Journal of Sports & Entertainment Law
HARVARD LAW SCHOOL

The Tax Consequences of Catalyzed Fans

Adam Chodorow*

This article, in honor of Dan Markel, explores the tax issues that would arise were fans to band together as a Fan Action Committee (FAC) to offer players additional compensation or a donation to a favored charity as an incentive to sign with the fans' team, the proposal at the heart of one of Dan's last articles. Both the direct compensation and charitable models raise questions regarding whether the players and owners have income, the tax consequences for the FAC of both contributions and distributions, and the fans' ability to deduct contributions to the FAC. Exploring these questions will help pave the way for FACs to move from academic discourse to the real world, offers the opportunity to consider a number of important tax policy issues that have far broader application, and seems like a wonderful way to honor Dan's memory.

I. Introduction

Dan Markel had an unquenchable desire to organize and connect people. If you were a legal academic over the past 10 years, Dan was either someone you knew or someone you knew about. Perhaps because we were in different fields (he in criminal law, I in tax), I fell into the latter category. That all changed in the summer of 2013, when we both attended the law and economics boot camp hosted by George Mason University School of Law, which, among its many virtues, brings together legal academics from a variety of fields. Dan was everything his reputation suggested, and more. The conference took place at Beaver Creek in Colorado, and, consistent with his reputation as a connector, Dan quickly organized a group of us to hike

* Professor of Law and Willard H. Pedrick Distinguished Research Scholar at the Sandra Day O'Connor College of Law at Arizona State University, Tempe, Arizona. I would like to thank Shu Yi Oei, Erin Scharff and Karen Bradshaw Schulz for comments on earlier drafts.

up the mountain after each session.[1] Consistent with his reputation as an intense intellectual, he insisted that we discuss our current scholarly projects, no mean feat when huffing and puffing up a mountain.

Calling us the 10,000 feet legal theory workshop, Dan marched over hill and dale as we talked about reshaping the joinder and claim preclusion rules,[2] considered how evidentiary rules might be changed to account for the ways that emotional influences subtly reshape jury perceptions,[3] and defended the propriety of writing about the tax consequences of a zombie apocalypse.[4]

Dan's contribution to the "workshop" was an interesting, off-topic article he was working on about how to involve fans in a team's decision whether to acquire or retain top talent.[5] The idea was that fans could form Fan Action Committees (FACs) and offer to pay players to sign with their team. Alternately, they could donate to a charity in the player's name.[6] Dan argued that fans should be considered third-party beneficiaries to the contract between the players and owner, and therefore they should have some say in the decisions that affected them. Dan always thought big, and he argued that this idea had applications far beyond sports teams.[7]

To a man with a hammer, every problem is a nail, and,as a tax professor, I have to admit that I fall prey to this tendency. Thus, when Dan began talking about the idea, I immediately began thinking of the tax consequences. Would amounts donated to charity be considered income to the player? Could the FAC deduct amounts transferred directly to the player or to charity? Could contributors to the FAC deduct amounts they gave?

While trying not to pass out from exertion (it was the altitude, I swear), I posed these and other questions to Dan, as others peppered him with their own questions. Despite Dan's focus on criminal law, he had a really good grasp of the tax questions. However, keen to get every last

1 The group consisted of Dan, Dan's Florida State colleague Mark Spottswood, Michael Mooreland at Villanova, Alan Trammell (the law professor, currently a Fellow at Columbia, not the former shortstop), and me.

2 Alan Trammell, *Transactionalism Costs*, 100 VA. L. REV. 1121 (2014).

3 Mark Spottswood, *Emotional Fact-Finding*, 63 U. KAN. L. REV. 41 (2014).

4 Adam Chodorow, *Death and Taxes and Zombies*, 98 IOWA L. REV. 1207 (2013).

5 Dan Markel et al., *Catalyzing Fans*, 6 HARV. J. SPORTS & ENT. L. 1 (2015).

6 This proposal could work equally for male or female athletes. However, given the dominance of male professional sports in the U.S., and to avoid confusion occasioned by switching back and forth, I will refer to the athletes as "he" throughout this article.

7 My personal favorite was fans banding together to induce a player to leave a hated enemy, but I was also taken by the idea of restaurant customers banding together to retain or attract a top chef.

detail correct, Dan put me in touch with his co-authors to explore further the issues we had discussed.

In the end, the article contained the following brief discussion of the tax issues raised by this innovative idea:

> This raises the final issue: If crowdfunded money is a supplement to that basic agreement, where should these funds go? We see two likely options.
>
> First is a direct compensation model, under which FACs pay the money directly to the star. This would be additional income for the player, comparable to outside income athletes regularly earn from endorsements and appearances. And it would be taxable as such; it comes attached to a quid pro quo ("We will give you this money if you sign with Team X"), making it compensation to the player as part of a market exchange, not a mere gift from the fans.
>
> Alternatively, under what we call the charitable model, FACs could give the money to a charity associated with the talent. . ..
>
> The charitable model may provide the additional benefit that money donated by fans to a charitable foundation will not (likely) qualify as income to the star, assuming the star is not directly coordinating with the fans or directing their contributions to any particular place. And because the money is going to charitable organizations, there is even some possibility that fan contributions will be tax deductible, as would an ordinary independent contribution to the player's foundation. The IRS might be suspicious of this arrangement, of course.[8] An alternative tax treatment would treat FAC donations as includable income to the talent and then tax-deductible (up to a point) by the talent as a charitable donation to his own foundation.
>
> . . .Seeing plausible arguments on both sides, we leave further exploration of the tax issues for another forum.[9]

---

[8] The authors elaborated on this point in a footnote: "The tax law issues raised here are somewhat tricky. On one hand, one might question whether fan contributions should be deductible. The *sine qua non* of a charitable contribution is that money or property is transferred without adequate consideration, meaning only "unrequited" payments qualify for deduction. This is determined by examining the external features of the transaction, without regard to the taxpayer's subjective motivations. FAC payments, even as charitable contributions, involve a *quid pro quo*—"here is money that we fans will donate to your foundation if you sign with the team."

That said, we can envision two arguments in favor of deductibility. First, any benefit to the donors is "intangible," merely the psychic benefit of having a great player on their team and giving their team a chance to win. Second, any such benefit is "incidental or tenuous," lacking any value so as to make the contributions a non-deductible purchase." Markel et al., *supra* note 5, at 11, n.26 (citations omitted).

[9] *Id.* at 11-12 (footnotes omitted).

I am honored to have the opportunity to take Dan and his co-authors up on the invitation to explore more fully the tax issues raised by this innovative proposal, and perhaps bring it one step closer to reality. In doing so, I hope to honor the memory of Dan and contribute in a small way to his legacy as a legal scholar.

II. The Tax Consequences of a Fan Action Committee. . .

A. *When a FAC Transfers Funds Directly to a Player*

Under the direct pay model, the FAC would agree to pay the athlete for signing with a team, raising a host of tax issues, including whether: (1) the player has income, (2) the owner has income, (3) the FAC has income on receiving the contributions or could deduct the payment to the player, and (4) the donors could deduct their contributions to the FAC. I address each in turn.

1. Player Income

Whether the player has income is the easiest of the questions to answer. Code Section 61[10] defines income broadly, and the Supreme Court has made clear that it includes any clearly realized accession to wealth.[11] Player receipt of a payment from a FAC is clearly an accession to wealth.

However, we need not rely on the broad, general definition of income. Although the player does not have a traditional employment relationship with the FAC, the transfer falls into the compensation category, explicitly included in income.[12] The player receives the payment for agreeing to sign with and play for the team.[13] In this regard, the payment is no different from a signing bonus.

As a matter of contract law, the FAC's offer to pay the player if he signs is a classic unilateral contract,[14] the acceptance of which occurs when the

---

[10] Unless otherwise specified, all code sections refer to the Internal Revenue Code of 1986, as amended.

[11] C.I.R. v. Glenshaw Glass, 348 U.S. 426 (1955).

[12] I.R.C. § 61(a)(1).

[13] For ease of reference, I will use the term "sign" to refer to both signing and playing.

[14] The Restatement (Second) of Contracts uses the term "options contract." However, that term seems confusing, given that actual options contracts exist, and I will stick to the old-fashioned term " classic unilateral contract" here.

player performs by signing with the team.[15] But what happens when a player signs with a team without regard for the offer? Could he claim that he hadn't earned the money and that it therefore couldn't be compensation?

For instance, the player might claim that he had no knowledge of the offer. This seems unlikely, given that the whole purpose of a FAC is to induce the player to sign. However, as a legal matter, lack of knowledge of an offer would defeat the formation of a contract.[16] The player could also disavow the offer before signing, thus giving up any contractual right to the payment.[17] Or the player could claim that, although he knew of the offer, it did not affect his decision to sign.[18]

While such claims may raise interesting questions of contract law, for tax purposes, the existence of a contract is not dispositive. Regardless of whether a player acted in expectation of being paid, he has income, with or without a contract, if he accepts the money.[19] Either it is compensation or an accession to wealth, which must be included in income absent an exemption.

The most promising tax-free category for the transfer would be a gift, but it does not fit within that category. As Markel and his co-authors note, whether a transfer qualifies as a gift is governed under the principles set forth in *Duberstein*.[20] Generally speaking, gifts proceed from disinterested generosity and do not involve a quid pro quo.[21] While the player might argue that *he* was not engaged in a quid pro quo, because he would have signed with the team regardless of the transfer, *Duberstein* makes clear that the analysis depends on the *donor's* intent. The very premise of the FAC is

---

[15] *See generally* Rene Wormser, *The True Conception of Unilateral Contracts*, 26 YALE L. J. 136 (1916). Much of the scholarly debate about unilateral contracts has focused on whether an offeror can withdraw the offer once someone begins to perform. That is not an issue for FACs.

[16] Glover v. Jewish War Veterans of the United States, Post No. 58, 68 A.2d 233 (D.C. 1949) (holding that a person must know about the offer to accept it through performance, at least in a private contract setting).

[17] *See, e.g.*, C.I.R. v. Giannini, 129 F.2d 638, 641 (9th Cir. 1942), Rev. Rul. 66-167.

[18] *See* Glover v. Jewish War Veterans of the United States, Post No. 58, 68 A.2d 233 (D.C. 1949) (noting that performance must be made with "the intention of accepting" an offer).

[19] A more interesting question arises if the player refuses to accept the money he has earned through performance. Some authorities suggest that he would have income, because disavowals must occur prior to earning the income. *See* Giannini, *supra* note . However, it seems wrong to assert that a player would have income if he refused to accept it.

[20] Markel et al., *supra* note 5, at 10.

[21] C.I.R. v. Duberstein, 363 U.S. 278, 285-86 (1960).

that it will pay the player if he signs, thus taking the transfer out of the gift realm, regardless of the player's intent.

No other exempt category suggests itself, leaving the transfer as income to the player, as Markel and his co-authors suggest.

2. Owners Income

A second question, and one that the authors do not address, is whether the *owners* would have income as a result of this transfer.[22] At first blush, it seems like a silly question. The deal as described in the article is between the player and the fans. The owners are third party beneficiaries at most and receive no money. However, they may have received a benefit. If the player would have signed regardless of the FAC's offer, the owners received no benefit and should not have income. If the player signed as a result of the extra money, the owners will get the player for less money than they would otherwise have had to pay. The question is whether this benefit rises to the level of income.

From a doctrinal perspective, taxpayers need not receive money to be considered to have received income. For instance, if someone satisfies a taxpayer's obligation, the payment is constructively seen as flowing through the taxpayer.[23] However, the owners were not relieved of an obligation under these facts, and therefore should not have income, at least under this theory. The owners may still benefit, but not all benefits create tax liability. I may benefit if my daughter earns money she can use to pay her tuition, but I do not have income. While the owners may be fortunate if a FAC steps in and pays a player, they should not be seen as having income.

The transaction could be reframed (either by changing the offer or recasting it) as a deal between the FAC and the owners, in which the FAC agrees to transfer funds to the player, if the owners will agree to sign the player. Such a framing would make the payment appear to be compensation for the owners' action, and not the player's. It seem likely that the IRS would try to recast the deal in this way. And even if the deal were structured or recast as a deal between the FAC and the owners, any income the

[22] This issue is somewhat analogous to the question addressed in the article regarding whether ancillary payments to players should count toward the salary cap. If the payments are deemed to flow through the owners to the players, they might count. However, if the owners are not considered to be in the loop, these payments should not be considered for salary cap purposes. Markel et al., *supra* note 5, at 16.

[23] *See, e.g.*, Old Colony Trust Co. v. C.I.R., 279 U.S. 716 (1929) (holding that employee has income when employer pays his tax liability).

owners would have would likely be offset by a deemed transfer of the funds from the owners to the player, which would be deductible as salary.[24]

3. FAC Income and Deductions

The next questions are whether a FAC would have income as a result of the contributions it receives and, if so, whether it could deduct the amounts it transfers to the player. The answer to the former depends in part on how the FAC is organized and how it receives the money. The answer to the latter depends on whether a deduction provision applies to this kind of transfer.

The article notes that a FAC:

> need not assume any particular form. It could be established either as a distinct organization or as an offshoot of an existing larger (unofficial) fan club. The FAC itself could be a formal legal organization or it could be one person or a group of individuals joined by physical or virtual space, reaching out and encouraging fundraising efforts among the fan base.. . .As with other mechanisms that channel money and influence, FACs likely would evolve over time, becoming more responsive, effective, and adaptable to changing free-agent markets and situations.[25]

Given the *ad hoc* nature of FACs, it seems likely that most would be loose collections of people contributing to the same cause, as typically happens on Kickstarter, Indiegogo, and other crowdfunding sites. However, in the interests of being thorough, I will consider the possibility that a FAC would organize as a formal entity.

To the extent that the FAC serves only as a conduit between the donors and the player, whether formally organized or not, it could likely avoid income in the same way that escrow agents do on the sums deposited with them. If they do not take title to the funds but rather hold them and then

[24] Another possibility is that the transfer could be viewed as a gift to the owners, with a corresponding transfer to the player. Under this approach, it could be tax-free to the owners, *see* I.RC. § 102, but create a deduction because the corresponding transfer would be seen as compensation. However, this result seems unlikely. As noted above, gifts typically involve disinterested generosity. The donors in this case are not disinterested. They are trying to induce the owner to sign the player and the player to stay. Thus, if the benefit were seen as flowing to the owners in a non-gift setting, there would be both income and an offsetting deduction.

[25] Markel et al., *supra* note 5, at 8.

pass them along to their rightful recipients, they shouldn't have income.[26] This seems the most likely outcome.

If the FAC takes title to the money, it clearly has an accession to wealth, and the question will be whether the contributions fall into a category exempt from income or whether the FAC itself is exempt from income tax. First, the contributions might be seen as gifts and therefore not taxable.[27] As discussed above, the outcome depends on whether there is a quid pro quo. The donors expect the FAC to aggregate the contributions and transfer them to the player if he signs. It is not clear whether such expectations are the kind of quid pro quo that defeats gift status. However, focusing on what the FAC will do with the money may not be appropriate. The purpose of the contribution is to induce the player to sign and will be made only if the player signs. This is a clear quid pro quo. Running the contribution through a FAC should not permit donors to avoid the underlying quid pro quo and turn their contributions into gifts.

Second, the FAC could organize as a for-profit business, such that the contributions could be considered tax-free contributions to capital.[28] While this might work, the difficulty is that the contributors would then be considered shareholders, partners, or members of the FAC. This could create significant management issues and seems an unlikely approach.[29]

Finally, the FAC could escape income if it obtains tax-exempt status. Contributions to a tax-exempt organization will not create tax liability for that organization.[30] As noted above, it seems unlikely that FACs will formally organize. Moreover, if they do, it seems highly unlikely that they would seek tax-exempt status, a process that takes significant time. However, they might. Code Section 501(c)(7) affords exemption for "clubs organized for pleasure, recreation, and other non-profitable purposes." However, donations to 501(c)(7) organizations are not tax deductible. Thus,

[26] In some cases, the FAC may collect only pledges that are fulfilled and immediately transferred when the player signs. Thus, it only has temporary control over the money.

[27] I.R.C. § 102.

[28] *See* I.R.C. § 721 and § 1032.

[29] Even if the FAC does not formally organize, there is some risk that the IRS could deem it to be a partnership for tax purposes, in which case I.R.C. § 721 might apply. Being deemed a partnership would also subject the FAC to all the reporting requirements imposed on partnerships. Given the lack of profits or profit sharing, this seems unlikely.

[30] There is a slim chance that contributions could be considered "unrelated business income," on which charities must pay taxes. I.R.C. § 511 *et seq*. This possibility seems very remote insofar as the whole point of the FAC is to raise funds to transfer to a player or a charity.

a FAC might try to organize under Code Section 501(c)(3). It seems highly unlikely that transferring funds to multi-million dollar athletes could ever qualify under that section.

If a FAC has no income, as seems likely, or if the FAC is tax exempt, deductions are not relevant. However, if the receipts are considered income subject to tax, deductions could prove quite valuable. Deductions are a matter of legislative grace.[31] Thus, the FAC would have to demonstrate that the transfer to the player fit within a statutory provision permitting a deduction. Unfortunately for FACs, the transfer would not likely qualify for a deduction.

The workhorse provision is Code Section 162, which permits a deduction for ordinary and necessary expenditures incurred as part of a trade or business. Even if FACs incorporate or organize as a partnership or LLC, they would likely not be considered to be engaged in a trade or business. Arguably, FACs are paying the owners' expenses, and the owners are clearly engaged in a trade or business.[32] However, it is well established that one cannot deduct the expenses paid on behalf of another.[33]

Code Section 212 permits a deduction for expenditures incurred for the "production or collection of income" or "for the management, conservation, or maintenance of property held for the production of income." However, FACs are not engaged in a for-profit activity. Their purpose is to induce a player to stay.

This leaves Code Section 183, which permits deductions to the extent of income from an activity, even absent a profit motive.[34] Deductions are allowed only if they would have been allowable had the activity been entered into for profit, that is, if it would have qualified for a deduction under Code Section 212 but for the lack of a profit motive.[35] If the transfer were viewed

[31] White v. U.S., 305 U.S. 281, 292 (1938). In some cases, Congress believes deductions to be constitutionally mandated. Accordingly, it permits a deduction for the cost of goods sold with regard to income from the illegal sale of drugs, while denying all other deductions. *See* I.R.C. § 280E.

[32] *See, e.g.*, Federal Baseball Club v. National League, 259 U.S. 200 (1922) (describing baseball as a business, but declaring it an intra-state business so as to avoid application of the Sherman Antitrust Act).

[33] *See* Welch v. Helvering, 290 U.S. 111 (1933).

[34] The goal is to offset income in situations where taxpayers have expenses so that they pay taxes only on true accessions to wealth. For instance, if Joey raises frogs for fun and pays $400/year for frog food, he can't deduct the cost because it is a personal expense. I.R.C. § 262. However, if he wins $300 in a frog-hopping contest, Code Section 183 permits him to deduct the costs to the extent of his gains, thus zeroing out his income from this activity.

[35] I.R.C. § 183(b)(2).

as an ordinary and necessary expense of the FAC (giving away money to induce a player to stay is the whole purpose for the FAC), the deductions would likely be allowed to the extent of any income.

It is hard to conceive of a FAC as a profit-seeking enterprise, or an organization with ordinary expenses, even if it has income as a result of donations. Simply put, Code Sections 162, 212 and 183 fit poorly, suggesting that there may be some merit to the argument Boris Bittker and George Rahdert raised years ago in defense of tax exemption, namely that the concept of profit makes little sense for organizations that solicit donations and give away the money they receive.[36]

One last point must be made. Assuming payment to a player could be considered a deductible expense, it could nonetheless be subject to capitalization if it created benefits that extended beyond 12 months.[37] For instance, if a FAC paid a player $5 million dollars for signing a 5-year contract, only $1 million might be deductible each year. Plumbing the depths of the capitalization rules is beyond the scope of this article.

4. Donor Deductions

The final question is whether those who donate to a FAC with the idea that the FAC transfer the money to a player if he signs would be entitled to a deduction. Unfortunately for donors, contributions would not likely qualify under any deduction provisions.

Donors, even more so than FACs, would not be considered to be engaged in a trade or business and thus would not qualify for a deduction under Code Section 162.[38] Nor would they qualify under Code Section 212 because they have no profit motive. Code Section 183 permits deductions for non-profit-seeking activities, but only to the extent of that activity's income. Donors have no income from this activity, and therefore Code Section 183 cannot help them.

The final possibility would be a deduction under Code Section 170, which permits deductions for charitable donations. For this to apply, the FAC would need to be recognized as a charity under Code Section 501(c)(3).

---

[36] Boris L. Bittker & George K. Rahdert, *The Exemption of Nonprofit Organizations from Federal Income Taxation,* 85 YALE L.J. 299 (1976).

[37] INDOPCO, Inc. v. Comm'r, 503 U.S. 79 (1992); Treas.Reg. § 1.263(a)-4.

[38] If the donor owns a business that benefits from the team's success, such as a parking lot near the stadium or arena, the donation could arguably be seen as a business expense, on the theory that retaining a player will be good for the donor's business. The ordinary and necessary requirement is fairly loose, but this may fall on the wrong side of the line.

As noted above, it seems highly unlikely that a FAC would organize as a corporation or seek tax-exempt status. Even if it did, it would not likely be granted tax-exempt status under Code Section 501(c)(3). Thus, charitable deductions are likely unavailable.

B. When a FAC Transfers Funds to a Charity

For a variety of reasons, the authors express a preference for the charitable model, under which the FAC would donate funds to a charity if the player signs with a team. The tax issues that arise under this model are more complex than under the direct compensation model and provide a wonderful opportunity to explore the assignment of income and constructive receipt doctrines, and the rules governing charitable deductions. More important, exploring these tax issues reveals a number of ways that FACs can minimize the tax risks to players and increase the chances that donors will be able to deduct their contributions. In particular, FACs should operate as conduits for donors and not as stand-alone entities. They should also make pledges to charities, as opposed to offers to players.

1. Player Income

The first question to be answered is whether the player has income if a FAC makes a charitable donation when he signs with a team. While it is true that the player receives no cash, the receipt of cash does not determine whether he has income.[39] The Supreme Court made clear in *Lucas v. Earl* that income is taxed to the person who earns it.[40] Thus, the question is whether a player signing with a team earns income when his signing triggers a donation to charity. As described in the article, the transaction is structured as a deal between the FAC and the player. However it could be structured (or recharacterized by the IRS) as a deal between the FAC and the owners or even between the FAC and the charity. The tax consequences to the player may well depend on how the transaction is structured or characterized.

a. FAC Offer to Player

If the FAC's offer is to the player, the issue will be whether the player has earned income and then assigned it to the charity. For instance, if I

---

[39] Old Colony Trust Co. v. C.I.R., 279 U.S. 716, 729-731 (1929).

[40] Lucas v. Earl, 281 U.S. 111 (1930) (holding that income earned by husband is taxed to husband despite contract between husband and wife to share it).

direct my employer to pay my salary to charity, whether before I earn it or after, I still have income. The transaction is simply recast as if the salary had been paid to me and I then donated it to the charity. In many cases, a charitable contribution deduction would offset the income, but not always.[41]

This outcome is made clear in Treasury Regulation 1.61-2, which addresses services contributed directly to a charity and situations where services are provided to a third party in return for a charitable donation. The former is tax free:

> Where, however, pursuant to an agreement or understanding, services are rendered to a person for the benefit of an organization described in section 170(c) and an amount for such services is paid to such organization by the person to whom the services are rendered, the amount so paid constitutes income to the person performing the services.[42]

Revenue Ruling 71, which considered an earlier version of this regulation, described a typical case in which the quoted language applied as one where a movie producer hires an artist and, by agreement with the artist, transmits the artist's payment to a charity picked by the artist.[43] In such cases, the artist has income and a corresponding charitable deduction.[44]

This regulation and ruling would appear to cover a player agreeing to sign with a team if a FAC donates to charity, even if it is the FAC that offers to donate, as opposed to the player insisting that the money go to charity. Nonetheless, the player might escape having income in two ways. First, the tax laws are often lenient regarding assignment when amounts are given to charity. While there is no statutory authority here, one can readily imagine the IRS using its administrative discretion to hold that the player has no income in such a situation. Second, one can always work for free, and play-

---

[41] The charitable deduction is only available to those who itemize. *See* I.R.C. §§ 62 and 67(b). Even for those who itemize, charitable deductions are capped at a percentage of a taxpayer's "contribution base." Thus, if the donation is too large relative to the taxpayer's income, the deduction would be limited, and any unused amounts would be carried forward. I.R.C. § 170(b). Finally, most itemized deductions, including charitable deductions, are reduced if a taxpayer's AGI exceeds $300,000, as adjusted for inflation. I.R.C. § 68.

[42] T.R. Sec. 1.61-2(c).

[43] C.B. 1953-1, 18. *See also* Rev. Rul. 77-290, 1977-2 C.B. 26. *But see* Rev. Rul. 57-135, 1957-1 C.B. 307, in which the IRS held that those who donated services to a charitable organization, which lent them out to other organizations and received donations in return, did not have wages for purposes of FICA.

[44] The ruling further states that an attempt to avoid this result by having the artist donate his services to the charity, which then lends the artist out to a movie producer in return for a donation, will yield the same result.

ers may be able to argue that they did not intend to accept the offer by signing and therefore didn't earn the income at issue.

i. Administrative Leniency

The assignment of income and constructive receipt doctrines are designed to prevent taxpayers from avoiding tax when they earn income and yet receive no cash. Typically, this occurs when employers agree to satisfy a taxpayer's obligations,[45] the taxpayer directs the employer to transfer amounts earned to someone else,[46] or where the taxpayer had the right to be paid but opted not to collect. When taxpayers instruct their employers or others to transfer amounts they earn to charities, many of the concerns that motivate the doctrines are reduced. While not a perfect offset,[47] the charitable deduction often leads to the taxpayer having no income.[48] Perhaps in light of this, Congress has created a number of exceptions to the rules. For instance, certain direct distributions from IRAs to charities are excluded from income entirely, rather than included and then deducted.[49] The same treatment applies to certain prizes donated to charity.[50]

No statutory provision applies to FACs. However, the IRS has significant leeway when it comes to applying the doctrines. Sometimes the leniency is formal.[51] For instance, after Hurricanes Katrina and Sandy and after 9/11, the IRS issued notices permitting direct donations of employee salaries to be excluded from the employee's income and precluding a charitable deduction.[52] It has done the same where professors and doctors assign certain outside income they earn to their employers.[53]

At others, it is more informal. For instance, the IRS is unlikely to rule that you have income when I promise to donate to charity if you complete a walk-a-thon, shave your head, or pour ice water over your head. Many em-

---

[45] Old Colony Trust Co. v. C.I.R., 279 U.S. 716 (1929).

[46] C.I.R. v. Giannini, 129 F.2d 638, 641 (9th Cir. 1942).

[47] *See* Lucas v. Earl, 281 U.S. 111 (1930).

[48] Charitable deductions do not offset payroll obligations. Thus, an amount included in income and then deducted in full will still lead to payroll tax liability.

[49] I.R.C. § 408(d)(8). This provision expired on December 31, 2013, but it may be resurrected and possibly made permanent.

[50] I.R.C. § 74(b).

[51] Bloomberg BNA Portfolio TM 502.

[52] Notice 2012-69, 2012-51 I.R.B. 712 (Hurricane Sandy); Notice 2005-68, 2005-40 I.R.B. 622 (Hurricane Katrina); Notice 2003-1, 2003-2 I.R.B. 257, modifying and superseding Notice 2001-69, 2001-46 I.R.B. 491 (Sept. 11, 2001, terrorist attacks); Notice 2001-69, 2001-46 I.R.B. 491 (Sept. 11, 2001, terrorist attacks).

[53] Rev. Rul. 74-581; GCM 39028 (IRS GCM), 1983 WL 197934.

ployers will match employee donations to charities. This is clearly a fringe benefit provided to employees. However, rather than include the match in the employee's income and then allow a deduction, if appropriate, the IRS simply excludes the match from income.

Ideally, if fans begin to form FACs, the IRS will issue formal guidance as to whether players have income under these circumstances.[54] If not, the question will come down to whether a player signing is more like traditional income earned and then donated to charity, or an act, such as shaving one's head, that leads to a charitable donation. Unlike most of the assignment cases, the player is not an employee of, or performing services for, the FAC or ultimate donors. . However, the player's signing is more than a dare or challenge that is typical of the informal rule that preserves the charitable donation for walk-a-thons and the like. The player is engaged in a recognized commercial activity for which he typically gets paid . . . a lot. If nothing else, this would make a great exam question.

ii. Disavowal

A second way in which a player might avoid income is to argue that he has not actually earned the income in question and therefore cannot have assigned it. One can always work for free, and the case law permits an employee to avoid income if he disavows his salary *before* earning it and exercises no control over where it goes.[55] Indeed, the seminal case in the area involved a bank executive who, half-way through the year told his employer that he would work for free for the rest of the year and that his employer should do something useful with the salary he would have earned. The employer donated the foregone salary to the University of California at Berkeley to establish a Foundation of Agricultural Economics in the employee's name. The IRS argued that the employee should include the donation in income and take a corresponding deduction. However, the court sided with the taxpayer and held that the disavowal before the income was earned, coupled with the purported lack of control, defeated the claim that the salary should be included in the employee's income.[56]

Just what constitutes control has not been developed in the case law. The IRS has held that knowledge of what will happen to the money if it is

[54] FACs could always seek Private Letter Rulings, but they are expensive and take time. Given the likely ad hoc nature of FACs, this path may not work.

[55] C.I.R. v. Giannini, 129 F.2d 638, 641 (9th Cir. 1942).

[56] *Id.*

disavowed does *not* rise to the level of control.[57] However, it is uncertain whether disavowal and a suggestion, strong or otherwise, of where the funds should go would permit a taxpayer to escape income under *Giannini*. Norms can be as strong as legal obligation, and a rule based solely on legal control permits significant game playing by those seeking to avoid income.

The acceptance mechanism involved with unilateral contracts and the fact that the benefit was never supposed to be paid to the player make it unclear how these principles will play out in the FAC context. If the player signs with the team in response to the FAC's offer, it seems clear that the player has income. Signing constitutes acceptance, and a binding contract is formed. The benefit that flows directly to the charity would be seen as a quid pro quo for signing and would be re-characterized as flowing first to the player and then to the charity. The only out would be IRS leniency of the type described above.

It gets far more complicated when a player signs with a team purportedly without regard for the offer. If the player could demonstrate that he had no knowledge of the offer, he cannot be said to have exchanged his performance for the offer. No contract was formed, and the player has no legal right to force the FAC to donate.[58] Thus, he has not earned any benefit. It seems wrong to claim that player has income as a result of a transfer of which the player had no knowledge.

A harder case is where the player knew of the offer at the time he signed but claims that it did not affect his decision. Typically, assignment of income depends on the existence of a contractual right to be paid or the control over where the money goes. Indeed, this is what distinguishes *Lucas v. Earl* from *Giannini*. In the former case, Mr. Earl performed the work and had a contract right to the income against his employer, even though he had assigned his right to half the income to his wife in a side deal. In the latter case, Mr. Giannini disavowed any right to the income before performing the work. Thus, although the donation is connected to the work he did, he does not have income.

As a matter of contract law, if a player signs without an intent to accept the FAC's offer, no contract is formed, and the income cannot be said

[57] Rev. Rul. 66-167 (executor who states up front that he will not accept payment does not have income even though he knows that the foregone income will be split between himself and his son as a tax-free inheritance).

[58] Glover v. Jewish War Veterans of the United States, Post No. 58, 68 A.2d 233 (D.C. 1949) (holding that a person has to know about the offer to accept it through performance, at least in a private contract setting).

to have been earned.[59] However, unlike the direct pay model, where the player could simply refuse to accept money he has disavowed, in the charity model, here the player gets precisely what he would have received had he signed with the intent to create a contract, that is, a donation to charity. Arguably, this is equivalent to rejecting the offer in the direct pay model and yet still receiving the FAC's payment, which in that context leads to income.[60]

It may well be that the bright-line test focused on the existence of a contract right to enforce the payment is the best rule. In such case, one might require an express disavowal before signing to avoid the evidentiary problems associated with the ex post claim that the offer did not motivate the signing.[61] However, this could create a trap for the unwary. Alternately, one could create a special rule for FACs, such that the donations will not be deemed to flow through the player, regardless of any contract rights. If we assume that the income will largely be offset by a corresponding charitable donation deduction, little harm will be done to the public fisc. Either way, clear guidance from the IRS would be helpful.

b. FAC Offer to Owners

The FAC could make its offer to the owners instead of the player. If the owners sign the player, the FAC will donate to charity. Thus, the owners could "earn" the donation by performing. The analysis under this scenario is the same as for offers made to the player.

---

[59] *See* Glover v. Jewish War Veterans of the United States, Post No. 58, 68 A.2d 233 (D.C. 1949).

[60] Rev. Rul. 66-167 might permit the player to avoid tax on the theory that knowing where the money will go is not the same as earning it and directing its disposition. A player who disavows a FAC's offer knows that the FAC will donate regardless of his disavowal. Under the ruling, this knowledge should not amount to control or otherwise create income for him absent a contract right to the income. The key difference between Rev. Rul. 66-167 and the charity model is that, in the charity model, the player receives the exact same thing – a donation to charity – whether he accepts the offer or not. Thus, it is not simply a case of knowing where the money will go, but rather a question of whether the disavowal actually alters the benefit received.

[61] Even if the player disavows the obligation and cannot be said to receive the payment, he receives some benefit. As the authors note, "[a]lthough stars do not receive anything from fan donations, FACs still are offering something of value to the player (even if the value is purely psychological or moral) to persuade him to play for one team over another." Markel et al., *supra* note 5, at 37. If the player has no direct income because of the disavowal, it seems unlikely that these more amorphous benefits would be considered income.

c. FAC Pledge to Charity

Finally, the deal could be structured or recast as between the FAC and the charity to which the money will be donated. In essence, the FAC would pledge to the charity that it will make a donation if the player signs. While such a pledge would lack consideration, such pledges are often enforceable, either because of some actual or presumed reliance.[62] While the player has to perform to trigger the obligation to donate, he is not performing services in return for the donation and therefore likely need not include it in income. For instance if I pledge to donate $100 to the American Red Cross if the Padres win the World Series and they actually win (an admittedly wishful hypothetical), the Padres should not have income when I make good on that pledge. This should be true even if they learned of my pledge and it motivated them to win. Structuring the deal this way makes it look more like a walk-a-thon pledge, for which no income is typically recorded.[63]

The outcome here may inform one's thinking about the other structures discussed above. That this form would likely avoid tax to the player strongly supports the notion that the IRS look leniently on the deal if it is structured as an offer directly to the player.

2. Owners' Income

The analysis of whether owners have income as a result of a FAC's donation to a charity is the same as that above. If the deal is with the player, the owners are not being relieved of any obligations under the deal described in the article. Any benefit they receive is tangential. However, were the deal structured as a promise from the FAC to the owners, then the owners might earn the donation by signing the player. Even if the owners were seen to earn income, they would likely have an offsetting deduction,

---

[62] Allegheny College v. National Chautauqua County Bank of Jamestown, 159 N.E. 173 (N.Y. 1927) (actual reliance substitutes for consideration); Rest. 2d Contracts § 90, Pt. 2 (reliance presumed for charitable pledges); Salsbury v. Northwestern Bell Telephone Co., 221 N.W.2d 609 (Iowa 1974) (finding reliance to be presumed in charitable subscription cases, where the pledge is evidenced in writing). *But see* Congregation Kadimah Toras-Moshe vs. DeLeo, 405 Mass. 365 (1989) (involving an oral pledge, but also upholding a requirement of detrimental reliance).

[63] In this example, the Padres are not performing services for me. Nor are they completely in control of whether they perform. As described above in Part II.B.1.a., if services are provided to me in return for a donation, I will be seen as paying for the services and therefore not entitled to a deduction.

either as compensation to the players who would get an offsetting charitable deduction, or as a direct charitable donation.

3. FAC Income and Deductions

The issue of whether the FAC has income is the same as in the direct pay model, discussed above in Part II.A.3. However, the argument that the FAC could qualify as a 501(c)(3) organization might be stronger. Instead of collecting funds to be transferred to a player, FACs would be aggregating donations to be given to a charitable organization. Thus, they might have a stronger claim that they have a charitable purpose and that there is no private inurement or benefit.[64] They might also have a stronger claim to conduit status.[65]

If the FAC is somehow deemed to have income, it would need to find a deduction provision that covers the payment to the charity. Unlike the analysis above in Part II.A.3, which focused on business and related deduction provisions, here Code Section 170 might permit a deduction. However, if the transfer is deemed a payment to the athlete, with a corresponding transfer to the charity, as discussed above in Part II.B.1, the athlete, not the FAC, would be entitled to the charitable deduction. If the donation is viewed as a donation to charity, but one involving an impermissible quid pro quo, as discussed below in Part II.B.4, no charitable deduction would be allowed. However, the FAC might be allowed a deduction under Code Section 183, to the extent of any income.

4. Donor Deductions

The case for a deduction for contributors to a FAC is more complicated when the money goes to a charity. While no business-like deduction would be available, donors might be able to claim a deduction under Code Section 170. As before, the answer depends on a variety of factors, including how the FAC is organized, whether the player is deemed to have income, and whether the donation is made with an impermissible quid pro quo in mind.

If the FAC is organized as a 501(c)(3) organization, then donations would likely be deductible under Code Section 170. If the FAC is not a

---

[64] The key issue would be whether the desire to induce the player to sign with the team is a substantial non-exempt purpose, which would defeat tax exemption. *See* Better Business Bureau of Washington D.C. v. United States, 326 U.S. 279 (1945).

[65] *See, e.g.*, Rev. Rul. 77-121, 1977-1 C.B. 17, in which the IRS held that a racetrack that acted as an agent for a charity in hosting a charity day at the track did not need to include the amounts donated to charity in income.

501(c)(3) organization, as will almost certainly be the case, it gets more difficult. A charitable deduction might be appropriate if the FAC were seen as a mere conduit, such that the donation to the FAC were understood to be a direct donation to the charity.[66] However, this option would be possible only if the player were deemed not to have income. If the player is deemed to have income, the player would be deemed to be making the donation, precluding a deduction by any FAC contributors.

At the heart of the deduction for charitable donations is the notion of donative intent, coupled with the related idea that deductions are appropriate when donors do not receive anything back, i.e., when there is no quid pro quo.[67] The easy case is where I purchase a $50 jacket from the American Red Cross, paying $50. Clearly, I have not made a deductible contribution. I received equal value back and cannot deduct the payment. At the other end of the spectrum, and equally easy, is where I simply give the American Red Cross $50 and receive nothing in return. While I may get a warm glow from giving, that glow does not rise to the level of a quid pro quo that defeats a charitable deduction.[68]

The more difficult case is where the donor receives something more substantial back. Where the donor receives goods and services, the contribution is deductible to the extent that it exceeds the market value of what is received in return. However, the donor must intend that the amounts paid in excess of the goods and services received be a donation.[69]

The receipt of intangible items poses more difficulties, both because they are hard to value and, as Markel and his co-authors note, not all intangibles received are considered to constitute a quid pro quo.[70] The most notorious example is naming rights. For instance, in return for a donation of $50 million, Drexel University recently agreed to name its law school after Thomas R. Kline.[71] By all rational accounts, this is a quid pro quo,[72] but it is not treated as such for tax purposes, though many think it should

---

[66] Plumbing the depths of the conduit theory is beyond the scope of this article.

[67] United States v. American Bar Endowment, 477 US 105 (1986).

[68] For a discussion of warm glow, *see* M. Todd Henderson & Anup Malani, *Corporate Philanthropy and the Market for Altruism*, 109 COLUM. L. REV. 571 (2009).

[69] *Id.*

[70] Markel et al., *supra* note 5, at 11, n.26.

[71] Jeff Blumenthal, *Drexel Law gets $50M gift, the largest ever for the university*, PHILA. BUS. J. (Sep. 18, 2014, 6:00 PM), http://www.bizjournals.com/philadelphia/news/2014/09/17/drexel-law-gets-50m-gift-the-largest-ever-for-the.html?page=all, *archived at* http://perma.cc/FZ89-QQDT.

[72] In commercial settings, businesses pay significant sums for signage and naming rights for buildings. *See, e.g.* Ryan Sharrow, *Ripken Stadium naming rights up for sale in Aberdeen*, BALT. BUS. J. (Aug 4, 2014, 7:40 AM), http://www.bizjournals.

be.[73] However, other examples exist, including acknowledgement of sponsors on public TV and radio and access to facilities or events unavailable to non-donors.

In the case of donations to FACs that are subsequently transferred to a charity, the issue is whether an agreement to give conditioned on a player's signing rises to the level of a quid pro quo that would defeat a deduction, either to a tax-exempt FAC or the ultimate charitable recipient. The quid pro quo need not come from the charity directly. Under *Singer v. U.S*, the question is whether the purported donor received something of value for his donation, above and beyond the benefits that inure to the public generally.[74]

As a practical matter, it is seldom the case that promises to donate if someone else performs some act defeat a charitable deduction. For instance, if I promise to donate $100 to KJZZ, my local public radio station, if you shave your head, I am really paying you to shave your head. Theoretically, you should have income of $100, along with a $100 deduction. However, it seems highly unlikely that the IRS would attempt to re-characterize the transaction in this manner. Instead, I would be seen as making the donation and allowed to deduct it.

A player signing with a team in return for a donation is arguably a difference in degree as opposed to kind, but, as Stalin is rumored to have said in response to criticism of Russia's plentiful but low-quality airplanes, quantity has a certain quality of its own. When the amount at issue is counted in the millions, the IRS may not be willing to overlook the exchange. However, it might be a difference in kind, regardless of the size. Shaving your head is not a commercial activity. In contrast, a player signing with my team is engaged in a regular commercial transaction and arguably

---

com/baltimore/news/2014/08/04/ripken-stadium-naming-rights-for-sale-aberdeen .html?page=all, *archived at* http://perma.cc/7DYK-XH8W.

[73] *See, e.g.*, John D. Colombo, *The Marketing of Philanthropy and the Charitable Contributions Deduction*, 36 WAKE FOREST L. REV. 657 (2001) (arguing that donations in return for naming rights should not lead to charitable deductions). Interestingly, the special status for naming rights tracks that found in Jewish law, which sets forth a hierarchy of charitable giving. *See* Adam Chodorow, *Maaser Kesafim and the Development of Tax Law*, 8 FL. TAX REV. 153, n.25 (2007); SHIMON TAUB, THE LAWS OF TZEDAKAH AND MAASER: A COMPREHENSIVE GUIDE 39-43 (Mesorah Publications, Ltd. 2001). Ideally, one is supposed to do charity anonymously. The one major exception is for donating money to a yeshiva or schul. In such cases, one is permitted to attach one's name to the gift in the hopes that others will be inspired to do the same. *Id.* at 47-48. While this information may seem somewhat off the point, Dan was religiously committed and deeply interested in Jewish law. I'm sure he would have appreciated it.

[74] Singer Co. v. United States, 449 F.2d 413, 423 (1971).

provides a more concrete benefit to me. Nonetheless, these benefits accrue to all and likely do not qualify as a quid pro quo under the rule in *Singer*.

The intersection of the income and charitable deduction analyses provides one final quid pro quo consideration. To claim a deduction, donors would have to clear two hurdles, both of which seem to use a quid pro quo standard. First, the donation must not be deemed a payment to the player for signing. Second, the contributors would have to establish that they gave without an expectation of a quid pro quo and did not, in fact, receive one. This suggests that a failure to find player income guarantees a finding that the donation is deductible. After all, if there is no quid pro quo between the player and the donor for determining income, it seems there should be no quid pro quo between the player and the donor for determining whether a charitable deduction is appropriate. However, these two standards may not be the same. The former arises from the assignment of income jurisprudence and focuses on the reputed earner's contractual rights to income and control over its disposition. The latter arises from the law of gifts, charitable and otherwise, and looks to the donor's intent and whether he expected and received something in return for the donation.

Insofar as the critical fact under each standard is the athlete's signing, a rule that required consistent results would seem appropriate. However, one can easily imagine a scenario where the signing does not create contractual rights (whether because the athlete was unware of or disavowed the offer), thus defeating income for the athlete, but where that same signing, and the donor's conditioning the donation on it, is an impermissible quid pro quo, thus defeating a charitable deduction. However, the lack of a specific benefit that accrues primarily to the donor likely precludes this result in this case.

Should FACs become a reality, IRS guidance on these issues would be quite helpful.

III. Conclusion

Dan Markel will be remembered in the legal academy for a variety of contributions. While his primary focus was criminal law, his interests were far broader, as is clear from this article on FACs. Catalyzing fans to get involved in decisions about which talent to go after or retain is a fascinating idea that raises a host of interesting tax questions. Dan and his co-authors (probably wisely) decided to identify a couple of those issues and then set them aside for further thought and analysis. I am honored and grateful to have had the opportunity here to expand on these issues and perhaps bring Fan Action Committees one step closer to reality.