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US Tax Law Considerations for
Non-US Tax Resident International Athletes



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Plan of Action

- Discussion of General US Tax Law Principles of Interest to International Athletes
- Discussion of Retief Goosen Case
- Discussion of the Sergio Garcia Case

Consequences of US Tax Residence

A U.S. Tax Resident is subject to U.S. federal income tax on his or her worldwide income regardless of source

- Generally, this includes salaries, endorsement income, royalties, bonuses, dividends from U.S. and foreign companies, capital gains
- US federal tax rates of up to 40%+
- Tax is on the net – after deduction for expenses

Strategies do exist for minimizing US taxes for athletes who become US tax resident but these are not part of this discussion

Who Has US Tax Residence?

- US Citizen
- Green Card Holder – Permanent US Resident
- Substantial Presence Test – Complex test
 - 183 days or more presence in the US over 3 year period
 - Weighted:
 - Current year (2016) each day counts in full(provided more than 31 days)
 - Prior year (2015) each day counts as 1/3
 - Second Prior Year (2014) – each day counts as 1/6
 - So problem area can be for an athlete who trains or performs here for even as little as 32 days in the current year
 - There are exceptions to US tax residence where individual has a “tax home” or “closer connection” with foreign country for the current year – (See Appendix)

US Taxation of Non US Tax Residents

- In contrast, a Non US Tax Resident is subject to U.S. federal income tax only on US source income :
 - “ECI” which is income effectively connected to conduct of a U.S. trade or business – US Federal Rates of up to 40%+ of net
 - ☐ Note: an athlete’s performance in the US will generally amount to engaging in a US trade or business
 - U.S. source passive income (known as FDAP) – Federal withholding of 30% on gross unless reduced or eliminated by an applicable Tax Treaty
 - I’ll discuss tax treaties next.

US Tax Treaties

- US Tax Treaties can Provide Significant Relief from US Tax Where Applicable
- Each Treaty is slightly different and the starting point to see if a Tax Treaty applies is knowing the country of tax residence of the athlete
- Probably the type of common tax treaty provision of most benefit to Non US Resident Athletes is the one for royalties, which where applicable, often permits taxation of the royalty payment only at the tax residence of the athlete – meaning no US federal tax on the royalty income
- The key to getting the benefit besides qualifying as a beneficiary of the treaty is generally that the royalties are paid for image rights and not for performance

Non-US Tax Resident Image Rights Case Studies

- The US Tax Court cases of Retief Goosen v Commissioner of Internal Revenue, 136 T.C. 547 (2011) and Sergio Garcia v Commissioner of Internal Revenue, 140 T.C. 141 (2013) will be used to illustrate the taxation of image rights in the US.

Retief Goosen - Facts

- Goosen was at the time (2002 and 2003) one of the leading professional golfers in the world,
- Goosen was a UK non-domiciliary tax resident at all times
- Goosen, either directly or through intermediary companies of which he was an employee, entered into endorsement agreements with sponsors Acushnet, TaylorMade, Izod, Upper Deck, Electronic Arts and Rolex.
- Goosen agreed to allow all sponsors to use his name, face, image and likeness in advertising and marketing campaigns worldwide
- Acushnet, Taylor Made and Izod were on course agreements that required Goosen to wear or use their products during golf tournaments.
- Rolex, Upper Deck and Electronic Arts were off-course agreements that did not have this requirement.

Retief Goosen – Goosen’s US Tax Reporting

- Goosen reported all prize money from golf tournaments and appearance fees in the United States as effectively connected income taxable in the United States
- Goosen characterized the endorsement fees and bonuses from the on-course endorsements (Acushnet, TaylorMade and Izod) as 50 percent personal services income (i.e. ECI) and 50 percent royalty income.
 - He sourced 3.4% of these on course royalties to the US
 - He sourced personal services income to the US by a ratio of US play/worldwide play
- Goosen characterized the endorsement fees from the off course endorsements (Upper Deck, Electronic Arts and Rolex) as 100 percent royalty income
 - He sourced 6.8% of Rolex and Electronic Art to the US
 - He sourced 9.1% of Upper Deck to the US

Retief Goosen – IRS View

- IRS determined that Goosen should have characterized the endorsement fees and bonuses from Acushnet, TaylorMade and Izod, (the on course endorsements) as 100 percent personal services income (i.e. ECI)
- IRS also reallocated a larger percentage of Goosen's on course endorsement fees as U.S.-source income.
- IRS agreed that Goosen's income from the off-course endorsement agreements was royalty income.
- IRS determined, however, that 25 percent of Goosen's royalty income should be U.S.-source income rather than the less than 10 percent U.S.-source income Goosen reported.

Retief Goosen – Court Analysis

Character of Income

- The on course endorsement contracts involved both an element of payment for Goosen’s services and a royalty payment for his image
 - ❑ Goosen was paid more for performance than image
 - ❑ He had requirements to play in quite a few tournaments
 - ❑ He had a rather sedate, not splashy personalty
 - ❑ Approaching middle age – not a lot of matinee idol characteristics
- The off course endorsement contracts were purely for image – i.e. royalties

Retief Goosen – Court Analysis - Continued

Sourcing of Royalty Income (1 of 3):

- Under US law royalty income paid for the right to use intangible property generally is sourced where the property is:
 - used or
 - granted the privilege of being used.
- Taxpayers must make an appropriate sourcing allocation if the royalty income relates to the right to use property both within and outside the United States.
- The contracting parties to the transaction have the burden of making a reasonable allocation of the royalty income between the U.S. and foreign sources.

Retief Goosen – Court Analysis - Continued

Sourcing of Royalty Income (2 Of 3):

- Goosen granted his sponsors the right to use his name and likeness worldwide.
- The contracting parties agreed to source 25 percent to the United Kingdom and 75 percent to the rest of the world.
 - The contracting parties did not specify, however, how the income should be sourced to the US
- US courts generally source all the royalty income (at least from a US sponsor) to the United States if the contracting parties have failed to make a reasonable allocation
- Unless the taxpayer can show there is a sufficient basis for sourcing the income between U.S. and foreign sources.

Retief Goosen – Court Analysis - Continued

Sourcing of Royalty Income (3 of 3)

- A sufficient basis exists when a taxpayer establishes that he or she has property rights outside the United States and furnishes evidence on the value of those rights.
- The Court determined that Goosen established that he owned the rights to his name and likeness outside the United States and that those rights had value.
- In valuing those rights Court looked at:
 - For Upper Deck and Electronic Arts - Where sales took place of Goosen golf cards (92%) in US and video games (70%) in US
 - For On Course Endorsements and Rolex –Sourced 50% to the US as the largest golf market in the world

Retief Goosen – Court Analysis - Continued

ECI

- On Course Endorsements – dependent on Goosen’s performance of services in US therefore ECI - Taxed at graduated US rates on net income sources to the US
- Off Course Endorsements – not dependent on performance of Goosen’s services in US therefore not ECI – Subject to flat 30% withholding on gross sourced to the US

Retief Goosen – Court Analysis - Continued

US – UK Tax Treaty

- The UK- US tax treaty could have provided some benefit to Goosen with regard to his US source royalties that were not ECI to the extent the royalties were remitted to Goosen in the UK.
- However the Court said Goosen could not show the receipt of any of this income into the UK

Retief Goosen – Court Decision

- The endorsement fees and bonuses Goosen received from Acushnet, TaylorMade and Izod were allocated:
 - 50 percent to personal services income (i.e. all taxed in the US as ECI) and
 - 50 percent to royalty income:
 - The royalty income Goosen received from Acushnet, TaylorMade and Izod was 50 percent U.S.-source income effectively connected with a U.S. trade or business (i.e. 50% taxed in the US ECI – 50% not taxed in the US as non US source)
 - The royalty income Goosen received from Rolex was 50 percent U.S. source income not effectively connected with a U.S. trade or business. (i.e. 50% taxed in the US as FDAP – 50% not taxed in the US as non US source)
 - The royalty income Goosen received from Upper Deck is 92 percent U.S.-source income not effectively connected with a U.S. trade or business. (i.e. 92% FDAP – 8% non US source)
 - The royalty income Goosen received from Electronic Arts is 70 percent U.S.-source income not effectively connected with a U.S. trade or business. (i.e. 70% FDAP – 30% non US source)
- Goosen did not benefit from any provision under the 1975 or the 2001 U.S.-U.K. income tax treaty.

Sergio Garcia - Facts

- Garcia was at the time (2003 and 2004) one of the leading professional golfers in the world.
- Garcia was treated as a Spanish citizen who was tax resident of Switzerland at all times
- Garcia, either directly or through an Swiss intermediary company which he owned entered into endorsement agreements with sponsor TaylorMade
- Garcia agreed to allow Taylor made to use his name, face, image and likeness in advertising and marketing campaigns worldwide
- Taylor Made was an on course agreement that also required Garcia to wear or use its products during golf tournaments.

Sergio Garcia - Facts

In return for his services and use of his image rights, Taylor Made agreed to pay Garcia certain compensation.

- Garcia and Taylor Made allocated 85% of Garcia's compensation to royalties (for use of his image rights) and 15% to personal services.
- Garcia used two intermediary companies which he essentially owned all of:
 - Even Par, LLC, in the State of Delaware, USA, which would (i) receive the royalty payments and then
 - (ii) pay a portion of the royalty payments (attributable to use of the image rights in the United States) to a second LLC, Long Drive Sarl, that Garcia established in Switzerland

Sergio Garcia– Garcia’s US Tax Reporting

- Garcia paid no U.S. tax on the royalty payments,
- Garcia did pay U.S. tax on the U.S. source personal service payments.

Sergio Garcia – IRS View

- Disputed the 85%–15% allocation between royalty and personal service payments, arguing for a larger portion attributable to Garcia’s personal services
- Claimed that the U.S. source royalty payments should have been treated as made directly to Garcia and that the form of the transaction involving the US LLC and Swiss LLC should be disregarded

Sergio Garcia– Court Analysis

Character of Income

- The on course endorsement contracts involved both an element of payment for services and a royalty payment for his image
- The contract allocation of 85% royalties and 15% services was not determinative but:
 - In sports no one is going to pay you much for on course endorsement if you are not a very good player – so performance is a major factor
 - Note: the comparison of Garcia to Goosen made in the Goosen case was cited
 - Garcia was paid more than Goosen although his record on the course was not as good
 - Garcia had significantly lower number of events he was required to play
- Court allocated 65% to royalties and 35% to services

Sergio Garcia– Court Analysis

Effect of Swiss Tax Treaty

Garcia was Swiss tax resident and royalty payments were in fact made into Switzerland to Garcia so the US-Switzerland Tax Treaty applied .

The royalty payments made to Garcia were exempt from US tax under the US-Switzerland tax treaty.

The “Artistes and Sportsman” provisions of the Switzerland treaty which allowed for US taxation did not apply as income from the sale of image rights was not predominantly attributable to Garcia’s performance right

Sergio Garcia – Court Decision

- The payments made by TaylorMade were allocated 65% to royalties and 35% to personal services
- Irrelevant whether US source royalties were income to Garcia or his Swiss company (Long Drive) as Garcia was not taxable on it
- No royalty income was taxed to Garcia in the US but all US source income for personal services was

Some Rough Conclusions (Staying Out of the Rough)

- Garcia did a lot better than Goosen
- Image is everything (at a certain very high skill level)
- At the highest echelon of many sports, looks lead to higher pay and lower taxes (at least in the USA) than performance
- Make allocations to US and non US source income in contracts
- Emphasize image more than performance in contracts
- Morals clauses in contracts are useful in weighting payments toward image rights



Thanks!!

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*Use your country's exit code as a prefix

Appendix -Tax Home Closer Connection Test

- The country of residence you designate on forms and documents
- The types of official forms and documents you file, such as Form W-9, Request for Taxpayer Identification Number and Certification, W-8BEN, Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding, or W-8ECI, Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States.
- The location of:
 - Your permanent home,
 - Your family,
 - Your personal belongings, such as cars, furniture, clothing, and jewelry,
 - Your current social, political, cultural, or religious affiliations,
 - Your business activities (other than those that constitute your tax home),
 - The jurisdiction in which you hold a driver's license,
 - The jurisdiction in which you vote, and
 - Charitable organizations to which you contribute.
- Note: It does not matter whether your permanent home is a house, an apartment, or a furnished room. It also does not matter whether you rent or own it. It is important, however, that your home be available at all times, continuously, and not solely for short stays.