

FINAL PRIVATE LETTER RULING

11-004

MEMORANDUM

To: File

From: Utah State Tax Commission

Date: January 24, 2012

Re: PLR 11-004

Private Letter Ruling 11-004 addresses the issues and facts provided verbally by NAME 1 with COMPANY 1; this ruling does not directly respond to NAME 1's written request letter, which has been included for reference only. After the Utah State Tax Commission received NAME 1's written request letter, NAME 1 explained and clarified the facts and issues for the private letter ruling through subsequent telephone conversations.

NAME 1 provided the following facts. COMPANY 1 prepares returns for many professional athletes and currently has questions about the Utah income tax treatment of the signing bonuses paid to non-Utah resident athletes. Various states treat the bonuses differently. In the past three years, COMPANY 1 has had many non-Utah resident clients who received signing bonuses and also income earned from playing in Utah. Additionally, some of the athletes' employers are not allocating signing bonuses according to duty days under Utah Admin. Code R865-9I-44 ("Rule 44") but are instead allocating the total signing bonuses to Utah when the teams to which the athletes are first assigned are located in Utah. These employers are reporting the entire signing bonuses as Utah income on the athletes' W-2s and also on the reports to the Utah Department of Workforce Services. These employers, who are not following Rule 44, might be instead following an internal agreement they made with the other teams in the league. The tax preparers at COMPANY 1 want to know the correct treatment of signing bonuses under Utah law. These tax preparers intend to allocate future signing bonuses for Utah returns according to this private letter ruling and also to attach a copy of this ruling and a copy of their allocation calculations to those returns. COMPANY 1 is not asking how to make specific calculations under Rule 44; instead, it wants this ruling to focus on the general applicability of Rule 44 to the situation presented.

NAME 1 provided the following two issues:

- A. For Utah, is the signing bonus part of the total compensation that is allocated according to duty days under Utah Admin. Code R865-9I-44 ("Rule 44")?

- B. Does the Utah State Tax Commission always accept a duty day calculation that follows Rule 44 when that allocation is prepared by a nonresident professional athlete, i.e. taxpayer?

Private Letter Ruling 11-004 addresses the facts and issues as explained above.

REQUEST LETTER
(Included for Reference Only)

August 10, 2011

Private Letter Ruling
Audit Department
Utah State Tax Commission
210 N. 1950 W
Salt Lake City, UT 84134

RE: NAME 2
2010 Individual Income Tax
Account ID: ACCOUNT NUMBER

To Whom It May Concern:

The above-referenced individual filed his 2010 Utah State return in April, 2011. We have received several notices from Utah (Letter IDs: L0888430208 and L1081466496) that unfairly tax all NAME 2's wages in Utah when he is a STATE 1 resident and a non-resident professional athlete (drafted by PROFESSIONAL TEAM 1 in 2010).

We have enclosed additional information that we would like to present in NAME 2's 2010 situation. Utah Section R865-9I-44 discusses Compensation Received by Nonresident Professional Athletes and specifically defines "duty days", "total compensation" and also states that the "purpose of the rule is to apportion to the state, IN A FAIR AND EQUITABLE MANNER, a nonresident member of a professional athletic team's total compensation for services rendered as a member of a professional athletic team."

We are therefore submitting an alternative allocation of Utah income for NAME 2's 2010 season based upon those rulings (copy attached). I have also submitted a copy of the BASEBALL LEAGUE 2010 schedule and a revised 2010 Utah Form TC-40 and TC-40B. Finally, a copy of NAME 2's W-2 showing TOTAL WAGES allocated to both Utah and STATE 1 and Addendums A, B and C-1 from NAME 2's contract are enclosed as proof of his bonus and when he signed and reported.

As you can see, this revised return results in a refund of NUMBER AMOUNT and is, in our opinion, a fair and equitable calculation. If Utah does not agree with this submission, then as stated under R865-9I-44(2), "the commission may require the member of a professional athletic

team to apportion that compensation under a method the commission prescribes, as long as the prescribed method results in a fair and equitable apportionment”.

We request a Private Letter Ruling on this matter to accept our revised return based on the guidelines outlined in R865-9I-44 or provide an alternate method that is fair and equitable.

Sincerely,

NAME 1, EA

Enclosures

RESPONSE LETTER

January 24, 2012

NAME 1, EA
COMPANY 1
ADDRESS 1
CITY, STATE ZIP CODE

RE: Private Letter Ruling Request—Individual Income Tax: Applicability of Utah Admin. Code R865-9I-44 to a Nonresident Professional Athlete for the Situation Presented

Dear NAME 1:

Through your letter dated August 10, 2011 and through subsequent telephone conversations, you have requested a ruling on behalf of the nonresident professional athletes for whom you prepare income tax returns. Your specific issues for this ruling are:

- A. For Utah, is the signing bonus part of the total compensation that is allocated according to duty days under Utah Admin. Code R865-9I-44 (“Rule 44”)?
- B. Does the Utah State Tax Commission always accept a duty day calculation that follows Rule 44 when that allocation is prepared by a nonresident professional athlete, i.e. taxpayer?

You explained that you prepare returns for many professional athletes and you have questions about the Utah income tax treatment of the signing bonuses paid to non-Utah resident athletes. You indicated that various states treat the bonuses differently. You also explained that in the past three years, you have had many non-Utah resident clients who received signing bonuses and also income earned from playing in Utah. Additionally, you explained that some of

the athletes' employers are not allocating signing bonuses according to duty days under Utah Admin. Code R865-9I-44 ("Rule 44") but are instead allocating the total signing bonuses to Utah when the teams to which the athletes are first assigned are located in Utah. These employers are reporting the entire signing bonuses as Utah income on the athletes' W-2s and also on the reports to the Utah Department of Workforce Services. You explained that these employers who are not following Rule 44 may be instead following an internal agreement they made with the other teams in the league. You further indicated that you want to know the correct treatment of signing bonuses under Utah law, that you intend to allocate future signing bonuses for Utah returns according to this private letter ruling, and that you plan to attach a copy of this ruling and a copy of your allocation calculations to those returns. You also said you are not asking how to make specific calculations under Rule 44; instead, you want this ruling to focus on the general applicability of Rule 44 to your situation.

I. Applicable Law

Utah Code § 59-10-116 imposes Utah income tax on nonresident individuals' Utah state taxable income. Sections 59-10-117 and 59-10-118 explain the calculation of Utah source income, which affects the computation of a taxpayer's Utah state taxable income.

Utah Administrative Code R865-9I-44 (Rule 44) provides a duty day calculation for Utah source income earned by nonresident professional athletes, stating in part:

(1) Definitions.

(a) "Duty days" means all days during the taxable year from the beginning of the professional athletic team's official preseason training period through the last game in which the team competes or is scheduled to compete.

(i) Duty days includes:

(A) days on which a member of a professional athletic team renders a service for a team on a date that does not fall within the period described in Subsection (1)(a), for example, participation in instructional leagues, the Pro Bowl, or promotional caravans. Rendering a service includes conducting training and rehabilitation activities, but only if conducted at the facilities of the team; and

(B) game days, practice days, days spent at team meetings, promotional caravans, and preseason training camps, and days served with the team through all postseason games in which the team competes or is scheduled to compete.

(ii) Duty days for any person who joins a team during the season shall begin on the day that person joins the team, and for a person who leaves a team shall end on the day that person leaves the team. If a person switches teams during a taxable year, a separate duty day calculation shall be made for the period that person was with each team.

(iii) Days for which a member of a professional athletic team is not compensated and is not rendering services for the team in any manner, including days when the member of a professional athletic team has been suspended without pay and prohibited from performing any services for the team, shall not be treated as duty days.

(iv) Days for which a member of a professional athletic team is on the disabled list shall be presumed not to be duty days spent in the state. They shall, however, be included in total duty days spent within and without the state.

(v) Travel days that do not involve either a game, practice, team meeting, promotional caravan or other similar team event are not considered duty days spent in the state, but shall be considered duty days spent within and without the state.

....

(d) "Total compensation" includes salaries, wages, bonuses, and any other type of compensation paid during the taxable year to a member of a professional athletic team for services performed in that year.

(i) Total compensation does not include strike benefits, severance pay, termination pay, contract or option-year buyout payments, expansion or relocation payments, or any other payments not related to services rendered to the team.

(ii) For purposes of this rule, "bonuses" subject to the allocation procedures described in Subsection (5) are:

(A) bonuses earned as a result of play during the season, including performance bonuses, bonuses paid for championship, playoff or bowl games played by a team, or for selection to all-star league or other honorary positions; and

(B) bonuses paid for signing a contract, unless all of the following conditions are met:

(I) the payment of the signing bonus is not conditional upon the signee playing any games for the team, or performing any subsequent services for the team, or even making the team;

(II) the signing bonus is payable separately from the salary and any other compensation; and

(III) the signing bonus is nonrefundable.

....

(3) If a nonresident member of a professional athletic team demonstrates that the method provided under this rule does not fairly and equitably apportion compensation, that member may submit a proposal for an alternative method to apportion compensation. If approved, the proposed method must be fully explained in the nonresident member of a professional athletic team's nonresident personal income tax return for the state.

....

(5) Nonresident professional athletes shall keep adequate records to substantiate their determination or to permit a determination by the commission of the part of their adjusted gross income that was derived from or connected with sources in this state.

(6) The Utah source income of a nonresident individual who is a member of a professional athletic team includes that portion of the individual's total compensation for services rendered as a member of a professional athletic team during the taxable year which, the number of duty days spent within the state rendering services for the team in any manner during the taxable year, bears to the

total number of duty days spent both within and without the state during the taxable year.

(7)(a) Professional athletic teams shall withhold and remit tax on behalf of nonresident professional athletes on a form prescribed by the commission.

(b) A schedule shall be included with the return, listing all of the following information for each nonresident member of a professional athletic team:

(i) name;

(ii) address;

(iii) social security number;

(iv) income attributable to Utah for the nonresident member of a professional athletic team;

(v) total compensation paid to the nonresident member of a professional athletic team by the professional athletic team;

(vi) the nonresident member of a professional athletic team's duty days both within and without the state;

(vii) the nonresident member of a professional athletic team's duty days within the state;

(viii) Utah tax deducted and withheld; and

(ix) federal income tax deducted and withheld.

....

II. Analysis

Below is a discussion of your two issues:

A. For Utah, is the signing bonus part of the total compensation that is allocated according to duty days under Utah Admin. Code R865-91-44 ("Rule 44")?

A signing bonus is part of a nonresident athlete's total compensation that is allocated according to duty days unless that bonus meets the three conditions listed in Rule 44(1)(d)(ii)(B).

According to Rule 44 subsection (1)(a), duty days are generally defined as "all days during the taxable year from the beginning of the professional athletic team's official preseason training period through the last game in which the team competes or is scheduled to compete." Subsections (1)(a)(i) through (1)(a)(v) provide further direction on what specifically is or is not a duty day. For example, under subsection (1)(a)(i)(A) a date that does not fall within the period described in subsection (1)(a) can still be a duty day if a professional ballplayer renders a service for a team on that day, such as by participating in a promotional caravan.

Rule 44(6) provides the duty day calculation, through which a part of an athlete's total compensation is Utah source income. Rule 44(1)(d) defines total compensation to include bonuses. Under Rule 44(1)(d)(ii)(B), bonuses include signing bonuses unless the following three conditions are met:

- (I) the payment of the signing bonus is not conditional upon the signee playing any games for the team, or performing any subsequent services for the team, or even making the team;
- (II) the signing bonus is payable separately from the salary and any other compensation; and
- (III) the signing bonus is nonrefundable.

Only when all of the three conditions are met are signing bonuses not part of the total compensation allocated according to duty days.

B. Does the Utah State Tax Commission always accept a duty day calculation that follows Rule 44 when that allocation is prepared by a nonresident professional athlete, i.e. taxpayer?

Under the circumstances, the Utah State Tax Commission will accept a duty day calculation that follows Rule 44 when the allocation is prepared by an athlete and reported according to Rule 44(3) unless that calculation does not fairly and equitably apportion the athlete's compensation.

Rule 44(7) requires professional athletic teams to withhold and remit tax on behalf of nonresident professional athletes based on duty days. When a professional team fails to follow Rule 44(7), an athlete may make and submit a duty day calculation that follows Rule 44. Rule 44(3) allows an athlete to propose an alternative method for apportioning compensation and instructs how this can be done. Rule 44(3) requires an athlete to demonstrate that the method provided in Rule 44 does not fairly and equitably apportion the compensation. Your clients could demonstrate this by showing their employers are not following Rule 44(7). Furthermore, Rule 44(3) allows a taxpayer to propose an alternative method. Your clients are proposing an alternative method when they perform the calculations themselves instead of accepting the employers' reported information. Lastly, Rule 44(3) requires athletes to include a full explanation of their proposed method and their calculations. Your plan to attach a copy of this ruling and a copy of your detailed calculations would help your clients meet this requirement.

However, even if your clients apportion their compensation according to Rule 44 and also follow Rule 44(3) providing the required explanations, the Utah State Tax Commission still cannot guarantee that its Processing Division will initially accept their returns. The information submitted by your clients will conflict with the information reported by their employers on the athletes' W-2s and also to the Utah Department of Workforce Services. Because of this mismatch, your clients may continue to get notices and may still need to work with the Taxpayer Services Division to resolve the matters. The only way to prevent the notices is for the employers to follow Rule 44. Employers must report state income to each state according to that state's laws, not just according to any internal agreement among teams within a league.

Furthermore, in general, acceptance of returns by the Processing Division does not preclude subsequent reviews by the Auditing Division. Likewise in your situation, a calculation by either an employer or an employee may still be reviewed by the Auditing Division.

Lastly, this ruling does not find that the Utah State Tax Commission always accepts a duty day calculation prepared by a nonresident professional athlete. While under the facts of this ruling a duty day calculation prepared by an athlete appears to be appropriate, there potentially could be other factual situations in which a calculation by an athlete would not be appropriate. Calculations must always be fair and equitable—even when a professional team makes the calculations. *See* Rule 44(2).

III. Conclusion

This ruling is summarized as follows. First, a signing bonus is part of a nonresident athlete's total compensation that is allocated according to duty days unless that bonus meets all three of the conditions listed in Rule 44(1)(d)(ii)(B). Second, the Utah State Tax Commission will accept a duty day calculation that follows Rule 44 when that allocation is prepared by an athlete and reported according to Rule 44(3) unless that calculation does not fairly and equitably apportion the athlete's compensation. However, if there is a mismatch in information reported by the athlete and his or her employer, the athlete may need to work with the Taxpayer Services Division to resolve the matter. Also, calculations by an athlete or his or her employer may still be subsequently reviewed by the Auditing Division.

This ruling is based on current law and could be changed by subsequent legislative action or judicial interpretation. Also, our conclusions are based on the facts as described. Should the facts be different, a different conclusion may be warranted. If you feel we have misunderstood the facts as you have presented them, you have additional facts that may be relevant, or you have any other questions, you are welcome to contact the Commission.

For the Commission,

Marc B. Johnson
Commissioner

MBJ/aln
11-004