the Internal Revenue Service’s “Twenty Factor” Test: Perspective on the Problems of Today and the Solutions for Tomorrow*, 57 WAYNE L. REV. 599, 609 (2011)) (arguing that the IRS’s twenty factors were established to represent a multitude of competing considerations that are not easily classifiable, that the three categories create only arbitrary groups without specific clarification as to any of the individual factors, and that courts have interpreted these twenty factors in various and unexpected ways, further adding to the layer of inconsistency). See also Christopher Buscaglia, *Crafting a Legislative Solution to the Economic Harm of Employee Misclassification*, 9 U.C. DAVIS BUS. L.J. 111, 113 (2009) (proposing that the IRS twenty-factor test is insufficient “to deal with the range of evils” arising from the misclassification of workers).

210. See Izyanariu, *supra* note 204, at 141. Other common tests utilized to determine the existence of an employment relationship include the economic realities test which is generally applied in the context of the Fair Labor Standards Act governing minimum-wage and overtime obligations, and the Hybrid Test which

Identifying the extent of control that universities have over student-athletes has been analyzed in academic literature, with scholars offering persuasive evidence of the magnitude of control that athletic departments and coaches hold.²¹¹ One legal analysis specifically focused on the degree of control that Division I-A (FBS) football coaches have over their players, and concluded that the Right-To-Control Test is already being met in college athletics.²¹² This analysis surmised that student-athletes may be subject to even more control than those employees on campus who are financially compensated for their work.²¹³ Reinforcing this idea, during his trial against the NCAA, Ed O'Bannon testified, "I was an athlete masquerading as a student . . . I was there strictly to play basketball."²¹⁴ Others in the *O'Bannon* trial noted that playing college sports was their main occupation and that it is difficult or impossible for student-athletes to function like normal students because of the amount of time they are required to devote to their sport.²¹⁵

was adopted specifically for determining employee status under federal discrimination statutes. See also Kisska-Schulze & Epstein, *supra* note 103, at 801–05.

211. See Kisska-Schulze & Epstein, *supra* note 103, at 799. See also Nicholas Fram & T. Ward Frampton, *A Union of Amateurs: A Legal Blueprint to Reshape Big-Time College Athletics*, 60 BUFFALO L. REV. 1003, 1032 (2012) (documenting that student-athletes' labor and lives are subject to the control of their universities, both on and off the field to an extent that most other employees would consider intolerable); Robert McCormick & Amy Christian McCormick, *The Myth of the Student-Athlete: The College Athlete as Employee*, 81 WASH. L. REV. 71, 97–119 (2006) (examining degree of control over student-athletes by their universities, including the excessive and mandatory daily practice schedules, conditioning, weightlifting sessions, study halls, game day activities, and required travel schedules during the pre-, regular, and post seasons); Steven L. Willborn, *College Athletes as Employees: An Overflowing Quiver*, 69 U. MIAMI L. REV. 65, 102 (2014) (documenting that college athletes are subject to highly detailed control by their universities over how they perform their services); Vine, *supra* note 205, at 251 (presenting that University athletic departments exercise enormous amount of control over scholarship athletes, including attendance at mandatory practices, games, film sessions, and study hall).

212. See McCormick & McCormick, *supra* note 211, at 98. Coaches' exercise of control over Division I-A athletes is apparent in the form of location, duration, and manner in which athletes participate in required practices, games, and academic commitments during the regular season, as well as the control that coaches have over players' lives in the off-season to include training, conditioning, team meetings, mandatory study halls, summertime weightlifting and running, and mandatory pre-season practices beginning in early August which encompasses the most intensive training period of the year. *Id.* at 98–105. Other demands on student-athletes include attendance at post-season bowl games, recruitment pressures and mandatory random drug testing. *Id.*

213. See *id.* at 97.

214. Kisska-Schulze & Epstein, *supra* note 103, at 807 (citing Isaac Brekken, *Judge Rules Against NCAA in Ed O'Bannon Case*, CBS NEWS (Aug. 8, 2014, 8:19 PM), <http://www.cbsnews.com/news/judge-rules-against-ncaa-in-ed-obannon-case/> [<https://perma.cc/M7BT-DNU2>]).

215. See Brekken, *supra* note 214.

There is now a growing spectrum of judicial cases against universities, the NCAA, and others which require an examination of the degree of control that select parties have over student-athletes' names, images, and likenesses.²¹⁶

Based on the application of the Right-To-Control Test, it is possible that the IRS could decide to characterize student-athletes as employees of their institutions for purposes of IRC §§ 104, 105, and 106. However, because the language embedded in these Code sections does not specifically address the taxability of insurance policy payouts when a non-employer pays the cost of the premium, the underlying question is whether the IRS would choose to tax student-athlete beneficiaries when their universities pay the premiums. Relying on the IRS's historical reluctance to tax student-athletes and the college sports industry in general, we conclude the IRS would ultimately resolve *not* to impose a tax on student-athletes' ESDI and LOV payouts when their universities pay for the premiums.

2. *Maintaining the Historical Preservation of Tax Favorability*

The IRS has thus far been reluctant to impose an income tax on student-athletes' grants-in-aid.²¹⁷ Similarly, the agency has historically granted positive tax positions to the college sports industry in general based on the tax-exempt status of universities, athletic departments, and the NCAA.²¹⁸ In combination with the NCAA and American court system's continued adherence to the preservation of amateurism in college sports, we resolve that the IRS will maintain its historical preservation of tax favorability of student-athletes and not impose a tax on ESDI and LOV payouts when their universities pay the cost of the premiums.

This presumption is primarily based on our reliance of the IRS's unwillingness to date to impose a federal tax on student-athletes' grants-in-aid, along with the agency's stance that education supersedes sports in the collegiate environment. In the late 1970s, the IRS documented that for federal tax purposes, the primary rationale for student-athletes to attend college is for educational reasons. This stance was acknowledged in two separate documents—Revenue Ruling 77-263 and Technical Advice Memorandum 78-51-

216. See Kisska-Schulze & Epstein, *supra* note 103, at 806.

217. See *supra* notes 109–135 and accompanying text.

218. See *supra* notes 137–152 and accompanying text.

004.²¹⁹ Although the U.S. Supreme Court and Tax Court have applied the quid pro quo condition of IRC § 117 to research assistants and fellowship recipients, this condition has not been similarly applied to student-athletes receiving qualified scholarships.²²⁰ Instead, the IRS issued Revenue Ruling 77-263 to exclude athletic scholarships from the strict quid pro quo limitation applied by the courts in other situations.²²¹

Such promulgation endorsed the IRS's stance that the benefit which a university might receive by having a student-athlete on the playing field is incidental to the primary purpose of collegiate sports, which is educational.²²² One year later, the IRS again noted the connection between education and college athletics in Technical Advice Memorandum 78-51-004, noting that college sports audiences contribute to the education of student-athletes.²²³ As of 2018, the IRS has neither challenged nor reexamined its tax treatment of athletic scholarships.²²⁴ We therefore hypothesize that the IRS will likewise find that any benefit received by a university that pays the cost of an ESDI and LOV premium on behalf of one of its own elite student-athletes would be incidental to the additional year of education and course credits that the student-athlete would receive by agreeing to postpone their entry into the professional draft for another year.

Similar to the IRS's reluctance to impose an income tax on student-athletes' athletic scholarships, the sports industry in general has benefited from favorable federal tax treatment. As the primary purpose of a university is to educate students, institutions and their college athletic programs have maintained federal tax-exempt statuses.²²⁵ This interconnection between education and college athletics continues to be a driving force, shielding the industry from otherwise unfavorable tax positions. In the 1970s, Congress amended the IRC to specifically identify amateur sports competi-

219. See I.R.S. Tech. Adv. Mem. 78-51-004 (Aug. 21, 1978); Rev. Rul. 77-263, 1977-2 C.B. 47, 1977 WL 43568 (1977).

220. See *supra* notes 113–127 and accompanying text.

221. See Rev. Rul. 77-263, 1977-2 C.B. 47, 1977 WL 43568 (1977).

222. See Morehouse, *supra* note 129.

223. I.R.S. Tech. Adv. Mem. 78-51-004 (Aug. 21, 1978).

224. See Morehouse, *supra* note 129. The agency did, however, rearticulate its stance that athletic scholarships qualify for exclusion from gross income outside the spectrum of quid pro quo in its letter to Senator Richard Burr (R-NC). See also KOSKINEN, *supra* note 11.

225. Haden, *supra* note 139, at 678.

tion as being charitable.²²⁶ Although in the past the IRS endeavored to impose a UBI tax on revenue from broadcasting rights from college bowl games and a tax on corporate sponsorship income received by tax-exempt organizations, both attempts were ultimately thwarted following significant protests and lobbying.²²⁷

The most recent tax development that will undoubtedly impact higher education is the Tax Cuts and Jobs Act (“TCJA”), which includes the imposition of a 21% excise tax on the five highest paid employees of non-profit organizations who earn over \$1 million per year.²²⁸ This tax reform will also require college athletic departments in the future to mitigate the possible fallout due to the elimination of tax deductions that college boosters have been able to receive for contributions towards season ticket purchases.²²⁹ Although the TCJA evidences that Congress has now has its eyes set on taxing certain aspects of educational institutions moving forward, the final draft of the law itself does not directly target students or student-athletes.

Our conclusion is also based on the fact that both the U.S. court system and the NCAA have continued to adhere to the principle of amateurism in college sports, maintaining the position that student-athletes are not employees of their institutions.²³⁰ Reliance on this posture is important because the tax impact on disability benefits, based directly on the language of the IRC, comes down to who pays the cost of the premium—the employer or the individual taxpayer.²³¹ Neither the IRC nor applicable Treas. Regs. address the taxability of payouts when a non-employer (university) pays the premium on behalf of a non-employee (student-athlete). Although the application of IRC §§ 104, 105, and 106 could be debatable due to the ambiguity of the term ‘employer’ in the Treas. Regs., we resolve that the IRS will not impose a tax on student-athlete-beneficiaries of ESDI and LOV payouts due to the agency’s historical

226. TAX REFORM ACT OF 1976, Pub. L. No. 94-455, § 1313(a), 90 Stat. 1520, 1730 (codified as amended at I.R.C. § 501(c)(3)).

227. See *supra* notes 142–147 and accompanying text.

228. TAX CUTS AND JOBS ACT, H.R. 1, 115th Cong. (2017–2018) which became Public Law No. 115-97 on Dec. 22, 2017.

229. *Id.* See also Darren Rovell, *Tax Reform Nixes Season-Ticket Donation Deductions; Schools Scramble into Action*, ESPN (Dec. 20, 2017), http://www.espn.com/college-football/story/_/id/21827570/tax-reform-bill-removes-deduction-donations-season-tickets-forcing-universities-make-other-plans [https://perma.cc/R9AJ-3LVQ].

230. See *supra* notes 158–182 and accompanying text.

231. See 26 U.S.C. §§ 104, 105(a).

reluctance to tax their grants-in-aid.²³² Similarly, we theorize that the IRS will not characterize student-athletes as employees of their institutions under the Right-To-Control Test as the agency has thus far not conceded to such characterization for purposes of IRC § 117 under the guise of the pay-for-play model.²³³ Unless the IRS were to change its posture on professionalizing the college sports arena for federal tax purposes, we presume that student-athletes will not be characterized as employees of their institutions for purposes of IRC §§ 104, 105, and 106.

3. *Addressing the Taxability of Proceeds Received from ESDI and LOV Insurance Policies*

As the IRC and Treas. Regs. do not provide clear guidance regarding the taxability of payouts when non-employers pay the insurance premiums on behalf of beneficiaries, and as more institutions entertain the idea of paying for LOV and ESDI premiums to entice elite student-athletes to postpone entering the professional league draft, we feel it would be prudent for the IRS to publish a Revenue Ruling to address the taxability of proceeds received from disability insurance policies purchased for student-athletes by their universities.²³⁴ Similar to its issuance of Revenue Ruling 77-263, we recommend that the IRS promulgate a Revenue Ruling to document its official interpretation of the application of IRC §§ 104, 105, and 106 to ESDI and LOV insurance policies.²³⁵

A Revenue Ruling is a pronouncement issued by the IRS to provide an official interpretation of the IRC and Treas. Regs. to a particular set of facts.²³⁶ Revenue Rulings may be relied upon as precedent by other taxpayers, and may be revoked or amended at

232. See Treas. Reg. § 1.410(b)-9.

233. See generally Kisska-Schulze & Epstein, *supra* note 103 (analyzing the possibility of taxing qualified scholarships should student-athletes be deemed employees of their universities).

234. We recommend that the IRS issue a Revenue Ruling in lieu of a Private Letter Ruling (“PLR”) in this instance. PLRs are issued by the IRS to a single taxpayer based on that taxpayer’s specific set of facts and circumstances. Because of the individual nature of PLRs, they are not relied on as precedent by other taxpayers. The IRS’s issuance of a PLR at the request of an individual taxpayer (here, a student-athlete) would not provide any uniformity in applying the Internal Revenue Code to ESDI and LOV payouts when the premiums are paid for by universities.

235. See Rev. Rul. 77-263, 1977-2 C.B. 47, 1977 WL 43568 (1977).

236. *Understanding the IRS Guidance—A Brief Primer*, IRS, <https://www.irs.gov/newsroom/understanding-irs-guidance-a-brief-primer> [<https://perma.cc/MH3M-MYLW>] (last visited Jan. 8, 2018). See also *Federal Tax Research: Documents & Resources: IRS Rulings and Pronouncements*, UCLA SCHOOL OF LAW, <http://libguides.law.ucla.edu/c.php?g=183332&p=4489881> (last visited Jan. 8, 2018).

any time by the IRS's National Office.²³⁷ We believe that the issuance of a Revenue Ruling would be the most appropriate method for interpreting the application of IRC §§ 104, 105, and 106 to ESDI and LOV insurance policies as such pronouncement would parallel the form of guidance that the IRS historically chose to use when interpreting IRC § 117 as applies to student-athletes. An official ruling in this case would clarify whether universities are to be deemed employers for purposes of disability insurance policies, provide uniformity in applying the IRC to student-athletes who are beneficiaries of disability insurance policies, and confirm whether the IRS intends to continue its favorable tax treatment of student-athletes in a legal environment that continues to face more challenges to the status quo than ever before.

VI. CONCLUSION

For a small number of elite student-athletes in the college sports arena, enrolling in the NCAA's ESDI and LOV insurance programs may be important to protect against career-ending injuries and loss of future earnings. To entice top student-athletes to remain on the amateur playing field for one additional year in lieu of entering the professional sports draft, some universities are electing to pay the premiums for these policies. However, the language of the IRC and Treas. Regs. is unclear as to whether an injury-related payout to a student-athlete-beneficiary amounts to a taxable event if their university pays the premium.

The IRS generally requires that insurance payouts received through accident or health plans paid for by an employer be reported as income. However, the American legal system has thus far not generally characterized student-athletes as employees of their institutions. Further, under the current standard of *amateurism* as adopted by the NCAA, the IRS has been reluctant to impose taxes on student-athletes with respect to their grants-in-aid, or the college sports industry in general.

Without any official interpretation of the tax consequences of ESDI and LOV payouts received from insurance policies purchased by their universities, it is currently unclear as to how the IRS would ultimately tax the proceeds of these payouts. Given the increasing number of elite student-athletes who are listed as beneficiaries of ESDI and LOV insurance policies, it is important to understand the tax consequences of these payouts when a student-athlete is listed as

237. See UCLA SCHOOL OF LAW, *supra* note 236.

a beneficiary on a policy that they individually purchase or finance, or is purchased by the university they play for.

To best ensure that an injury payout received from an ESDI or LOV insurance policy is tax-free, we conclude that a student-athlete should purchase the policy individually. This proposal is based on the language of the IRC, which exempts from gross income damages received from personal injuries unless those amounts are paid for by an employer. Similarly, a student-athlete who takes out a personal loan to finance the cost of an ESDI and LOV insurance policy should also receive favorable tax treatment on any injury payout since an income tax is only imposed on a gain or increase in income. However, to ensure the loan transaction results in a tax-free payout it must be properly structured so that the loan is not deemed to be forgivable by the university.

Alternatively, if a student-athlete receives an injury payout from a disability insurance policy paid for by their university, it could potentially trigger a taxable event since the IRC requires that payouts received by injured parties are taxable when their employers pay the price of the premium. Nevertheless, this proposal is debatable since the definition of the term 'employer' in the Treas. Regs. is vague. Such ambiguity could result in varied interpretations of whether universities are deemed employers of student-athletes for purposes of IRC §§ 104, 105, and 106. Although the IRS could choose to characterize student-athletes as employees, we conclude that the IRS will continue to maintain its historic preservation of tax favorability of student-athletes, and ultimately decide not to impose a tax on student-athletes' ESDI and LOV payouts when their universities pay the cost of the premiums.

However, because there could be areas open to debate on this issue, we recommend that the IRS publish a Revenue Ruling to address the taxability of proceeds received from disability insurance policies purchased for student-athletes by their universities to clarify whether universities are employers, provide uniformity in applying the tax Code to disability insurance policies paid for by universities, and confirm whether the IRS intends to continue its favorable tax treatment of student-athletes.