

The University of Akron  
IdeaExchange@UAkron

---

Akron Law Review

Akron Law Journals

---

August 2016

# Northwestern, O'Bannon and The Future: Cultivating a New Era for Taxing Qualified Scholarships

Kathryn Kisska-Schulze

Adam Epstein

Please take a moment to share how this work helps you [through this survey](#). Your feedback will be important as we plan further development of our repository.

Follow this and additional works at: <http://ideaexchange.uakron.edu/akronlawreview>

 Part of the [Tax Law Commons](#)

---

## Recommended Citation

Kisska-Schulze, Kathryn and Epstein, Adam (2015) "Northwestern, O'Bannon and The Future: Cultivating a New Era for Taxing Qualified Scholarships," *Akron Law Review*: Vol. 49 : Iss. 4 , Article 1.

Available at: <http://ideaexchange.uakron.edu/akronlawreview/vol49/iss4/1>

This Article is brought to you for free and open access by Akron Law Journals at IdeaExchange@UAkron, the institutional repository of The University of Akron in Akron, Ohio, USA. It has been accepted for inclusion in Akron Law Review by an authorized administrator of IdeaExchange@UAkron. For more information, please contact [mjon@uakron.edu](mailto:mjon@uakron.edu), [uapress@uakron.edu](mailto:uapress@uakron.edu).

***NORTHWESTERN, O'BANNON AND THE FUTURE:  
CULTIVATING A NEW ERA FOR TAXING QUALIFIED  
SCHOLARSHIPS***

*Kathryn Kisska-Schulze\**

*Adam Epstein\*\**

I.	Introduction .....	772
II.	<i>The NLRB v. Northwestern</i> —The Pay-for-Play Model Gains Traction .....	775
III.	History in the Making—Taxing Athletic Scholarships in the Wake of the NLRB’s 2014 <i>Northwestern</i> Decision .....	782
	A. Taxing Qualified Scholarships—Understanding IRC Section 117.....	783
	B. Compensation for Services Rendered—Treasury Regulation § 1.117-4(c) and Judicial Interpretation.....	785
IV.	The Student-Athlete as Employee—The Federal Income Tax Perspective.....	793
	A. Examining the Employer-Employee Relationship	795
	1. The Common Law/IRS Twenty-Factor Test ..	795
	2. The Economic Realities Test .....	801
	3. The Hybrid Test .....	803
	B. Characterizing Student-Athletes as Employees for Federal Income Tax Purposes .....	805
V.	Conclusion .....	810

---

\* JD, 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.

## I. INTRODUCTION

On March 26, 2014, the Chicago district (Region 13) of the National Labor Relations Board (NLRB) ruled that Northwestern University's scholarship football players were employees of the institution under the National Labor Relations Act (NLRA) and could unionize and bargain collectively.<sup>1</sup> Traditionally, college sports have operated under the National Collegiate Athletic Association's (NCAA) fundamental principle of "amateurism,"<sup>2</sup> only allowing student-athletes to receive grants-in-aid (i.e., athletic scholarships) to help pay for their college educations while concurrently engaging in competitive athletics for their universities.<sup>3</sup> This principle of "amateurism" ensures that generally, student-athletes who are, or have been, paid to play are essentially permanently ineligible to compete in varsity athletic competition in that particular sport.<sup>4</sup>

The Chicago district's milestone 2014 ruling threatened the fundamental paradigm of amateurism in collegiate sports by permitting

---

1. See also Kathryn Kisska-Schulze & Adam Epstein, "Show Me the Money!"—Analyzing the Potential State Tax Implications of Paying Student-Athletes, 14 VA. SPORTS & ENT. L.J. 13, 13-14 (2014); Brian Bennett, *Northwestern Players Get Union Vote*, ESPN COLLEGE FOOTBALL (Mar. 27, 2014, 9:23 AM), [http://espn.go.com/college-football/story/\\_/id/10677763/northwestern-wildcats-football-players-win-bid-unionize](http://espn.go.com/college-football/story/_/id/10677763/northwestern-wildcats-football-players-win-bid-unionize); Ben Strauss & Steve Elder, *College Players Granted Right to Form Union*, N.Y. TIMES (Mar. 26, 2014), <http://www.nytimes.com/2014/03/27/sports/ncaafootball/national-labor-relations-board-rules-northwestern-players-are-employees-and-can-unionize.html>.

2. See 2015-2016 NCAA DIVISION I MANUAL, available at <https://www.ncaapublications.com/p-4388-2015-2016-ncaa-division-i-manual-august-version-available-august-2015.aspx>. [hereinafter "NCAA Manual"]. NCAA rules are also known formally as Bylaws; see, e.g., NCAA Manual 2.9, The Principle of Amateurism ("Student-athletes shall be amateurs in an intercollegiate sport, and their participation should be motivated primarily by education and by the physical, mental and social benefits to be derived. Student participation in intercollegiate athletics is an avocation, and student-athletes should be protected from exploitation by professional and commercial enterprises."); see generally Adam Epstein & Paul Anderson, *Utilization of the NCAA Manual as a Teaching Tool*, 26 J. LEGAL STUD. EDUC. 109, 118, 124 (2009); T. Matthew Lockhart, Comment: *Oliver v. NCAA: Throwing a Contractual Curveball at the NCAA's "Veil of Amateurism"*, 35 U. DAYTON L. REV. 175, 186 (2010) (noting the deference that courts have given to the manner in which the NCAA defines and regulates amateurism according to its rules, more formally known as bylaws).

3. See Kisska-Schulze & Epstein, *supra* note 1, at 14, 21; see also Strauss & Elder, *supra* note 1. We recognize that the vast majority of colleges and universities are members of the NCAA but that the National Association of Intercollegiate Athletics (NAIA) also exists for others as well. See National Association of Intercollegiate Athletics, Member Schools, [http://www.naia.org/ViewArticle.dbml?DB\\_OEM\\_ID=27900&ATCLID=205322922](http://www.naia.org/ViewArticle.dbml?DB_OEM_ID=27900&ATCLID=205322922) (last visited Oct. 8, 2015).

4. Josephine (Jo) R. Potuto, William H. Lyons & Kevin N. Rask, *What's in a Name? The Collegiate Mark, the Collegiate Model, and the Treatment of Student-Athletes*, 92 OR. L. REV. 879, 882 (2014).

scholarship football players to unionize.<sup>5</sup> Specifically, the decision concluded that Northwestern football players receive the substantial economic benefit of scholarship money in exchange for performing football-related services under what amounts to a contract for hire and noted that the university's football coaching staff exert a significant amount of control over the players to such a degree that scholarships may be revoked if players break team rules.<sup>6</sup>

Following this landmark decision, Northwestern University filed an appeal with the NLRB in an effort to invalidate the regional decision.<sup>7</sup> On August 17, 2015, the NLRB rejected the bid by football players at Northwestern University to form a union in a unanimous seven-page decision in which the board declined to assert jurisdiction in the case because allowing athletes at a private university to organize would not "promote stability in labor relations."<sup>8</sup> Still, this case—which currently maintains the status quo of student-athletes as amateurs—helped reignite the sixty-year, heavily deliberated concern over whether student-athletes should be paid to play.<sup>9</sup> While the NLRB overturned the Chicago district's

---

5. See Kisska-Schulze & Epstein, *supra* note 1.

6. WithumSmith+Brown, CPAs, *A Win for Student Athletes or for the IRS?*, DOUBLE TAXATION: A TAX ON ALL THINGS TAXES (Apr. 8, 2014), <http://double-taxation.com/2014/04/08/a-win-for-student-athletes-or-for-the-irs/>; see also Strauss and Elder, *supra* note 1 (addressing that the NLRB's ruling was based on various factors, to include the amount of time devoted to the sport of football, the extent of control exercised by coaches, and the scholarship agreements entered into between universities and student-athletes).

7. See Kisska-Schulze & Epstein, *supra* note 1, at 13-14; see also Amanda Becker, *Northwestern University Appeals Decision Granting Football Team Union Vote*, REUTERS (Apr. 9, 2014, 4:31 PM), <http://www.reuters.com/article/2014/04/09/us-college-football-unions-idUSBREA381VT20140409>.

8. Northwestern Univ. and College Athletes Players Ass'n (CAPA), 362 NLRB No. 167, 2-3, (Aug. 17, 2015). Michigan and Ohio soon passed and implemented laws barring student-athletes from the right to unionize at all. See OHIO REV. CODE §3345.56 (West, Westlaw through Files 1 to 54 of the 131st General Assembly (2015-2016) and 2015 State Issues 1 and 2); Definitions; rights of public employees, MICH. COMP. LAWS 423.201 (1(e)(iii)) (West, Westlaw through P.A.2016, No. 86 of the 2016 Regular Session, 98th Legislature). It should be noted that the case as presented was specific to unionization at private universities, and did not specify how this decision could affect such efforts at public universities in the future.

9. See Kisska-Schulze & Epstein, *supra* note 1; see also Sean Gregory, *It's Time to Pay College Athletes*, TIME (Sept. 16, 2013), <http://time.com/568/its-time-to-pay-college-athletes/>; EVENING INDEP. (Oct. 4, 1951), available at <http://www.newspapers.com/newspage/3608625/> (reporting on University of Denver (DU) football player Ernest Nemeth's filing of a worker's compensation claim against DU after injuring his back during spring football practice); State Comp. Ins. Fund v. Indus. Comm'n, 314 P.2d 288 (Colo. 1957) (denying benefits to the widow of a scholarship athlete killed during a football game); Rensing v. Indiana State University Bd. of Trs., 444 N.E.2d 1170 (Ind. 1983) (denying recovery to a football player who was rendered a quadriplegic during a collegiate sporting event); Coleman v. Western Michigan Univ., 336 N.W.2d 224 (Mich. Ct. App. 1983) (holding that a scholarship agreement between an athlete and institution does not entitle the athlete to workers' compensation); Taylor v. Wake Forest Univ., 191 S.E.2d 379, 382 (N.C. Ct.

ruling, this Article explores the plausible federal tax consequences should student-athletes in the future be deemed employees of their institutions.<sup>10</sup>

The language of the Internal Revenue Code (IRC) mandates that earned income be taxable, no matter the source.<sup>11</sup> However, the IRC also grants certain exclusions to this canon to include an accommodation that an individual's gross income excludes money received in the form of qualified scholarships.<sup>12</sup> Thus far, the Internal Revenue Service (IRS) has taken the position that so long as student-athletes are not "required" to participate in any specific sport in exchange for scholarship awards, the language of the IRC does not prevent students' scholarships from being deemed excludable qualified scholarships.<sup>13</sup> Thus, under the purview of both the IRC and IRS, student-athletes receiving qualified scholarships do not pay income taxes on scholarship moneys received.<sup>14</sup>

From a federal income tax perspective, the significance of the NLRB's 2014 *Northwestern* case as a paradigm for future cases involving student-athletes' unionization mobilization efforts, in conjunction with the recent decision in *O'Bannon v. NCAA*, where former Division I athletes settled a \$40 million suit against EA Sports for improperly using their likenesses in video games, could redefine the principle that select student-athletes are no longer unpaid amateurs receiving qualified scholarships, but instead are employees of their institutions earning scholarship funds in exchange for services rendered as college athletes.<sup>15</sup> Accordingly, a crucial question following the original NLRB holding was whether the IRS can logically continue to treat qualified scholarships received by student-athletes as excludable from gross income based on the language of the IRC or instead reexamine the taxability of student-

---

App.), *cert denied*, 192 S.E.2d 197 (N.C. 1972) (excusing a university's obligation to provide financial assistance to a student-athlete who refused to play football as a result of his poor academic showing).

10. See Sara Ganim, *Labor Board: Northwestern University Football Players Can Unionize*, CNN (Mar. 27, 2014, 3:55 PM), <http://www.cnn.com/2014/03/26/us/northwestern-football-union/>; see also WithumSmith+Brown, CPAs, *supra* note 6; Kathryn Kisska-Schulze & Adam Epstein, *supra* note 1.

11. IRC § 61(a) (LEXIS 2015).

12. IRC § 117(a) (LEXIS 2015).

13. Potuto et al., *supra* note 4, at 890 n.40 (referencing commentary within note 40 with respect to the exclusion of qualified scholarships from the parameters of IRC § 117(c)).

14. IRC § 117(c)(1) provides that the exclusion for qualified scholarships does not apply to amounts received which represent "payment for teaching, research, or other services by the student required as a condition for receiving the qualified scholarship . . . ."

15. See Tom Farrey, *Players, Game Makers Settle for \$40M*, USA TODAY (May 31, 2014), [http://espn.go.com/espn/otl/story/\\_id/11010455/college-athletes-reach-40-million-settlement-ea-sports-ncaa-licensing-arm](http://espn.go.com/espn/otl/story/_id/11010455/college-athletes-reach-40-million-settlement-ea-sports-ncaa-licensing-arm); see also *O'Bannon v. NCAA*, 7 F. Supp. 3d 955, 962-63 (N.D. Cal. 2014).

athletes' qualified scholarships.<sup>16</sup>

The momentum of law surrounding student-athletes' employment characterization indicates that qualified scholarships could be heavily scrutinized in the future and found to fall within the scope of taxable federal income. The purpose of this Article, then, is to analyze the potential taxability of qualified scholarships should student-athletes be deemed employees of their institutions. To achieve this objective, Part II offers a brief history of judicial scrutiny surrounding the pay-for-play model within college athletics; Part III analyzes the language of the IRC and related Treasury Regulations as they apply to qualified scholarships; Part IV evaluates the potential characterization of student-athletes as employees of their universities; and Part V concludes that the IRS and courts may categorize at least some scholarship athletes as employees of their institutions in the future, which may cultivate a new era in the taxing of qualified scholarships under federal income tax law.<sup>17</sup>

## II. *THE NLRB V. NORTHWESTERN*—THE PAY-FOR-PLAY MODEL GAINS TRACTION

After Johnny Manziel first flashed his infamous “show me the money” hand gesture during the 2013 NCAA college football season, the issue of paying student-athletes has garnered heavy media attention.<sup>18</sup>

---

16. See David Murphy & Christopher Amundsen, *What Exactly is the Long-Term Impact of the NLRB's Decision? Part 3*, DORSEY (Apr. 24, 2014), <http://www.dorsey.com/eu-nlr-decision-college-athletes-and-unions-pt3/>. It should be noted that in addition to the NCAA's principle of amateurism, the NCAA currently considers pay as an extra benefit, a term that could render a student-athlete ineligible for competition. See NCAA MANUAL 12.1.2, Amateur Status (“An individual loses amateur status and thus shall not be eligible for intercollegiate competition in a particular sport if the individual: (a) Uses his or her athletics skill (directly or indirectly) for pay in any form in that sport; (b) Accepts a promise of pay even if such pay is to be received following completion of intercollegiate athletics participation; (c) Signs a contract or commitment of any kind to play professional athletics, regardless of its legal enforceability or any consideration received, except as permitted in Bylaw 12.2.5.1; . . . (d) Receives, directly or indirectly, a salary, reimbursement of expenses or any other form of financial assistance from a professional sports organization based on athletics skill or participation, except as permitted by NCAA rules and regulations; (e) Competes on any professional athletics team per Bylaw 12.02.8, even if no pay or remuneration for expenses was received, except as permitted in Bylaw 12.2.3.2.1; (f) After initial full-time collegiate enrollment, enters into a professional draft (see Bylaw 12.2.4); (g) Enters into an agreement with an agent.”).

17. The purpose of this Article is to specifically address specified federal income tax implications on the pay-for-play model of college sports. Although the authors acknowledge that state and local taxes will likewise have an impact on this model, such analysis is outside the scope of this Article. For more information on the state tax implications of paying student-athletes, see Kisska-Schulze & Epstein, *supra* note 1.

18. See, e.g., Gregory, *supra* note 9; see also Sharon Terlep & Ben Cohen, *Judge Rules Against NCAA Ban on Paying Players*, WALL ST. J. (Aug. 8, 2014), <http://www.wsj.com/articles/judge-rules-against-ncaa-ban-on-paying-players-1407539820>; Steve Siebold, *It's Time to Pay College Athletes*,

However, while currently on the front line of public debate, the investigation into whether student-athletes should be paid is not a new phenomenon.<sup>19</sup> The origin of this discussion arose in the 1950s in Colorado when the judicial system first embarked on analyses of whether injured student-athletes qualified for workers' compensation under state law.<sup>20</sup>

Courts in different jurisdictions have used several analyses to determine whether students are considered employees of their universities. Colorado has considered whether student-athletes were entitled to workers' compensation for injuries sustained.<sup>21</sup> Other state cases have consistently sided with arguments of the NCAA and member universities in finding that student athletes are unpaid amateurs.<sup>22</sup> The *O'Bannon* case demonstrates an evolution in the law as athletes have gained rights to some form of financial remuneration generated in their role with the university.<sup>23</sup> This culminated in the case of *NLRB v. Northwestern*, which considered football players' ability to unionize.<sup>24</sup>

In *University of Denver v. Nemeth*, the Colorado Supreme Court found that Ernest Nemeth, a college football player who had also been employed and compensated by the university in various capacities in

---

HUFFINGTON POST (last updated Oct. 13, 2014, 5:59 AM), [http://www.huffingtonpost.com/steve-siebold/its-time-to-pay-college-athletes\\_b\\_5672988.html](http://www.huffingtonpost.com/steve-siebold/its-time-to-pay-college-athletes_b_5672988.html); Andrew Steadman, *College Athletics For Sale?*, 8 U. FLA. L. REV. 10 (2014), available at <https://www.law.ufl.edu/uflaw/feature/college-athletics-for-sale> (cover story of the University of Florida Fredric G. Levin College of Law Annual Report Issue); Skip Bayless, *Unleash the Boosters—drop the false idol of amateurism in college sports*, ESPN COLLEGE FOOTBALL (July 25, 2014), [http://espn.go.com/college-football/story/\\_/id/11260822/college-football-paying-athletes](http://espn.go.com/college-football/story/_/id/11260822/college-football-paying-athletes).

19. See Kisska-Schulze & Epstein, *supra* note 1; see also Dennis A. Johnson & John Acquaviva, *Point/Counterpoint: Paying College Athletes*, SPORT J. (June 15, 2012), <http://thesportjournal.org/article/pointcounterpoint-paying-college-athletes/> (exploring the history and evolution of the discussion of whether or not student-athletes should be paid); Gregory, *supra* note 9 (arguing that because college sports equate to mass entertainment, it is time to reward players for their work).

20. See, e.g., *Univ. of Denver v. Nemeth*, 257 P.2d 423 (Colo. 1953); see also *Univ. of Denver v. Indus. Comm'n of Colorado*, 335 P.2d 292 (Colo. 1959) (holding that private agreements may neither violate public policy nor abrogate statutory requirements or conditions affecting the public policy of the state. Nemeth, whose compensation had been awarded incrementally and who asked for additional workers' compensation due to a change in his condition, was granted a reopening of his case.); *State Comp. Ins. Fund v. Indus. Comm'n*, 314 P.2d 288 (Colo. 1957) (denying benefits to the widow of a student-athlete killed during a football game).

21. See, e.g., *Nemeth*, 257 P.2d 423; see also *Univ. of Denver v. Indus. Comm'n of Colorado*, 335 P.2d 292.

22. See, e.g., *State Comp. Ins. Fund v. Indus. Comm'n*, 34 P.2d 288.

23. See *O'Bannon v. NCAA*, 7 F. Supp. 3d 955, 1007-08 (N.D. Cal.), *aff'd in part and rev'd in part*, *O'Bannon v. NCAA*, 802 F.3d 1049 (9th Cir. Cal. 2015).

24. *Northwestern Univ. and College Athletes Players Ass'n (CAPA)*, 362 N.L.R.B. No. 44 (2015).

exchange for his participation on the football team, qualified for workers' compensation after sustaining injuries during a football practice.<sup>25</sup> Four years later, in *State Compensation Insurance Fund v. Industrial Commission*, the Colorado Supreme Court denied workers' compensation benefits to the widow of a student-athlete killed during a football game, finding no existence of a contractual obligation to play football between the decedent and the university, thereby negating any claim for compensation.<sup>26</sup> During that same decade, the NCAA coined the term "student-athlete," which the organization then rapidly embedded into all of its rules and interpretations.<sup>27</sup>

Following the early Colorado workers' compensation decisions, several other state courts heard similar claims made by student-athletes, and consistently followed the NCAA's position that student-athletes are not employees of their universities.<sup>28</sup> For over half a century, the NCAA and its member institutions have rigorously defended that student-athletes are unpaid amateurs.<sup>29</sup> However, the more recent surge in financial benefits afforded to the NCAA and its member institutions from lucrative television rights has increased scrutiny over whether some portion of this wealth should be directed towards student-athletes themselves.<sup>30</sup>

---

25. *Nemeth*, 257 P.2d. at 430.

26. *State Comp. Ins. Fund v. Indus. Comm'n*, 314 P.2d at 289-90.

27. See Kisska-Schulze & Epstein, *supra* note 1 at 20; see also Taylor Branch, *The Shame of College Sports*, ATLANTIC (Oct. 2011), <http://www.theatlantic.com/magazine/archive/2011/10/the-shame-of-college-sports/308643/> ("We crafted the term student-athlete," Walter Byers [the NCAA's first Executive Director] himself wrote, "and soon it was embedded in all NCAA rules and interpretations.").

28. See Kisska-Schulze & Epstein, *supra* note 1; see also, e.g., *Rensing v. Ind. State Univ. Bd. of Trs.*, 444 N.E.2d 1170, 1175 (Ind. 1983) (reversing and holding that the resulting disability to the scholarship athlete nevertheless did not establish that either party had the intent to enter into an employer-employee relationship); *Coleman v. W. Mich. Univ.*, 336 N.W.2d 224 (Mich. Ct. App. 1983) (holding that WMU had little control over Coleman, and even if it did, Coleman's football skills were not an integral part of WMU's school business); *Waldrep v. Texas Emp'rs Ins. Ass'n*, 21 S.W.3d 692 (Tex. Ct. App. 2000) (holding that TCU did not direct or control all of Waldrep's activities as a football player before suffering his spinal cord injury which led to paralysis). *But see Van Horn v. Indus. Accident Comm'n*, 33 Cal. Rptr. 169 (Cal. Ct. App. 1963) (holding in favor of the wife of California State Polytechnic football team member who successfully brought a workers' compensation claim to recover for the death of her husband as a result of a plane crash while returning from a game).

29. Kisska-Schulze & Epstein, *supra* note 1.

30. *Id.*; see also Joe Nocera, *Let's Start Paying College Athletes*, N.Y. TIMES (Dec. 30, 2011), [http://www.nytimes.com/2012/01/01/magazine/lets-start-paying-college-athletes.html?pagewanted=all&\\_r=0](http://www.nytimes.com/2012/01/01/magazine/lets-start-paying-college-athletes.html?pagewanted=all&_r=0) ("And what does the labor force have that makes it possible for coaches to earn millions, and causes marketers to spend billions, get? Nothing. The workers are supposed to be content with a scholarship that does not even cover the full cost of attending college. Any student athlete who accepts an unapproved, free hamburger from a coach, or even a fan, is in violation of N.C.A.A. rules.").



Although the NCAA has not officially amended its posture on the pay-for-play model, recent court cases, coupled with the March 2014 NLRB ruling, have made significant strides in attempting to establish that student-athletes are more than mere unpaid amateurs.<sup>31</sup> In 2009, Sam Keller, a former Division I college quarterback, and Ed O'Bannon, a former UCLA basketball player, merged separately-filed lawsuits into a single suit against the NCAA, labeled the *NCAA v. Student-Athlete Name & Likeness Licensing Litigation*.<sup>32</sup> Keller, O'Bannon, and a group of former and current Division I student-athletes claimed that the characteristics of the players in the NCAA Football video series mirrored theirs and those of other actual college athletes, violating their right of publicity and image rights.<sup>33</sup> In addition to seeking damages from the use of their likenesses in video games, the *O'Bannon* suit further claimed the NCAA was violating federal antitrust law in preventing student-athletes from capitalizing on their names and likenesses, specifically with regard to the use of their likenesses in Electronic Arts (EA) Sports' video games.<sup>34</sup>

After years of court filings, in May and June 2014, both EA Sports and the NCAA offered settlement agreements to the plaintiffs involved in the *NCAA v. Student-Athlete Name & Likeness Licensing Litigation* case.<sup>35</sup> The settlement culminated with a \$40 million agreement in which EA Sports paid the plaintiffs for improperly using the likenesses of student-athletes.<sup>36</sup> In addition, for the first time in NCAA history, the organization agreed to pay \$20 million to student-athletes for rights relating to their play on the field and for their contribution to the profitable nature of college athletics.<sup>37</sup>

Following these settlement agreements, a series of legal decisions

---

31. See Kisska-Schulze & Epstein, *supra* note 1; see also, Mark Koba, *Student-Athletes to Get Paid? It Looks That Way*, NBC NEWS (Aug. 12, 2014, 7:23 AM), <http://www.nbcnews.com/business/business-news/student-athletes-get-paid-it-looks-way-n178131>.

32. See Kisska-Schulze & Epstein, *supra* note 1, at 22; see also, Keller v. Elec. Arts. Inc. (*In re* NCAA Student-Athlete Name & Likeness Licensing Litig.), 724 F.3d 1268 (9th Cir. 2013); John Wolohan, *Update on O'Bannon v. NCAA*, LAWINSPORT (Mar. 31, 2014), <http://www.lawinsport.com/articles/intellectual-property-law/item/update-on-o-bannon-v-ncaa> (discussing the merger of lawsuits filed against the NCAA).

33. Keller, 724 F.3d at 1271-73; see also Wolohan, *supra* note 32.

34. See Kisska-Schulze & Epstein, *supra* note 1 at 22-23; see also Wolohan, *supra* note 32 (discussing the various lawsuits involved by and the specific issues brought forth against the NCAA).

35. See Farrey, *supra* note 15.

36. *Id.*

37. See Rob Dauster, *NCAA Settles for \$20 Million in Keller v. NCAA Lawsuit*, NBC SPORTS (Jun. 9, 2014, 2:31 PM), <http://collegebasketballtalk.nbcsports.com/2014/06/09/ncaa-settles-for-20-million-in-keller-v-ncaa-lawsuit/>.

emerged, demonstrating that the judicial branch did not share the same position on amateurism as the NCAA. For example, on August 8, 2014, a California district court judge ruled in favor of O'Bannon, who had continued his federal antitrust lawsuit against the NCAA.<sup>38</sup> This decision resulted in a short-lived rejection of the NCAA's principle of "amateurism," though it did not affect the NCAA's current stance on not paying student athletes under a pay-for-play model.<sup>39</sup> However, according to the decision, beginning in 2016 universities could have offered select football and basketball players individual trust funds that could be accessed after graduation.<sup>40</sup> Senior District Judge Claudia Wilken of the U.S. District Court for the Northern District of California held that the relevant NCAA member institutions may provide deferred compensation of \$5,000 or less.<sup>41</sup> Almost immediately thereafter, in October of 2014 the University of Texas's athletics director had announced the intention to pay each of its student-athletes a sum of money covering the cost of attendance, coupled with its deferred compensation for likeness rights, beginning fall 2015.<sup>42</sup> The *O'Bannon* decision did not affect the NCAA's

38. *O'Bannon v. NCAA*, 7 F. Supp. 3d 955, 1008 (N.D. Cal. 2014) (Per this ruling, the NCAA has the ability to cap compensation at \$5,000 per year above the value of full college scholarships.); *see also* Koba, *supra* note 31 (documenting the *O'Bannon* decision).

39. *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](http://espn.go.com/espn/otl/story/_id/11332816/ed-obannon-says-antitrust-ruling-only-beginning-change) (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*, THE WASHINGTON 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](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 of the *O'Bannon* decision, the NCAA "has given no indication it is eager to embrace any form of pay-for-play model").

40. Ben Strauss & Marc Tracy, *N.C.A.A. Must Allow College to Pay Athletes, Judge Rules*, N.Y. TIMES (Aug. 8, 2014), [http://www.nytimes.com/2014/08/09/sports/federal-judge-rules-against-ncaa-in-obannon-case.html?\\_r=0](http://www.nytimes.com/2014/08/09/sports/federal-judge-rules-against-ncaa-in-obannon-case.html?_r=0) (noting that football players in the top ten conferences and all Division I men's basketball players could be offered trust funds which can be accessed after graduation, giving players an opportunity to share the television revenue they help generate for their colleges and the NCAA).

41. *Judge Rules Against NCAA*, ESPN (Aug. 9, 2014, 6:20 PM), [http://espn.go.com/college-sports/story/\\_id/11328442/judge-rules-ncaa-ed-obannon-antitrust-case](http://espn.go.com/college-sports/story/_id/11328442/judge-rules-ncaa-ed-obannon-antitrust-case) (U.S. District Judge Claudia Wilken, in a 99-page decision finding in favor of O'Bannon, found that "the NCAA rules unreasonably restrain trade in the market for certain educational and athletic opportunities offered by NCAA Division I schools." However, she did rule that individual schools can offer less money so long as they do not unlawfully conspire among themselves to set those amounts.).

42. *See* Zach Barnett, *Texas Will Begin Paying Each of Its Athletes \$10,000 A Year*, FOOTBALL SCOOP (Oct. 22, 2014), <http://footballscoop.com/news/texas-will-begin-paying-athletes-10000-year/>; *see also* Jason McIntyre, *Texas is NOT Paying Each Athlete \$10,000, But AD Steve Patterson Said They Might if UT Loses in Court*, THE BIG LEAD (Oct. 22, 2014, 11:46 PM), <http://thebiglead.com/2014/10/22/texas-is-not-paying-each-athlete-10000-but-ad-steve-patterson-said-they-might-if-ut-loses-in-court/> (disputing the original claim that Texas will pay each student-

stance on the pay-for-play model, but the 2014 NLRB ruling appeared to open the door for student-athletes to be deemed employees of their institutions.<sup>43</sup>

Then, on March 26, 2014, the NLRB ruled that Northwestern University football players qualified as employees of the institution and could unionize and bargain collectively.<sup>44</sup> In making its decision, the NLRB distinguished its ruling from that of its 2004 *Brown University* decision where it held that graduate research assistants were not university employees eligible for union representation.<sup>45</sup> The NLRB reasoned that Brown University graduate assistants' activities were primarily educational, whereas Northwestern University athletes' activities were largely "economic."<sup>46</sup> This ruling specifically established that Northwestern scholarship football players could unionize based on certain factors, including the extent of time devoted to their sport, the level of control exerted by coaches, and their scholarship agreements.<sup>47</sup> However, following this decision, Northwestern University immediately filed an appeal with the NLRB in Washington, D.C., which proved to be fatal to the impact of the 2014 decision.<sup>48</sup>

Later, Samantha Sackos, a former soccer player at the University of Houston, filed a complaint in the U.S. District Court for the Southern District of Indiana naming the NCAA and all NCAA Division I member

---

athlete \$10,000, but noting that such payment will occur if the University of Texas loses in court).

43. See *supra* note 41 and accompanying text.

44. See Kisska-Schulze & Epstein, *supra* note 1 at 13-14; see also Bennett, *supra* note 1; Strauss & Elder, *supra* note 1.

45. See Joel Barras, *NLRB Regional Director Says College Athletes Can Unionize*, FORBES (March 27, 2014, 12:06 PM), <http://www.forbes.com/sites/theemploymentbeat/2014/03/27/nlr-regional-director-says-college-athletes-can-unionize/>; see also *Brown Univ. and Int'l Union*, Case No. 1-RC-21368, slip op. 342 N.L.R.B. 42 (2004) available at <http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=0CB4QFjAA&url=http%3A%2F%2Fflynrlb.nlr.gov%2Flink%2Fdocument.aspx%2F09031d45800076ac&ei=P8yJVNWQKqPasATntILABA&usg=A> FQjCNEEQbIA-f\_mbwIJ5xesCybHQd9jug&sig2=xUpCeOWQxvFncEWiHHfXKQ&bvm=bv.81456516,d.cWc (last visited Feb. 23, 2015).

46. See *Brown Univ.*, Case 1-RC-21368, slip op. 342 N.L.R.B. 42 (2004); see also Sara Hebel, *Employees or Not? Graduate-Student Assistants Versus Scholarship Athletes*, CHRON. OF HIGHER EDUC. (Mar. 27, 2014), <https://chronicle.com/article/Employees-or-Not-/145573/> (analyzing the *Brown University* decision, in which the NLRB ruled that "students serving as graduate-student assistants spend only a limited number of hours performing their duties, and it is beyond dispute that their principal time commitment at Brown is focused on obtaining a degree and, thus, being a student").

47. See Strauss & Elder, *supra* note 1.

48. Kisska-Schulze & Epstein, *supra* note 1, at 14; see also Becker, *supra* note 7. In 2015, the NLRB overruled the 2014 decision. See *Northwestern Univ.*, 362 NLRB No. 167 (Aug. 17, 2015).

institutions as defendants.<sup>49</sup> The suit alleged that the NCAA and its Division I member schools violated the Fair Labor Standards Act (FLSA) by failing to pay college athletes for hours worked while practicing and playing college sports.<sup>50</sup> This complaint asserted that students who participate in paid, work-study, part-time employment programs are treated differently than NCAA Division I student-athletes pursuant to NCAA Bylaws, and contends that student-athletes meet the criteria for recognition as temporary employees of NCAA Division I member schools under the FLSA.<sup>51</sup> Sackos claimed that since student-athletes receive no academic credit for participating on a sports team, they should be characterized as employees under the FLSA.<sup>52</sup>

All of these examples—from the early Colorado workers' compensation rulings to the *Northwestern University* (NLRB), *Keller*, and *O'Bannon* decisions to the Sackos filing—continued to shape the debate over whether student-athletes should be paid.<sup>53</sup> As the idea of paying student-athletes continues to gain traction, an important issue to consider is whether student-athletes, ultimately characterized as employees of their institutions, could eventually be taxed on scholarship moneys received from their institutions. While the language in the IRC generally excludes qualified scholarships from federal taxation, changing the nature of the relationship between student-athletes and their universities could transform the manner in which the IRS classifies scholarship income.<sup>54</sup>

---

49. Sackos v. NCAA, No. 1:14-CV-1710 WTL-MJD (S.D. Ind. Oct. 20, 2014), available at <http://www.scribd.com/doc/243718053/Samantha-Sackos-v-NCAA-and-NCAA-Division-I-Member-Schools> (last visited Oct. 9, 2015).

50. *Id.* See also Jonathan L. Israel, *The Next Cleat Drops . . . College Athletes Sue for Unpaid Wages*, LABOR & EMPLOYMENT LAW PERSPECTIVES (Nov. 3, 2014), <http://www.laboremploymentperspectives.com/2014/11/03/the-next-cleat-drops-college-athletes-sue-for-unpaid-wages/>.

51. Sackos, No. 1:14-CV-1710 WTL-MJD.

52. *Id.*; see also Kevin Trahan, *Lawsuit Alleges NCAA is Breaking Minimum Wage Laws*, SBNATION (Oct. 22, 2014, 6:19 PM), <http://www.sbnation.com/2014/10/22/7042297/lawsuit-alleges-ncaa-is-breaking-minimum-wage-laws>; *But see* Steve Berkowitz, *Judge Dismisses NCAA Wage Lawsuit Involving Penn Track Athletes*, USA TODAY (Feb. 17, 2016) (offering that U.S. District Court (S.D. Ind.) Judge William T. Lawrence dismissed the [Sackos] case against over 100 Division I NCAA member schools holding that Congress did not intend the FLSA to apply to student-athletes in the first place). The authors note that since the time of the original Sackos filing, Sackos actually resigned from the case and former University of Pennsylvania Women's Track and Field athletes Gillian Berger, Lauren Anderson, and Taylor Henning became the named plaintiffs in the lawsuit. See Berger v. NCAA, Cover Letter to Amended Complaint, Civil Action No. 1:14-CV-1710 WTL-MJD.

53. NLRB v. Northwestern, 2014 N.L.R.B. LEXIS 221, 2014-15 NLRB Dec. (CCH) ¶ 15,781 (2014); Keller v. NCAA 2014 U.S. Dist. LEXIS 71433 (N.D. Cal. May 23, 2014); O'Bannon v. NCAA, 7 F. Supp. 3d 955 (N.D. Cal. 2014); Sackos, No. 1:14-CV-1710 WTL-MJD.

54. See IRC § 117(a) (LEXIS 2015); see also Michael Sanserino, *College Athletes Union*

As such, an understanding of the taxability of qualified scholarships in the wake of the NLRB's 2014 *Northwestern* decision, though it was later overturned and dismissed the following year, is critical in identifying the potential impact such a decision could have on student-athletes' scholarship funds in the future.<sup>55</sup>

### III. HISTORY IN THE MAKING—TAXING ATHLETIC SCHOLARSHIPS IN THE WAKE OF THE NLRB'S 2014 *NORTHWESTERN* DECISION

The Sixteenth Amendment to the U.S. Constitution authorizes Congress to tax income, no matter the source.<sup>56</sup> On October 3, 1913, the same year that the Sixteenth Amendment took effect, Congress approved a tax on the net income of individuals and corporations.<sup>57</sup> Since the 1954 revision of the IRC, the language of Code Section 61 explicitly defines the term “gross income” to include “all income from whatever source derived.”<sup>58</sup>

The following sections discuss how the compensation of student athletes is viewed by the IRS, and analyzes the Supreme Court rulings that have tried to define compensation. Subsection III.A explores how the IRS taxes qualified scholarships. Subsection III.B covers the limiting definition of “compensation for services rendered.” The Court has held that scholarship money that is really compensation for services is taxable under the quid pro quo analysis of *Bingler*. However, the IRS and courts considering the issue have not applied the quid pro quo *Bingler* analysis directly to student-athletes' scholarships. If the issue is considered by the IRS and courts, it is likely that the portion of student-athlete scholarships that are deemed “compensation for services rendered” will be taxable income.

The IRC purposefully grants certain exclusions to the Section 61 canon, including an accommodation under Section 117 that an individual's gross income exclude money received in the form of qualified

---

*Raises Tax, Discrimination Questions*, PITTSBURGH POST-GAZETTE (Apr. 6, 2014, 12:07 AM), <http://www.post-gazette.com/business/employment/2014/04/06/College-athletes-union-raises-tax-discrimination-questions/stories/201404030298> (noting that a change in employment characterization of student-athletes at the universities they play for may require that the IRS look more closely at the taxability of scholarship money).

55. *NLRB v. Northwestern*, 2014 N.L.R.B. LEXIS 221; *but see* *Northwestern Univ. and College Athletes Players Association (CAPA)*, 362 NLRB No. 167 (Aug. 17, 2015).

56. U.S. CONST. amend. XVI.

57. *See* REVENUE ACT OF 1913, ch. 16, 38 Stat. 114 (1913), *last amended* by Pub. L. 95-600, 92 Stat. 2763 (1978); *see also* Michael J. Graetz & Michael M. O'Hear, *The “Original Intent” of U.S. International Taxation*, 46 DUKE L.J. 1021, 1022 (1997) (providing a brief history of U.S. taxation).

58. IRC § 61(a) (LEXIS 2015).

scholarships.<sup>59</sup> An important limitation to this exclusion requires that if any “portion of scholarship money received . . . represents a payment for teaching, research or other services by the student required as a condition for receiving the qualified scholarship . . . ,” such funds are taxable.<sup>60</sup>

From a federal income tax perspective, the significance of the NLRB’s 2014 *Northwestern* decision lay in the interpretation of whether, as employees of their private institution, Northwestern University football players—along with other student-athletes in similar situations—would be found to receive some or all of their scholarship money *in exchange for services required* as a condition for receiving their scholarship money.<sup>61</sup> To advance this issue, an understanding of IRC Section 117 and the corresponding Treasury Regulations is necessary.<sup>62</sup>

#### A. Taxing Qualified Scholarships—Understanding IRC Section 117

Prior to the middle of the twentieth century, no specific exclusion existed within the language of the IRC governing the omission of scholarship money from the parameters of federal income taxation.<sup>63</sup> Such a bright line tenet was not implemented into the structure of the IRC until the Congressional enactment of Code Section 117 in 1954, which specifically excluded scholarship and fellowship grants from the taxability of gross income.<sup>64</sup>

The original scholarship exclusion was largely eroded in 1986 when Congress required (1) that scholarships be taxable to the extent of the value of services provided, (2) limited the exclusions for degree candidates to amounts for qualified tuition and related expenses, and (3) compelled that all grants for living expenses be taxable.<sup>65</sup> A primary objective of the federal government enacting Section 117 was to encourage and provide access to students seeking higher education,

59. See IRC § 117(a) (LEXIS 2015).

60. IRC § 117(c) (LEXIS 2015).

61. NLRB v. Northwestern, 2014 N.L.R.B. LEXIS 221, 2014-15 NLRB Dec. (CCH) ¶ 15,781 (2014).

62. IRC § 117(a); Treas. Reg., §§ 1.117-1(a), 1.117-3(b), and 1.117-4(c) (LEXIS through Oct. 28, 2015 issue of the Fed. Register).

63. Richard C.E. Beck, *Loan Repayment Assistance Programs for Public-Interest Lawyers: Why Does Everyone Think They are Taxable?*, 40 N.Y.L. SCH. L. REV. 251, 258 (1996) (Providing a brief history of tax exclusions for scholarships); see also Mimi Sharamitaro, Comment: *The Federal Tax System and Treatment of Scholarships For Graduate Students: Should Scholarships Be Taxed?*, 48 ST. LOUIS L.J. 1501, 1502-03 (2004) (noting that prior to 1954, scholarships were excludible under the general provision of the Internal Revenue Code exempting gifts).

64. See IRC § 117 (LEXIS 2015); see also Beck, *supra* note 63, at 258.

65. See Beck, *supra* note 63, at 260-61; see also Tax Reform Act of 1986, Pub. L. No. 99-514, 123, 100 Stat. 2085, 2112 (codified at IRC § 117(a) (1994)); IRC § 117(b) (LEXIS 2015).

notwithstanding income level.<sup>66</sup> Today, Section 117 excludes from gross income amounts received as qualified scholarships by individuals who are candidates for degrees at educational institutions.<sup>67</sup> It is the sole Congressional provision excluding such amounts from gross income.<sup>68</sup>

Generally, the term “qualified scholarship” includes amounts received by individuals as scholarship funds used for qualified tuition and related expenses, including fees, books, supplies, and equipment required for courses of instruction, to aid in the pursuit of study or research.<sup>69</sup> In order to be treated as related expenses, fees, books, supplies, and equipment must be required of all students in the specified course of instruction.<sup>70</sup> Scholarship money used for incidental expenses, such as room, board, travel, and research, is not excludable from gross income.<sup>71</sup>

Section 117 further mandates that scholarship recipients be candidates for a degree at an educational organization to qualify for the tax exclusion.<sup>72</sup> Specifically, amounts paid to an individual to help pursue their studies or to conduct research are considered Section 117 scholarship amounts “if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity . . . .”<sup>73</sup> Such requirement entails that the student attend a primary or secondary school or be an undergraduate or graduate student pursuing a degree at a

66. See Sharamitaro, *supra* note 63, at 1503.

67. See IRC § 117(a); see also IRC § 170(b)(1)(A)(ii) (defining the term “educational organization” as “an educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or student in attendance at the place where its educational activities are regularly carried on”); Stuart Lazar, *Schooling Congress: The Current Landscape of the Tax Treatment of Higher Education Expenses and a Framework for Reform*, 2010 MICH. ST. L. REV. 1047, 1083 (2010) (discussing the tax exclusion for scholarships and fellowship grants).

68. See Lazar, *supra* note 67, at 1083-84; see also Treas. Reg. § 1.117-1(a) (LEXIS through Oct. 28, 2015 issue of the Fed. Register).

69. IRC § 117(b)(1); see also Treas. Reg. § 1.117-3(a) (LEXIS through Oct. 28, 2015 issue of the Fed. Register) (The term qualified scholarship also applies to fellowship grants received by individuals and used for qualified tuition and related expenses.); Lazar, *supra* note 67, at 1084 (discussing the inclusion of related expenses within the parameter of IRC Section 117); IRC § 117(b)(2)(A) (defining the term “qualified tuition and related expenses” as “tuition and fees required for the enrollment or attendance of a student at an educational organization . . .”).

70. Prop. Treas. Reg. § 1.117-6(c)(2), 53 Fed. Reg. 21688 (Jun. 9, 1988).

71. IRC § 117(b)(1); see also Prop. Treas. Reg. § 1.117-6(c)(2); Lazar, *supra* note 67, at 1084 (noting those items associated with scholarship and fellowship grants which are includable in gross income).

72. IRC § 117(a); see also IRC § 170(b)(1)(A)(ii) (defining the term “educational organization” as a facility that “normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on”); Treas. Reg. § 1.117-3(b) (LEXIS through the Nov. 4, 2015 issue of the Fed. Register).

73. Treas. Reg. § 1.117-4(c)(2) (1988).

college or university.<sup>74</sup>

Although Section 117 and the applicable Treasury Regulations offer tax exclusions for scholarship recipients pursuing educational studies or research, a key limitation applies if any scholarship amounts “represent either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.”<sup>75</sup> Prior to 1986, students receiving funds representing payment for services could exclude such amounts received from their gross income so long as all candidates were performing the same services.<sup>76</sup> However, such exclusion was repealed by the Tax Reform Act of 1986.<sup>77</sup>

Under the present Code, IRS Regulations clarify that scholarship amounts paid to recipients *representing compensation or payment for services* are specifically not excludable from gross income.<sup>78</sup> Treasury Regulation § 1.117-4(c), promulgated under Code Section 117, purposefully identifies scholarship amounts representing compensation for services as includable in gross income and therefore taxable.<sup>79</sup> In 1969, the U.S. Supreme Court upheld the validity of Treasury Regulation § 1.117-4(c), denying a scholarship exclusion from gross income where tuition represented compensation for services.<sup>80</sup> Therefore, an understanding of the language of this Treasury Regulation, along with judicial interpretations, follows.

#### *B. Compensation for Services Rendered—Treasury Regulation § 1.117-4(c) and Judicial Interpretation.*

The IRC has specific statutory sections in place governing qualified scholarship funds. Both the U.S. Supreme Court and Tax Court have applied the applicable Treasury Regulations to scholarship recipients and

---

74. Lazar, *supra* note 67, at 1084-85 (noting the IRC Section 117 requirements that an individual receiving a scholarship or grant be a candidate for degree at a qualified educational organization); *see also* Prop. Treas. Reg. § 1.117-6(c)(4) 53 Fed. Reg. 21688 (Jun. 9, 1988).

75. Treas. Reg. § 1.117-4(c)(1) (LEXIS through Nov. 4, 2015 issue of the Fed. Register).

76. Sharamitaro, *supra* note 63, at 1502-04.

77. *Id.*; *see also* Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2112 (1986).

78. *See* IRC § 117(c)(1) (LEXIS 2015); *see also* Treas. Reg. § 1.117-4(c)(2).

79. *See* Treas. Reg. § 1.117-4(c).

80. *See* Bingle v. Johnson, 394 U.S. 741 (1969) (finding that respondent-engineers, participating in a fellowship program which required both a “work-study” obligation requiring that they work part-time while attending university classes, and a “research” obligation which provided respondents a leave of absence to work on their doctoral dissertations, was taxable because respondents had provided services in exchange for their scholarship money); *see also* Adam Hoefflich, Note, *The Taxation of Athletic Scholarships: A Problem of Consistency*, 1991 U. ILL. L. REV. 581, 589-92 (1991).



have consistently held that there must be a quid pro quo in order for the scholarship funds to be taxable.<sup>81</sup> In situations in which students' scholarship money is dependent upon rendering services to the university, the Courts have held that the funds are taxable income.<sup>82</sup>

The primary objective of Treasury Regulation § 1.117-4 is to earmark circumstances where tuition remission represents compensation for services, and thereby deny the application of the Section 117 scholarship exclusion from taxability.<sup>83</sup> Payments are not considered scholarship amounts or fellowship grants if: (1) the amount represents compensation for "past, present or future employment purposes," (2) the activity the scholarship or grant payment funds is "subject to the direction or supervision of the grantor," or (3) the amount paid enables the recipient "to pursue studies or research primarily for the benefit of the grantor."<sup>84</sup>

Over the years, various courts have scrutinized the application of Treasury Regulation § 1.117-4(c) to scholarship recipients.<sup>85</sup> However, the premier case characterizing the proper application of this regulation is *Bingler v. Johnson*.<sup>86</sup> In *Bingler*, the U.S. Supreme Court held that taxpayers who provide services in exchange for their scholarship grants—quid pro quo—may not exclude the value of such grants from their gross income.<sup>87</sup> The taxpayers in this case—engineers at Westinghouse—sought to exclude amounts received by their employer from income while attending graduate school in pursuit of their Ph.D. degrees.<sup>88</sup> The respondents in *Bingler* participated in a fellowship program requiring both work-study and research obligations.<sup>89</sup> The work-study segment entailed that the respondents work part-time and obtain a part-time release from

---

81. *E.g.*, *Bingler v. Johnson*, 394 U.S. 741 (1969); *Willie v. Comm'r*, 57 T.C. 383, 386 (1971).

82. *E.g.*, *Bingler*, 394 U.S. 741; *Willie*, 57 T.C. at 386.

83. *See* Wendy Gerzog Shaller, *The New Fringe Benefit Legislation: A Codification of Historical Inequities*, 34 CATH. U. L. REV. 425, 434 (1985).

84. *See* Treas. Reg. § 1.117-4(c)(1), (2).

85. *See e.g.*, *Willie* 57 T.C. at 386 (1971) (Petitioner, an instructor employed by the Biloxi School District, participated in an education program funded through the U.S. Department of Health, Education, and Welfare (HEW). Although not required, the Biloxi School District encouraged teachers to participate in the program with the goal of improving the education of children and providing teachers with teaching and coping methods to be utilized in the newly desegregated schools in the area. Petitioner did not include the reimbursed amount of his attendance in his taxable income for the year at issue. Finding that the payments received by the HEW represented compensation for services rendered, the U.S. Tax Court held that petitioner's participation in the training program was primarily for the benefit of the Biloxi School District, and therefore includable in his gross income.).

86. 394 U.S. 741 (1969).

87. Hoeflich, *supra* note 80, at 589.

88. *See Bingler*, 394 U.S. at 742; *see also* Gary C. Randall, *Athletic Scholarships and Taxes: Or a Touchdown In Taxes*, 7 GONZ. L. REV. 297, 300 (1972) (reviewing the *Bingler* case in detail).

89. *See Bingler*, 394 U.S. at 742-44; *see also* Hoeflich, *supra* note 80, at 589-90.

work to attend university classes, while the research obligation allowed the respondents a leave of absence from employment to work on their doctoral dissertations.<sup>90</sup> Westinghouse paid the respondents' tuition and expenses during the work-study phase, as well as a stipend during the research phase of the program.<sup>91</sup> The taxpayers contended that the stipends received from Westinghouse during the research phase of the fellowship program were scholarship amounts and should be excludable from gross income.<sup>92</sup>

Endorsing the legitimacy of Treasury Regulation 1.117-4(c) in its review of this case, the *Bingler* Court remarked:

[T]he definitions supplied by the Regulation clearly are prima facie proper, comporting as they do with the ordinary understanding of "scholarships" and "fellowships" as relatively disinterested, "no-strings" educational grants, with no requirement of any substantial quid pro quo from the recipients.<sup>93</sup>

In making this statement, the U.S. Supreme Court stressed the importance of the quid pro quo test, maintaining that students who provide services in exchange for scholarships or grants may not exclude their awards from gross income.<sup>94</sup> Specifically, the Court held that a payment cannot be earmarked as a scholarship in circumstances "where the recipient receives money, and in return provides a quid pro quo."<sup>95</sup> Thus, any amounts received in return for services rendered are treated as compensation rather than scholarship funds.<sup>96</sup>

Apart from *Bingler*, interpreting Code Section 117 and its applicable Treasury Regulations has been articulated in various U.S. Tax Court reviews.<sup>97</sup> In *Bonn v. Commissioner*, the U.S. Tax Court held that funds

---

90. *Bingler*, 394 U.S. at 743-44; see also Hoeflich, *supra* note 80, at 590.

91. *Bingler* 394 U.S. at 743 (the stipends received from Westinghouse ranged from 70-90% of the respondents' prior salaries); see also Hoeflich, *supra* note 80, at 590.

92. *Bingler*, 394 U.S. at 744-45 (Westinghouse, under its in-house accounting program, listed the stipend paid to the respondents as "indirect labor" expenses, and withheld the appropriate federal income tax from those amounts paid. Respondents subsequently filed claims for income tax refunds); see also Hoeflich, *supra* note 80, at 590.

93. *Bingler*, 394 U.S. at 751; see also Randall, *supra* note 88, at 300.

94. Hoeflich, *supra* note 80, at 591.

95. *Bingler*, 394 U.S. at 758 (quoting Brief for Petitioner 22); see also Jonathan M. Layman, Comment: *Forgiven but Not Forgotten: Taxation of Forgiven Student Loans Under the Income-Based Repayment Plan*, 39 CAP. U. L. REV. 131, 149 (2011).

96. See Prop. Treas. Reg. 1.117-6(d)(2) (1988); see also Ernest R. Larkins, *Coming To America: International Students Face a Labyrinth of Income Tax Issues*, 15 CONN. J. INT'L. L. 47, 70 (2000).

97. *Bingler*, 394 U.S.. See, e.g., *Bonn v. Comm'r*, 34 T.C. 64 (1960); *Proskey v. Comm'r*, 51 T.C. 918 (1969).

received by a physician in exchange for services provided to a Veterans' Administration (VA) hospital under a fellowship program constituted compensation for services rather than a fellowship grant.<sup>98</sup> In making this determination, the Court found that the VA hospital existed primarily for patient care and that the needs of the fellowship training program were incidental to the valuable services, which petitioner provided to assist in the care and treatment of patients in exchange for compensation.<sup>99</sup> Similarly, in *Proskey v. Commissioner*, the U.S. Tax Court sustained the Commissioner of Revenue's determination that a stipend received by the taxpayer, a resident physician, in exchange for his supervisory role over medical students, interns, and assistant residents constituted compensation for services rendered to the hospital rather than a fellowship grant.<sup>100</sup>

In *Zolnay v. Commissioner*, the U.S. Tax Court held that payments received by a Ph.D. candidate from his institution were taxable as compensation for services rendered and therefore not excludable as a scholarship or fellowship grant.<sup>101</sup> In this case, the petitioner, a Ph.D. candidate in electrical engineering, performed studies for the Ohio State University as a research assistant.<sup>102</sup> In exchange for his required forty-hour work weeks, the petitioner received monthly compensation.<sup>103</sup> The Court, concluding that such payments were compensation in exchange for

---

98. *Bonn*, 34 T.C. 64. Petitioner, a physician, was accepted into a fellowship program operated by the Menninger Foundation, and was appointed by the Veterans' Administration (VA) to a psychiatry residency at a VA hospital under a fellowship program. In consideration for petitioner's services, which included supervising course instruction and training in psychiatry, neuropathology, and neurophysiology to medical residents, petitioner received certain funds which she documented on her income tax return as being a fellowship grant. The Commissioner of Internal Revenue found that the funds received during the tax year at issue to be compensation for valuable services rendered. The U.S. Tax Court sustained this decision. *Id.* at 64-66, 73.

99. *Id.* at 73.

100. *Proskey v. Comm'r*, 51 T.C. 918 (U.S. Tax Ct. 1969). Petitioner, a licensed physician and resident at University Hospital in Ann Arbor, Michigan, received yearly monetary stipends during his medical residency. The amounts received were based upon the number of years of service that petitioner provided as a resident. In return, petitioner supervised the activities of medical students, interns, and assistant residents. During the years of his residency, petitioner was not a candidate for a degree. The Commissioner of Internal Revenue found that the stipend received during the tax year at issue was compensation for employment services rendered, not a fellowship grant. The U.S. Tax Court sustained this determination. *Id.* at 919-22.

101. *Zolnay v. Comm'r*, 49 T.C. 389, 399 (1968). During that tax period at issue, petitioner worked solely on the subject of her thesis, which was not an established University research project, thus fulfilling the Masters Program's degree requirements. During this period, the facts document that the University did not treat petitioner as an employee and that the terms of the graduate assistantship did not require that she do any teaching or research on University projects while receiving funding. *Id.* at 394.

102. *Id.* at 394-95.

103. *Id.* at 396-97.

services, noted several considerations, including: (1) petitioner's forty-hour work weeks; (2) the requisite supervised activities, planned time schedules, and progress reports; (3) the amount paid to petitioner; (4) the disconnect between petitioner's research and his doctoral dissertation; (5) the fact that petitioner's application for a graduate fellowship had been disapproved; and (6) that the university regarded petitioner as an employee.<sup>104</sup>

In contrast to *Zolnay*, the U.S. Tax Court in *Smith v. Comm'r* determined that funds given by a university to a student working as a graduate assistant while completing her Master's degree constituted a scholarship or fellowship grant.<sup>105</sup> In its published opinion, the Tax Court cited to *Bingler* and documented several factors used in drawing its conclusion, including the fact that petitioner worked only on her studies during the tax period at issue, that the University did not receive a direct substantial benefit from petitioner's research, that petitioner did not teach or conduct research on any University project during the funding period, and that there was no indication that petitioner was required to publish her findings in exchange for receiving university funds.<sup>106</sup> Although the respondent argued that payments made to petitioner were taxable as income because they were made in exchange for services rendered to the University, the Tax Court denied this argument, finding no quid pro quo present.<sup>107</sup>

The above case examples articulate the IRS's treatment of academic scholarships as non-taxable income where there is no quid pro quo involved.<sup>108</sup> However, amounts that represent payment in exchange for teaching, research or other services as a condition for receiving the scholarship are deemed valuable consideration and therefore taxable as income.<sup>109</sup> Although the quid pro quo interpretation of Section 117 and the Treasury Regulations as enunciated in *Bingler* seems clear, such application has not necessarily been an operational reality at the collegiate level, as universities have not yet moved towards treating student-athlete scholarships as qualified taxable income.<sup>110</sup>

---

104. *Id.* at 397-99.

105. *Smith v. Comm'r*, 51 T.C.M. (CCH) 1348 (1986).

106. *Id.* at 1350.

107. *Id.*

108. See Jake Linford, *Organ Donation & Human Subjects Research: New Perspectives: 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).

109. *Id.*

110. *Id.*; see also Hoeflich, *supra* note 80, at 592 (noting that the law is clear that if an

Numerous scholarly publications have noted a disconnect between the imposition of Section 117 and *Bingler* to athletic grants-in-aid.<sup>111</sup> Although the debate is open as to whether student-athletes actually provide services in exchange for their athletic scholarships, the IRS has never sought to tax athletic scholarships.<sup>112</sup> Of intrigue to this ongoing deliberation, on January 21, 2015, two former University of North Carolina Chapel Hill (UNC) student-athletes—Rashanda McCants and Devon Ramsay—filed a lawsuit against the school and the NCAA alleging that they represented hundreds of thousands of student-athletes nationwide who were promised an education in return for generating millions of dollars in revenue each year, yet receive an inferior instruction.<sup>113</sup> The complaint accuses the NCAA of knowingly allowing

---

educational institution requires services of a student in exchange for a grant or stipend, that student must include such amount in their gross income).

111. See, e.g., Randall, *supra* note 88, at 299-309 (analyzing the application of IRC Section 117 and related case law to the current scholarship model in college athletics and ultimately concluding that athletic scholarships should be taxable under the current language of the Code); Hoeflich, *supra* note 80, at 602, 614-17 (scrutinizing the quid pro quo application of Section 117 to athletic scholarships, and proposing that the IRS tax student-athletes' scholarship money, or alternatively suggesting that the NCAA change its rules in order to avoid such treatment); 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 it is "widely recognized" that athletic scholarships do not meet the exclusionary requirements of IRC Section 117 because student-athletes are required to perform athletic services in exchange for receipt of their scholarship money); Daniel Nestel, Note: *Athletic Scholarships: An Imbalance of Power Between the University and the Student-Athlete*, 53 OHIO ST. L. J. 1401, 1413 (1992) (arguing that athletic scholarships create a quid pro quo relationship between the university and student-athlete because student-athletes are required to perform services in exchange for their scholarship money); William B. Gould IV, Glenn M. Wong & Eric Weitz, *Full Court Press: Northwestern University, A New Challenge to the NCAA*, 35 LOY. L.A. ENT. L. REV. 1, 60 (2014) (noting that if the value of an athletic scholarship is deemed a salary, student-athletes may be taxed on such income based on the holding in *Bingler*).

112. See, e.g., Hoeflich, *supra* note 80, at 592 (observing that because the IRS has never sought to tax athletic scholarships, schools must not require services in exchange for scholarship money; however, the author further provides that such conundrum indicates otherwise.); see also Nestel, *supra* note 111, at 1413 (scrutinizing that the current language of Section 117 creates a quid pro quo relationship as the student-athlete is required to perform services for the university); Robert McCormick & Amy Christian McCormick, *The Myth of the Student-Athlete: The College Athlete as Employee*, 81 WASH. L. REV. 71, 86 (2006) (arguing that the NCAA's insistence on characterizing student-athletes as amateurs masks the reality that universities employ players to provide athletic services in exchange for compensation); Linford, *supra* note 108, at 302 (providing that it is uncertain why the IRS does not tax athletic scholarships regardless of the fact that it is a bargained-for exchange between player and university).

113. See *McCants v. NCAA*, Class Action Complaint, Jury Trial Demand, 15 CVS 1782 (Super. Ct. NC, Jan. 22, 2015), available at <http://www.cbssports.com/images/blogs/Hausfeld-complaint.pdf>; see also Sara Ganim, *Lawsuit Claims UNC and NCAA Broke Promises In 'Spectacular Fashion'*, CNN (last updated Jan. 23, 2015, 7:58 AM), <http://www.cnn.com/2015/01/22/us/unc-paper-classes-lawsuit/index.html> (evaluating the lawsuit filed against UNC and the NCAA); Michael McCann & John Wertheim, *Rashanda McCants, Devon Ramsey file suit against UNC, NCAA*, SPORTS

member schools to commit academic fraud in promising educations and educational opportunities to scholarship student-athletes, and yet failing to implement adequate monitoring systems to prevent such fraud from occurring.<sup>114</sup> Specifically, the lawsuit takes aim at “the NCAA and UNC’s abject failure to safeguard and provide a meaningful education to [scholarship] athletes who agreed to attend UNC—and take the field—in exchange for academically sound instruction.”<sup>115</sup> Although this complaint does not include a tax issue, the key language within the complaint specifying the verbiage *in exchange for* could pose another interesting twist in the future application of IRC Section 117 should taxing athletic scholarships stimulate the IRS’s interest in the future.<sup>116</sup>

Applying *Bingler’s* quid pro quo analysis to student-athletes is straightforward—if a university requires that the student-athlete perform services in exchange for their grant-in-aid, that student may not exclude the scholarship amount from gross income.<sup>117</sup> An examination of the degree of control that universities and coaches exert on student-athletes throughout the course of the calendar year, coupled with the compensation paid to them in the form of athletic grants-in-aid, and the economic dependency of student-athletes on their universities suggest that student-athletes are in fact paid-to-play.<sup>118</sup> Further, a review of the court testimony from the *O’Bannon* case provides strong evidence that certain student-athletes are required to participate in sports in exchange for their scholarship earnings.<sup>119</sup> Specifically, during trial, Ed O’Bannon and other former student-athletes testified that their job at school was to play sports and that playing college sports was their main occupation due to the

---

ILLUSTRATED (last updated Jan. 23, 2015), <http://www.si.com/college-basketball/2015/01/06/rashanda-mccants-unc-paper-classes-lawsuit> (analyzing the *McCants v. UNC* case).

114. Steve Berkowitz, North Carolina, *NCAA Sued for Academic Scandal*, USA TODAY (Jan. 22, 2015, 9:50 PM), <http://www.usatoday.com/story/sports/college/2015/01/22/lawsuit-filed-against-north-carolina-ncaa-on-academic-scandal/22173755/>.

115. Steven Ginsburg, *Two ex-North Carolina Athletes File Lawsuit Alleging Academic Fraud*, REUTERS (Jan. 22, 2015, 6:12 PM), <http://www.reuters.com/article/2015/01/22/us-unc-fraud-lawsuit-idUSKBN0KV2RO20150122>; see also Jon Solomon, *Ex-North Carolina athletes sue NCAA, UNC over academic scandal*, CBS SPORTS (Jan. 22, 2015, 4:20 PM), <http://www.cbssports.com/collegefootball/writer/jon-solomon/24984287/ex-unc-athletes-sue-ncaa-unc-over-academic-scandal> (noting that the plaintiffs’ lawyers are seeking an injunctive relief class defined as “anyone who attended North Carolina on an athletic scholarship, past or present”).

116. *E.g.*, Solomon, *supra* note 115.

117. See Hoefflich, *supra* note 80, at 602.

118. See McCormick & McCormick, *supra* note 112, at 97-119 (providing a thorough analysis of the extent of control that universities have over student-athletes).

119. *Id.*

magnitude of time they were required to devote.<sup>120</sup> Finally, the original NLRB *Northwestern* decision reinforced the argument that student-athletes receive a substantial economic benefit of scholarship money in exchange for performing football-related services, under what amounts to a contract-for-hire.<sup>121</sup>

NCAA member institutions hold vast power which allows them to cancel scholarship benefits.<sup>122</sup> In order to receive full benefits during the term of the scholarship, recipients must be academically eligible, not fraudulently misrepresent information on their application, letter of intent, or financial aid agreement, not engage in serious misconduct warranting substantial disciplinary penalty, and must continue to participate in the athletic program.<sup>123</sup> Such broad range of university power further articulates the possible application of *Bingler's* quid pro quo analysis to student-athletes.<sup>124</sup>

Still, as the IRS has not pronounced any specific interest in pursuing athletic scholarships to date, the complex inquiry into whether college scholarships are taxable in the future could hinge on whether student-athletes are identified as actual “employees” of the universities they represent.<sup>125</sup> The option of compensating student-athletes as scholarship-earning employees may be more complicated than merely paying them monetary compensation or stipends, as such preference presents the possibility of future legislative changes to the IRC itself or further judicial interpretation of Section 117 with respect to athletic scholarships.<sup>126</sup>

Currently, so long as student-athletes are not required to participate in any specific sport in exchange for scholarship awards, the language of the IRC has not been applied to prevent student-athletes from excluding

---

120. 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/>.

121. WithumSmith+Brown, *supra* note 6.

122. See NCAA Manual 15.3.4.2; see also Nestel, *supra* note 111, at 1413 (noting that “the NCAA rules only prevent a university from terminating a student-athlete’s scholarship benefits during the award term on the basis of injury or athletic ability”).

123. See Nestel, *supra* note 111, at 1413; see also NCAA Manual 15.3.4.2.

124. See Nestel, *supra* note 11, at 1413; see also *Bingler v. Johnson*, 394 U.S. 741 (1969).

125. See Hoeflich, *supra* note 82, at 581; see also Sanserino, *supra* note 56 (noting the potential IRS implications which could emerge from the changing nature of the relationship between student-athletes and universities).

126. See Hoeflich, *supra* note 80, at 592 (noting that the IRS has never sought to tax athletic scholarships); see also Robert W. Lee, *The Taxation of Athletic Scholarships: An Uneasy Tension between Benevolence and Consistency*, 37 U. FLA. L. REV. 591, 592 (1985) (documenting that the IRS has never sought to tax athletic scholarships); Mike Schinner, *Touchdowns and Taxes: Are Athletic Scholarships Merely Disguised Compensation?*, 8 AM. J. TAX POL’Y. 127, 139 (1990) (stating that since enactment of section 117, no court has specifically addressed issue of whether athletic scholarships constitute taxable income).

their scholarships from gross income.<sup>127</sup> Thus, under the purview of the current application of Section 117 and *Bingler*, student-athletes receiving qualified scholarships do not pay income taxes on scholarship moneys received.<sup>128</sup> However, such application could change in the future should the NLRB revisit the question as to whether or not to characterize student-athletes as employees of their institutions.

Although the IRC does not specifically define the term “services” with regard to the application of Section 117, the pertinent Treasury Regulations limit “services” to those “in the nature of part-time employment required as a condition to receiving the scholarship.”<sup>129</sup> Based on the previous examination and application of Section 117, evaluating whether student-athletes’ grant-in-aid money could be taxable in the future may pivot on whether student-athletes are deemed to receive some or all of their scholarship money in exchange for services required as a condition for receiving their scholarship money as employees of their institutions.<sup>130</sup> To appreciate the potential impact of characterizing student-athletes as employees of their institutions from a federal income tax perspective, an understanding and application of the employer-employee relationship is critical.

#### IV. THE STUDENT-ATHLETE AS EMPLOYEE—THE FEDERAL INCOME TAX PERSPECTIVE

As previously analyzed, the IRC allows that a taxpayer’s gross income not include amounts received as qualified scholarships by individuals who are degree candidates at educational institutions.<sup>131</sup> However, as also noted, qualified scholarship awards are limiting in that if an educational institution requires services of a student “in exchange” for a monetary grant, then the student cannot exclude scholarship amounts received from their gross income.<sup>132</sup> While the IRC does not specifically

---

127. Potuto et al., *supra* note 4, at 890 n.40 (referencing commentary within footnote 40 with regard to the exclusion of qualified scholarships from the parameters of IRC §117(c)).

128. IRC § 117(c)(1) (LEXIS 2015) (stating that the exclusion for qualified scholarships does not apply to amounts received which represent “payment for teaching, research, or other services by the student required as a condition for receiving the qualified scholarship . . .”).

129. *See* Treas. Reg. § 1.117-2(a)(1) (LEXIS through the Nov. 4, 2015 issue of the Fed. Register).

130. *See id.*; *see also* NLRB v. Northwestern, 2014 N.L.R.B. LEXIS 221, 2014-15 NLRB Dec. (CCH) ¶ 15,781 (2014).

131. IRC §117(a) (LEXIS 2015).

132. *See* Treas. Reg. § 1.501(c)(3)-1(c)(1) (LEXIS, through Nov. 4, 2015 issue of the Fed. Register); *see also*, Hoeflich, *supra* note 80, at 592; Hurst & Pressly, *supra* note 111, at 74 (documenting that although IRC § 117 does not exclude portions of athletic scholarships constituting



define the term “services,” Treasury Regulation 1.117-2 limits services to those “in the nature of part-time employment required as a condition to receiving the scholarship.”<sup>133</sup> Although athletic scholarships are not currently taxable to the student-athlete, if players are deemed “employees” of their institutions, it is feasible that the IRS may eventually reevaluate whether student-athletes are receiving part or all of their scholarship money in exchange for services rendered.<sup>134</sup>

The employee characterization of scholarship athletes indicating a shift from the amateur/ education model to the commercial/education model could increase the likelihood that athletic scholarships will be taxable as gross income.<sup>135</sup> Specifically, if any portion of an athletic scholarship is found to be granted in exchange for services provided to their institution, such portion would constitute taxable income to the student-athlete.<sup>136</sup> The original NLRB 2014 *Northwestern* decision supported the notion that student-athletes receive a substantial economic benefit of scholarship money in exchange for performing football-related services, under what amounts to a contract-for-hire.<sup>137</sup> A contract-for-hire “binds an employer to pay compensation to an employee who performs services, sets forth the place to perform such services and the work to be performed, and sets the compensation for the performance of such work.”<sup>138</sup> In the event a contract-for-hire exists, the question is whether such contract creates an employer-employee relationship.<sup>139</sup>

To thoroughly analyze whether an employer-employee relationship exists between student-athletes and their universities, Subsection IV.A explores the various tests used to determine whether a scholarship falls

---

room and board from gross income, few student-athletes report room and board as income, and the IRS has not pursued the issue); Schinner, *supra* note 126, at 146-48, 155 (noting that room, board, or incidental expenses must be included in a recipient’s gross income); Lee, *supra* note 126, at 595 (stating that IRC § 117(c) applies to scholarship athletes because they must be degree candidates).

133. Treas. Reg. § 1.117-2(a)(1) (LEXIS through the Nov. 4, 2015 issue of the Fed. Register).

134. See *infra* notes 174-210 and accompanying text.

135. Timothy Davis, *Intercollegiate Athletics: Competing Models and Conflicting Realities*, 25 RUTGERS L.J. 269, 323 (1994) (providing that “under the amateur/education model, the student-athlete is viewed as an amateur, and college athletics is considered an integral part of the education purpose of universities.” *Id.* at 273. Under the commercial/education model, education still remains a component; however, a predominant characteristic is that college athletics is a commodity capitalizing on “the potential benefits of a successful athletic program.”) *Id.* at 279-80.

136. See IRC § 117(c)(1) (LEXIS 2015); see also C. Peter Goplerud III, *Symposium: Sports Law As A Reflection Of Society’s Laws And Values: Pay for Play For College Athletes: Now, More Than Ever*, S. TEX. L. REV. 1081, 1102 (1997).

137. WithumSmith+Brown, *supra* note 6.

138. Davis, *supra* note 135, at 283; see also Ray Yasser, *Are Scholarship Athletes at Big-Time Programs Really University Employees?—You Bet They Are!*, 9 THE BLACK L.J. 65, 65 (1984).

139. Davis, *supra* note 135, at 284.

within taxable income. First Subsection IV.A.1 reveals that the IRS twenty-factor test and some state workers' compensation cases support construction of the student-athlete as an employee. Subsection IV.A.2 concludes that the economic realities test used under FLSA and by some states for workers' compensation supports finding student-athletes as employees. Additionally, Subsection IV.A.3 addresses a hybrid test for federal discrimination supporting the treatment of student-athletes as employees. Finally, Subsection IV.B includes commentators who support defining student-athletes as employees for various reasons.

### A. Examining the Employer-Employee Relationship

Whether an individual is covered by a particular employment, labor, or tax law hinges on the definition of "employee."<sup>140</sup> Because no set standard at the federal or state level affords a legislative definition of the term employee, various tests have been occupied to help decipher the appropriate characterization of such a worker.<sup>141</sup> The depiction of an individual as an employee generally requires an analysis under one of the various commonly utilized tests, including: (1) the common law test (embraced by the IRS), (2) the economic realities test, and (3) the hybrid test.<sup>142</sup>

#### 1. The Common Law/IRS Twenty-Factor Test

The common law test was developed under the traditional legal basis of agency law, which requires that within an employment context one person (the employee) acts for or represents another (the employer) by the

---

140. Susan N. Housman, *Who Is an Employee? Determining Independent Contractor Status*, U.S. DEP'T. OF LABOR (Aug. 1999), [http://www.dol.gov/dol/aboutdol/history/herman/reports/futurework/conference/staffing/9.1\\_contractors.htm](http://www.dol.gov/dol/aboutdol/history/herman/reports/futurework/conference/staffing/9.1_contractors.htm).

141. *See id.*

142. *See* Charles J. Muhl, *What is an Employee? The Answer Depends on the Federal Law*, MONTHLY LABOR REV. 1, 5-6 (Jan. 2002), <http://www.bls.gov/opub/mlr/2002/01/art1full.pdf>; *see also* Karen R. Harned, Georgine M. Kryda & Elizabeth A. Milito, *Creating A Workable Legal Standard for Defining an Independent Contractor*, 4 J. BUS. ENTREPRENEURSHIP & L. 93, 99-100 (2010) (noting that state and local governments have used several different tests to address the question of employer/employee relationship, to include the common law approaches, the IRS approach, and the ABC Test (a third test used by some states in determining whether workers are classified as employees or independent contractors for state unemployment tax purposes)); YOUR DICTIONARY, ABC test—Legal Definition, <http://www.yourdictionary.com/abc-test> (last visited Feb. 24, 2015) (The ABC test asks: (1) does the individual work independently of the employer's control (A = Alone), (2) does the individual maintain his own place of business (B = Business), and (3) Does the individual work at an established trade and exercise control over his own schedule and work environment (C = Control)).

employer's authority.<sup>143</sup> Under the common law test, courts have evaluated both contractual intent and the right to control to analyze whether an employer-employee relationship exists.<sup>144</sup>

In conjunction with the idea of contractual intent, courts have noted that there must be a showing of "intent to enter into an employee-employer relationship at the time the parties entered into the agreement."<sup>145</sup> Specifically, there must be an indication of a shared understanding that an employer-employee relationship exists.<sup>146</sup> In evaluating the right to control, an examination of whether the employer possesses "the right to control the manner, means, and details of the worker's performance" is required.<sup>147</sup> Factors influencing this analysis include "contractual provisions, the exercise of control, the method of payment, the furnishing of equipment, and the right to terminate the employee."<sup>148</sup> Although the common law test involves an evaluation of ten individual factors to determine whether a person is an employee, with no one single factor being dispositive, the IRS uses a derivative of this test, taking into account some of the common law test factors as part of its own twenty-factor test.<sup>149</sup>

143. Muhl, *supra* note 142, at 3 (citing to BLACK'S LAW DICTIONARY, p. 62); *Id.* at 5.

144. Justin C. Vine, Note: *Leveling the Playing Field: Student Athletes Are Employees of their University*, 12 CARDOZO PUB. L. POL'Y. & ETHICS J. 235, 246-47 (2013); *see also* Rensing v. Indiana State Univ. Bd. of Trs., 444 N.E.2d 1170, 1173 (Ind. 1983) (involving a collegiate football player who suffered a debilitating injury resulting in his claim for recovery under workmen's compensation; the court noted, "It 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."); *see also* E.E.O.C. v. Sidley Austin Brown & Wood, 315 F. 3d 696, 705 (7th Cir. 2002) (noting that "[t]he 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).

145. Vine, *supra* note 144, at 248; *see also* Rensing v. Indiana State Univ. Bd. of Trs., 444 N.E.2d 1170, 1173 (Ind. 1983).

146. Vine, *supra* note 144, at 248.

147. Davis, *supra* note 135, at 286; *see also* Cmty. For Creative Non-Violence v. Reid, 490 U.S. 730, 751-52 (1989).

148. Davis, *supra* note 135, at 286; *see also* ARTHUR LARSON, THE LAW OF WORKMEN'S COMPENSATION, § 44.31, at 8-89 (1990).

149. *See* Muhl, *supra* note 142, at 5, 7 (offering that the ten factors analyzed under the common law test are: right to control, type of business, supervision, skill level, tools and materials, continuing relationship, method of payment, integration, intent, and employment by more than one firm); *see also* 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)); Marilyn Barrett, *Independent Contractor/Employee Classification in the Entertainment Industry: The Old, the New and the Continuing Uncertainty*, 13 U. MIAMI ENT. & SPORTS L. REV. 91, 96-98 (1995, 1996) (expanding on the IRS's twenty-factor test when differentiating between employees and independent contractors:

1. Instructions or Degree of Control. An employer generally exercises a far greater degree of supervision and control over the details of the work being done by employees than by

The IRS twenty-factor test on employment status (IRS test) is not a test per se but an analytical tool employed to arrive at a determination of the control test.<sup>150</sup> Similar to the common law test, no single factor within the IRS test is weighted heavier than another, and there is no minimum

---

independent contractors.

2. Furnishing of Training. An employer generally does not provide training to independent contractors.

3. Integration. An independent contractor generally engages in projects that are not a part of the day-to-day operations of the company.

4. Services Rendered Personally; Right to Delegate Work. An employee is generally required to render the requested services personally.

5. Right to Hire, Supervise, Pay and Fire Assistants. An independent contractor provides the labor necessary to accomplish the purpose of the contract and has the right to hire, supervise, pay and fire assistants. In contrast, if the person for whom the services are performed has these rights, an employee relationship is indicated.

6. Continuing Relationship. An independent contractor is generally hired for a specified time period whereas an employee is generally hired for an indefinite period of time.

7. Control Over Hours of Work. The employer's right to set the hours worked indicates employee status.

8. Independent Trade; Full Time Work. Where a worker must work full time for the employer for whom services are provided, such person has greater control over the worker's work.

9. Place of Work. Working on the employer's premises indicates employer control and employee status.

10. Sequence of Work. An employer does not direct an independent contractor as to the sequence in which the work should be performed, only the outcome of the work to be.

11. Reports Required. An independent contractor is generally not required to submit regular reports or attend regular meetings.

12. Payment by Hour, Week, or Month. An independent contractor is generally paid by the job whereas an employee is generally paid by the hour, week or month.

13. Payment of Business and/or Travel Expenses. A worker whose business and/or traveling expenses is reimbursed by the person for whom services are performed is ordinarily an employee.

14. Furnishing of Tools. An employee is provided tools by the employer.

15. Investment in Facilities. Lack of an investment in facilities indicates dependence upon the person for whom services are provided and employee status.

16. Profit and Loss. An employee generally does not bear a real economic risk.

17. Working for More than One Firm. An independent contractor frequently works for many firms simultaneously.

18. Making Work Available to the General Public. A worker who makes his services available to the general public on a regular and consistent basis is generally an independent contractor.

19. Right to Discharge. An employer may terminate an employee at will, absent a written employment contract and subject to limitations under applicable labor and tort laws.

20. Right to Terminate. If a worker has the right to terminate the relationship at any time without incurring liability, an employee relationship is indicated.)

150. Judson D. Stelter, Note, *The IRS' Classification Settlement Program: Is It an Adequate Tool to Relieve Taxpayer Burden for Small Businesses that Have Misclassified Workers As Independent Contractors?*, 56 CLEV. ST. L. REV. 451, 457-58 (2008) (citing Jack E. Karns, *Current Federal and State Conflicts in the Independent Contractor Versus Employee Classification Controversy*, 22 CAMPBELL L. REV. 105, 108 (1999)).

number of factors necessary to conclude that an employer-employee relationship exists.<sup>151</sup> The factors analyzed as part of this test are categorized into three groups—behavioral control, financial control, and type of relationship—and include training, integration of workers' services into business operations, services rendered personally, continuing relationship, set hours of work, working on the employer's premises, right to discharge, and right to terminate.<sup>152</sup> Although the IRS test is commonly used to help characterize a worker as an employee, it is met with some skepticism in academic literature for its inefficiency and subjectivity in distinguishing between employees and independent contractors.<sup>153</sup>

Still, the common law/IRS test has been applied to issues associated with the NLRA, which governs labor-management relations and collective bargaining for unionized employers.<sup>154</sup> Further, in *Nationwide Mutual Insurance Co. v. Darden*,<sup>155</sup> the U.S. Supreme Court cited favorably to the IRS's test, ruling that for Federal laws not containing a clear definition of the term employee, the relationship between an employer-employee should be evaluated on the basis of the common law test, focusing specifically on who has the right to control the worker.<sup>156</sup> Summarily, under the common law test, an individual whose work process and product are found to be controlled by the employer will be deemed an employee.<sup>157</sup>

From a federal income tax perspective, the IRS specified in Revenue

---

151. See Rev. Rul. 87-41, 1987-1 CB 296.; see also 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, 601 (2011).

152. See Harned, et al., *supra* note 142, at 103; see also Rev. Rul. 87-41, 1987-1 CB 296 for a full list of all twenty applicable test factors.

153. See Zucco, *supra* note 151, at 609 (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 Harned et al., *supra* note 142, at 103 (analyzing certain negative issues arising from the IRS twenty-factor test, to include burdensome compliance obligations, the subjectivity in interpreting the various factors, and the applicability limitations of this test to federal employment taxes and income tax withholding); 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).

154. Muhl, *supra* note 142, at 5.

155. *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 323-24 (1992).

156. *Id.*; see also Susan Schwochau, Note: *Identifying an Independent Contractor For Tax Purposes: Can Clarity and Fairness Be Achieved?*, 84 IOWA L. REV. 163, 181 n. 112 (1998) (noting the *Darden* Court's favorable application of the IRS's twenty-factor test).

157. Muhl, *supra* note 142, at 6.

Ruling 87-41 that “an individual is an employee for federal employment tax purposes if the individual has the status of an employee under the usual common law rules applicable in determining the employer- employee relationship.”<sup>158</sup> Although some courts have moved away from express reliance on the IRS test, it is noteworthy that Revenue Ruling 87-41 is still the current law and reflects the IRS’s classification of employment status from an income tax perspective.<sup>159</sup>

Although the IRS has itself acknowledged that additional factors may be important in classifying the employment relationship, its potential reliance on the twenty-factor test in the future with regards to student-athletes cannot be discounted.<sup>160</sup> Employing the application of the twenty-factor test in *Darden*, the relationship between student-athletes and the university they play for must focus specifically on who has the right to control.<sup>161</sup> The original NLRB ruling relied on the premise that Northwestern University scholarship football players were employees and were entitled to form a union based on certain factors, which included the extent of time dedicated to their sport, the amount of control exerted by coaches, and the scholarship agreements which paralleled contracts for compensation.<sup>162</sup> Analyzing the right of control that universities have over student-athletes has been heavily scrutinized in academic literature, offering a composite sketch of the magnitude of daily, pervasive control imposed by athletic departments and coaches on student-athletes.<sup>163</sup> Analyzing the enormous control that universities have over some student-

158. Rev. Rul. 87-41, 1987-1 C.B. 296.

159. Robert Wood, *Independent Contractor vs. Employee and Blackwater*, 70 MONT. L. REV. 95, 106 (2009); see also *Avis Rent-a-Car Sys., Inc. v. United States*, 503 F. 2d 423, 428-29 (2d Cir. 1994); *Leb’s Enter. Inc. v. United States*, 2000 WL 139551, 5-6 (N.D. Ill. Jan. 26, 2000).

160. See Wood, *supra* note 159, at 106 (citing to IRS Employment Tax Handbook, I.R.S. Pub. No. 104, at § 5.81 (2007); Independent Contractor or Employee?, I.R.S. Pub. Training Materials No. 3320-102, TPDS 842381 (Oct. 30, 2996)).

161. See *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 323-24 (1992).

162. Strauss & Elder, *supra* note 1.

163. See McCormick & McCormick, *supra* note 112 at 97-119 (examining the 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); see also Vine, *supra* note 144, at 251 (2013) (presenting that University athletic departments exercise an enormous amount of control over scholarship athletes, including attendance at mandatory practices, games, film sessions, and study hall); Nicholas Fram and 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); 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).

athletes suggests an employee-employer relationship exists under the common law/IRS Twenty-Factor Test.<sup>164</sup>

One potential outlier that could be considered should the IRS reevaluate the tax status of student-athletes' scholarship money in the future is the 1983 case, *Rensing v. Indiana State University Board of Trustees*.<sup>165</sup> This case addressed the question of whether an injured student-athlete qualified as a university employee for purposes of workers' compensation benefits.<sup>166</sup> In vacating the Indiana Court of Appeals decision in favor of *Rensing* as an employee under the Indiana statute, the state Supreme Court denied the student-athlete any benefits, finding no evidence of an employer-employee relationship.<sup>167</sup>

Although this case primarily addressed a workers' compensation issue, the Indiana Supreme Court focused in part on the scholarship offer itself, finding that *Rensing's* acceptance of the scholarship did not elevate to the level of an employment contract as neither party considered the scholarship to be either pay or income.<sup>168</sup> Particularly, the court stated that neither "the University, the NCAA, the IRS [or] *Rensing*, himself" considered the scholarship benefits to be income.<sup>169</sup> The court further documented that "*Rensing* did not consider the [scholarship] benefits as income as he did not report them for income tax purposes."<sup>170</sup>

The Indiana Supreme Court concluded that the IRS does not distinguish between athletic and academic scholarships and that scholarship recipients are not taxed on their scholarship proceeds.<sup>171</sup> In essence, if the scholarship proceeds were not considered reportable to the IRS, the Court did not consider it income.<sup>172</sup> However, as the reasoning behind the *Rensing* analysis was specific to the qualification of workers' compensation benefits, such rationale would not suffice in situations where student-athletes are specifically defined as employees by their institution.<sup>173</sup> The *Rensing* court focused on the amateur nature of college

---

164. NLRB v. Northwestern, 2014 NLRB LEXIS 221; Muhl, *supra* note 142, at 5.

165. *Rensing v. Indiana State Univ. Bd. of Trs.*, 444 N.E.2d 1170 (Ind. 1983).

166. *Rensing*, 444 N.E.2d at 1170-71.

167. IND. CODE ANN. § 22-3-1-1 et seq. (Burns, through the 2015 First Regular Session of the 119th General Assembly, P.L. 1-2591974); *see also Rensing*, 444 N.E.2d at 1171, 1175.

168. Stephen L. Ukeiley, *No Salary, No Union, No Collective Bargaining: Scholarship Athletes Are An Employer's Dream Come True*, 6 SETON HALL J. SPORTS L. 167, 188 (1996); *see also Rensing*, at 1174.

169. *Rensing*, 444 N.E.2d at 1174.

170. *Id.* at 1173.

171. *Id.* *See also* Rev. Rul. 77-263, 1977-31 I.R.B.

172. Ukeiley, *supra* note 168, at 188.

173. *See* Goplerud, *supra* note 136, at 1099 (opining, similarly, that the *Rensing* analysis would not be available to a court reviewing the issue of whether a stipend paid to student-athletes would

sports in conjunction with the NCAA's prohibition on paying student-athletes.<sup>174</sup> If universities were to officially label select student-athletes as employees and subsequently offer scholarships or stipends to cover their tuition, fees, room, board, and books in exchange for participating on the sports field, such payments would begin to look more like a professional sports contractual relationship.<sup>175</sup>

As the *Rensing* Court focused on the amateurism perspective of college athletics in concluding that an employment contractual agreement did not create a contract-for-hire, it would not likely be heavily relied upon in determining whether student-athletes' scholarship funds are taxable should they be officially deemed employees of their institutions in the future.<sup>176</sup> However, the decision is intriguing for its demonstration of how the perception of amateurism in college athletics sways the legal determination of the relationship between student-athletes to their universities.<sup>177</sup>

## 2. The Economic Realities Test

An alternative test used to characterize a worker as an employee is the economic realities test. This test, which is generally applied in the context of the FLSA governing minimum-wage and overtime obligations, specifically targets the economic relationship between the worker and the employer.<sup>178</sup> Specifically, an individual is defined as an employee if they are economically dependent on the employer for continued employment, regardless of how the employer chooses to label them.<sup>179</sup> This test is generally satisfied "where a worker performs tasks integral to the employer's regular business, and does not provide an independent business or service vis-à-vis the employer."<sup>180</sup>

Under the purview of the economic realities test, the nature of the relationship between worker and employer is examined "in light of the fact that independent contractors would typically not rely on a sole

---

constitute a wage paid for services as a stipend provision within scholarships would likely fall within the existing definition of "employee").

174. *Id.*, citing *Rensing*, 444 N.E.2d at 1173.

175. *Id.*

176. *See* Davis, *supra* note 135, at 290-91.

177. *Id.* at 293 (documenting the significance of the *Rensing*, *Coleman*, *Van Horn*, and *Nemeth* court decisions within the legal analyses of relationships between athletes and their universities).

178. Muhl, *supra* note 142, at 6-9.

179. *Id.*; *see also* Lewis L. Maltby & David C. Yamada, *Beyond "Economic Realities": The Case for Amending Federal Employment Discrimination Laws to Include Independent Contractors*, 38 B.C. L. REV. 239, 240 (1997).

180. Davis, *supra* note 135, at 287 (citing LARSON, *supra* note 150, at § 45.00, at 8-193).



employer for continued employment at any one time, but would work for, and be compensated by, many different employers, whereas most employees hold a single job and rely on that one employer for continued employment and for their primary source of income.”<sup>181</sup> It is the easiest test for a plaintiff to satisfy in construing a person as an employee because of its broad application of the term employee.<sup>182</sup> Factors used to determine a worker’s status under the economic realities test are: (1) whether the worker’s services are integral to the employer’s business, (2) the worker’s investment in the facilities and equipment, (3) the management’s right to control, (4) the worker’s opportunity for profit or loss, (5) the skill and initiative required in performing the job, and (6) the permanency of the relationship.<sup>183</sup>

Although there are similarities between the economic realities test and common law test, the economic realities test ultimately focuses on whether the economic reality is that a worker “depends on someone else’s business” for continued employment.<sup>184</sup> Specifically, the function of this test aims to analyze the dependent nature of the worker to determine whether the worker can operate without the employer.<sup>185</sup> If an individual “operates an independent business basis, the worker is classified as an independent contractor under the economic realities test.”<sup>186</sup>

The economic realities test was utilized by a Michigan state court when analyzing the existence of any employer-employee relationship between a university and scholarship athlete in *Coleman v. Western Michigan University*.<sup>187</sup> However, the test was applied to ascertain whether a scholarship athlete was entitled to workers’ compensation following a debilitating injury, which barred him from playing football.<sup>188</sup> At no juncture during its review of this case did the Michigan Court of Appeals reference the application of the economic realities test (or any other test) to the taxability of the injured player’s scholarship money.<sup>189</sup> Specifically, the court applied the economic realities test solely to inquire into the existence of an employment contract between the university and

---

181. Muhl, *supra* note 142, at 7.

182. Nicola Kean, *The Unprotected Workforce: Why Title VII Must Apply to Workfare Participants*, 9 TEX. J. C.L. & C.R. 159, 189 (2004).

183. Muhl, *supra* note 142, at 8.

184. *Id.* at 9; *see also* Margot Rutman, *Symposium: Exotic Dancers’ Employment Law Regulations*, 8 TEMP. POL. & CIV. RTS. L. REV. 515, 538-39 (1999).

185. Rutman, *supra* note 184, at 539.

186. Muhl, *supra* note 142, at 9.

187. *See, e.g., Coleman v. Western Michigan Univ.*, 336 N.W.2d 224 (Mich. Ct. App. 1983).

188. *Id.*

189. *See Coleman*, 336 N.W.2d 224.

the student-athlete.<sup>190</sup>

Similarly, in the 1984 case *Cheatham v. Workers' Compensation Appeals Board*, a California court held that student-athletes are not employees of their universities, noting an "absence of any fair inference of economic benefit" to the university from its wrestling program.<sup>191</sup> In this case, a scholarship recipient student-athlete was injured during a wrestling scrimmage and subsequently sought to recoup workers' compensation.<sup>192</sup> Comparable to the *Coleman* decision, the *Cheatham* court opined only on the question of whether petitioner was an employee within the meaning of the California labor standards, not tax law.<sup>193</sup>

Because the IRS utilizes its own twenty-factor test to determine whether a worker is an employee under common law principles from a federal income tax perspective, and as the economic realities test has been relied on in analyzing employment characterization specifically from a labor standards viewpoint, the economic realities test would not likely be the tool utilized exclusively to analyze the taxability of student-athletes' scholarship money in the future.<sup>194</sup> However, student-athlete scholarship funds would arguably qualify as taxable income under the economic realities test.

### 3. The Hybrid Test

Although a middle ground test that combines elements of both the common law and economic realities test, the hybrid test was adopted specifically for the purpose of determining employee status under federal discrimination statutes. The hybrid test is a combination of elements of the common law and economic realities tests.<sup>195</sup> The economic realities of the working relationship is a crucial factor under the hybrid test, but the employer's right to control the work process is the determinative factor.<sup>196</sup>

While the NLRA has generally applied the common law right to control test when scrutinizing the employment classification of a worker, courts resolving cases involving the Americans with Disabilities Act (ADA) tend to apply the economic realities test, while the wider judicial trend is to apply the hybrid test to cases involving Title VII of the Civil

---

190. *Id.* at 225; see also Craig D. Alfred, Comment: *The Illusion of Amateurism: A Climate of Tortious Interference in the World of Amateur Sports*, 86 TUL. L. REV. 465, 483 (2011).

191. *Cheatham v. Workers' Compensation Appeals Board*, 49 Cal. Comp. Cases 54, 61 (1984).

192. *Id.* at 54.

193. *Id.*

194. See Zucco, *supra* note 151, at 601.

195. Muhl, *supra* note 142, at 9.

196. *Id.*

Rights Act of 1964 and the Age Discrimination in Employment Act (ADEA).<sup>197</sup> However, many courts have also rejected the adoption of the hybrid test in light of the U.S. Supreme Court's 1992 decision in *Darden*, indicating that the common law standard was the appropriate test to use where a statute fails to specifically define the term employee.<sup>198</sup>

The U.S. Supreme Court's decision in *Darden* focused only on defining an "employee" under ERISA, allowing federal and state courts to continue to apply the hybrid test in other areas of the law.<sup>199</sup> The combined common law/economic realities test components considered in applying the hybrid test include supervision, skill level, method of payment, supplier of tools and materials, duration of employment relationship, and integration of work into the employer's business.<sup>200</sup> Other factors further examined under this test include the manner in which the work relationship is terminated, whether annual leave and/or retirement benefits are provided, and whether the employer paid Social Security taxes for the worker.<sup>201</sup>

Although a middle ground test that combines elements of both the common law and economic realities test, the hybrid test was adopted specifically for the purpose of determining employee status under federal discrimination statutes.<sup>202</sup> Although federal and state courts have applied the hybrid test, the application of this test in evaluating the employment status of a student-athlete from a federal income tax perspective is not likely given both the *Darden* holding as well as the overriding reality that the IRS could choose to apply its own twenty-factor test.<sup>203</sup>

Following an analysis of the various tests that may be reviewed in determining whether workers are defined as employees from a federal tax perspective, the next query is specifically analyzing how paid student-athletes would be characterized for federal income tax purposes. As the proper characterization of paid student-athletes is imperative to

---

197. Cliff E. Spencer, Comment, *Oregon's Independent Contractor Statute: A Legislative Placebo for Employers*, 31 WILLAMETTE L. REV. 647, 673 (1995).

198. See *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318; see also Mitchell H. Rubinstein, *Employees, Employers, and Quasi-Employers: An Analysis of Employees and Employers Who Operate in the Borderland Between an Employer-And-Employee Relationship*, 14 U. PA. J. BUS. L. 605, 627 (2012) (referencing *Deal v. State Farm Mut. Ins.*, 5 F.3d 117, 118-19 (5th Cir. 1993), *Magallanes v. Penske Logistics LLC*, 570 F. Supp. 2d 907, 912 (W.D. Tex. 2008), *Hopkins v. Cornerstone Am*, 545 F.3d 338, 347 (5th Cir. 2008)).

199. Rubinstein, *supra* note 198, at 627.

200. *Id.*

201. Muhl, *supra* note 142, at 10; see also *Diggs v. Harris Hospital-Methodist, Inc.*, 847 F.2d 270, 272-73 (9th Cir. 1988).

202. Harned, et.al., *supra* note 142, at 101.

203. *Id.*; see also *Darden*, 503 U.S. 318.

understanding the overall federal tax implications, which certain college athletes could face in the future, the following analysis ensues.

*B. Characterizing Student-Athletes as Employees for Federal Income Tax Purposes*

The proper characterization of a worker as an employee or independent contractor within a working, business relationship is vitally important to both the employers and workers in terms of their mutual obligations and protection under federal law.<sup>204</sup> When employment status is blurred, employment rights and obligations are likewise uncertain.<sup>205</sup> Uncertainty breeds litigation.<sup>206</sup> Although such classification depends on the application of federal law, the overriding factor in every test analyzed previously is who has the right to control the work process, not the label affixed by the employer.<sup>207</sup>

Recent literature querying whether student-athletes should be characterized as employees under the right to control test suggests there is a sufficient basis to demonstrate that an employer- employee relationship already exists.<sup>208</sup> Specifically, scholars have critically explored the question of whether student-athletes are exploited by the universities they play for and have challenged that student-athletes are in fact employees given that academics has taken a back seat to the true purpose of university agendas—to increase revenue and furnish to their programs greater exposure.<sup>209</sup>

---

204. Muhl, *supra* note 142, at 10.

205. See Rubinstein, *supra* note 198, at 609.

206. *Id.*

207. See Muhl, *supra* note 142, at 10.

208. See Vine, *supra* note 144, at 266 (providing a comprehensive discussion and analysis of major NCAA-related decisions involving the issue of whether student-athletes should be characterized as student-athletes, analyzing the tests used by the IRS and courts to determine the nature of an employment relationship, and concluding that, “NCAA scholarship athletes are employees of their respective university. They are employees under common law. They are employees under federal law. Now, more than ever, it is time to put an end to the idea that recipients of an athletic scholarship are not employees of the university. Equity demands Courts to deem scholarship athletes employees.”); see also Jason Gurdus, *Protection Off of the Playing Field: Student Athletes Should be Considered University Employees for Purposes of Workers’ Compensation*, 29 HOFSTRA L. REV. 907, 909-12 (2001) (applying the various control tests to conclude that student-athletes are arguably employees of the institutions they play for); McCormick & McCormick, *supra* note 112, at 82, 130-55 (asserting that the relationship between a university and student-athletes primarily commercial, not academic, in nature and that an objective judiciary must recognize the employee status of student-athletes).

209. Vine *supra* note 144, at 266 (“allowing their academics to play second fiddle”); see also Gurdus, *supra* note 208, at 929 (stating that student-athletes are employees of their university and “[t]he amount of proof available to show that an employment relationship exists between student

In evaluating the characterization of student-athletes as unpaid amateurs versus professional employees, the argument can be made that college sports have not been strictly amateur for countless years, if ever.<sup>210</sup> Specifically, a literary analysis of the extent of control exerted by coaches over Division I-A football players both on and off the field, during the athletic season and extending into the remainder of the academic year, concluded that the common law right to control test is already being met.<sup>211</sup>

Drawing on data derived from personal interviews with Division I-A football players, research establishes that coaches exert an inordinate amount of control over college football players not only during the regular season, but extending into the off-season as well.<sup>212</sup> Collegiate coaches control student-athletes' playing time, competitive eligibility, and access to training resources.<sup>213</sup> Arguably, student-athletes are subject to greater control by their universities than are any other employees or group of employees already being financially compensated for working at such institutions.<sup>214</sup>

The concept that student-athletes should remain unpaid amateurs has been further criticized as universities' outward control over their student-athletes has increased in the media.<sup>215</sup> Particularly, an examination of the degree of control that universities have over student-athletes' names, images, and likenesses has in recent years transformed from literary

---

athletes and colleges is substantial").

210. See McCormick & McCormick, *supra* note 112, at 75.

211. *Id.* at 98. Today, the NCAA refers to Division I-A football as the Football Bowl Subdivision (FBS) whereas Division I-AA is the Football Championship Subdivision (FCS).

212. *Id.* at 98-105 (noting that coaches' exercise of control of 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 which 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. Other demands on student-athletes include attendance at post-season bowl games, recruitment pressures and mandatory random drug testing.).

213. Susan L. Smith & Miriam Schuchman, *Sickle Cell Screening of College Athletes: Legal Obligations Fulfilled, Moral Obligations Lacking*, 92 OR. L. REV. 1127, 1141 (2014).

214. McCormick & McCormick, *supra* note 112, at 97.

215. See W. Burlette Carter, *Responding to the Perversion of In Loco Parentis: Using a Nonprofit Organization to Support Student-Athletes*, 35 IND. L. REV. 851, 923 (2001) (stating, "It is possible to argue that, in the name of keeping intercollegiate athletics an integral part of education, institutions should be permitted to exercise broader controls over student-athletes than over non-athletes. Evidence suggests that without some controls intercollegiate athletics can get out of hand.").

discussion<sup>216</sup> to judicial litigation involving the NCAA.<sup>217</sup> As previously discussed, legal attacks against the NCAA have recently pivoted on whether student-athletes' likenesses are unlawfully being used in commercial video games and, therefore, whether certain student-athletes should be compensated.<sup>218</sup> Such scrutiny surrounding the classification of the relationships among student-athletes, the institutions they play for, and the NCAA is indicative of the continued momentum to characterize student-athletes as employees under the law.<sup>219</sup>

During his trial against the NCAA, Ed O'Bannon specifically testified that his role at UCLA was to play basketball and that making it to class was difficult due to the amount of time he spent training.<sup>220</sup> O'Bannon stated, "I was an athlete masquerading as a student . . . I was there strictly to play basketball."<sup>221</sup> Others who testified at the *O'Bannon* trial stated that they viewed playing sports in college as their occupation, noting that it is difficult, or even impossible, for student-athletes to function like normal students due to the amount of time they are required to devote to their sport.<sup>222</sup>

Student-athletes, in return for universities' promises of free higher education, the opportunity to earn a seat in the spotlight, and the potential

---

216. See, e.g., Kristal S. Stippich & Kadence A. Otto, *Carrying a Good Joke Too Far? An Analysis of the Enforceability of Student-Athlete Consent to Use of Name & Likeness*, 20 J. LEGAL ASPECTS OF SPORT 151, 180 (2010) (discussing the Ed O'Bannon lawsuit in light of name, image and likeness litigation and offering that "the definition of "amateur" will ultimately need to be resolved."); see also Spencer H. Larche, *Pink-Shirting: Should the NCAA Consider a Maternity and Paternity Waiver?*, 18 MARQ. SPORTS L. REV. 393, 401-02 (2008) (presenting both sides of the argument over whether student-athletes should be employees and noting that courts generally have not regarded student-athletes as employees and offering that educational institutions do not have "significant right of control" over their activities and cannot fire them, per se. Larche also offers that some individuals believe otherwise and that athletics departments do, in fact, exercise a significant degree of control over their time on campus including, "what classes to take, when to study, and when and what to eat, in addition to the traditionally known demands placed upon student-athletes by practice schedules and games.").

217. See Lee Romney, *Judge Rules against NCAA in Ed O'Bannon Antitrust Lawsuit*, LA TIMES (Aug. 8, 2014), <http://www.latimes.com/local/lanow/la-me-ln-ncaa-obannon-ruling-20140808-story.html> (discussing the decision by U.S. District Court Judge Claudia Wilken, which held that the NCAA's policies that prohibit student-athletes from profiting from their own names, images, and likenesses "unreasonably restrain trade").

218. See Wolohan, *supra* note 32.

219. *Id.*; see also Chris Dufresne, *Ed O'Bannon Ruling is not the Real Game-changer for the NCAA*, LA TIMES (Aug. 11, 2014), <http://www.latimes.com/sports/sportsnow/la-sp-sn-ncaa-game-changer-20140811-story.html> (quoting Southeastern Conference Commissioner Mike Slive who states that colleges are "going through a historic evolution" in light of the *O'Bannon* decision).

220. 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/>.

221. *Id.*

222. *Id.*

for future opportunities in the professional world of sports, “give their blood, sweat, tears, and their lives for the success of their team and the school’s reputation.”<sup>223</sup> College athletics is more than mere friendly competition among schools—but a huge revenue and reputation-garnering business venture.<sup>224</sup>

Although the NCAA continues to defend its preservation of amateurism in college sports amidst past arguments that student-athletes are employees of their institutions and are controlled by the coaching staff, the IRS has thus far refused to characterize student-athletes as employees from an income tax perspective.<sup>225</sup> However, in conjunction with growing arguments that universities overtly control student-athletes, specifically identifying student-athletes as employees of the institutions they play for may require the IRS to eventually reevaluate its stance on taxing student-athletes’ scholarship income.

On April 19, 2014, the IRS drafted a public letter to the Honorable Richard Burr, North Carolina U.S. Senator, confirming the current federal tax treatment of college athletic scholarships.<sup>226</sup> Within this letter, the IRS noted that “whether an individual is treated as an employee for labor law purposes is not controlling of whether the individual is an employee for federal tax purposes.”<sup>227</sup> The letter further documented: “It has long been the position of the IRS that athletic scholarships can qualify for exclusion from income under section 117.”<sup>228</sup> Revenue Ruling 77-264, 1977 1 C.B. 47, addresses the tax treatment of athletic scholarships where the student-athlete is expected to participate in the sport and where the scholarship is not cancelled in the event the student is not required to engage in any other activities in lieu of participating in the sport.<sup>229</sup> The ruling holds that the athletic scholarship awarded by the university is primarily to aid the

---

223. Roy A. Helmat, *Malpractice During Practice: Should NCAA Coaches Be Liable For Negligence?*, 22 LOY. L.A. ENT. L. REV. 613, 635 (2002).

224. See Gurdus, *supra* note 208, at 929 (2001).

225. See Marc Edelman, *The District Court Decision in O’Bannon v. National Collegiate Athletic Association: A Small Step Forward for College-Athlete Rights, and a Gateway for Far Grander Change*, 71 WASH. & LEE L. REV. 2319, 2342 (2014) (discussing the NCAA’s current stance on amateurism); see also NCAA Manual 2.9 (stating that “student-athletes shall be amateurs in an intercollegiate sport, and their participation should be motivated primarily by education and by the physical, mental and social benefits to be derived. Student participation in intercollegiate athletics is an avocation, and student-athletes should be protected from exploitation by professional and commercial enterprises.”).

226. See Department of the Treasury, Internal Revenue Service, CONEX 113035-14, No. 2014-0016, (Apr. 19, 2014), <http://www.irs.gov/pub/irs-wd/14-0016.pdf> (last visited Feb. 22, 2015).

227. *Id.*

228. *Id.*

229. Rev. Rul. 77-264, 1977 1 C.B. 47.

recipients in pursuing their studies and, therefore, is excludable under Section 117.<sup>230</sup>

Regardless of this public assurance, future contractual agreements between student-athletes and their universities that involve “additional cash and a share of royalties could cause the IRS to conclude that an athletic scholarship is part of a larger compensation package,” thereby making the entire package taxable.<sup>231</sup> If certain student-athletes are represented by a union, the result may ensue that qualified scholarships become part of the overall negotiated term of the contractual agreement.<sup>232</sup> Once a labor union is involved with negotiating the qualified scholarships for student-athletes, it is more likely that the scholarship money will become taxable income.

The *O’Bannon* decision referred to student-athletes’ share of revenue from the use of their names and likenesses as compensation.<sup>233</sup> The federal reporting of such compensation would undoubtedly be considered taxable income.<sup>234</sup> Similarly, student-athletes’ share of licensing revenue would arguably be treated as taxable income by the IRS regardless of the fact that such funds may be deposited into trusts.<sup>235</sup> Therefore, the current NCAA notion that scholarship athletes are truly students first and athletes second—rather than paid employees of their institutions—could be heavily scrutinized in the future.<sup>236</sup>

The landmark case in this area which signifies that athletic scholarships could be taxable if student-athletes are treated as employees falls to *Bingler*.<sup>237</sup> As discussed previously, the U.S. Supreme Court impressed the significance of the quid pro quo test, preserving the notion that students who provide services in exchange for scholarships or grants may not exclude their awards from gross income.<sup>238</sup> Therefore, amounts

---

230. See Department of the Treasury, Internal Revenue Service, CONEX 113035-14, No. 2014-0016, *supra* note 226.

231. See *Game On! Recent Legal Developments and Tax Issues for Collegiate Athletics*, ROPES & GRAY (Sept. 15, 2014), <http://www.ropesgray.com/news-and-insights/Insights/2014/September/Game-On-Recent-Legal-Developments-and-Tax-Issues-for-Collegiate-Athletics.aspx>.

232. *Id.*

233. Jackie Perlman & Alison Flores, *Students, Athletes—and Taxpayers? A Recent Court Decision may have Major Repercussions for Colleges’ Star Players*, ACCOUNTING TODAY (Dec. 2, 2014), <http://www.accountingtoday.com/taxprotoday/news/students-athletes-226128-and-taxpayers72898-1.html>.

234. *Id.*

235. *Id.* (further noting that although student-athletes may not have immediate access to trust funds while they are in attendance at school, the athletes would likely be taxed when the compensation is paid to the trust).

236. *Id.*

237. *Bingler v. Johnson*, 394 U.S. 741 (1969).

238. See *id.* at 751 (The Court noted, “Here, the definitions supplied by the Regulation clearly



received in return for services rendered are treated as compensation rather than scholarship funds.<sup>239</sup>

The *Bingler* decision exposes student-athletes to the possibility that scholarship funds may inevitably be taxable given the totality of contractual opportunities that could become part of student-athletes' negotiable package deals in the future.<sup>240</sup> Distinguishing scholarship funds from stipends or compensation, which schools may begin to offer select student-athletes, along with potential licensing revenues, could create blurred lines when applying the *Bingler* quid pro quo test.<sup>241</sup> Ultimately, the decision of how to treat student-athletes' scholarship funds would likely come down to an IRS pronouncement or federal judicial determination. For student-athletes, the tax code leaves no room for interpretation—any form of compensation received in exchange for playing sports will invalidate the tax-exempt nature of their scholarship funds.<sup>242</sup>

## V. CONCLUSION

The NLRB's 2014 ruling that Northwestern University's scholarship football players were employees of the institution under the NLRA and could unionize and bargain collectively, though subsequently unanimously overturned, temporarily threatened the NCAA's deep-seeded principle of amateurism in college sports.<sup>243</sup> Under the strong tradition of amateurism, student-athletes may only receive athletic scholarships to help pay for their higher education, while simultaneously engaging in competitive athletics for their respective universities.<sup>244</sup> Amateurism requires that student-athletes who are, or have been, paid to

---

are prima facie proper, comporting as they do with the ordinary understanding of 'scholarships' and 'fellowships' as relatively disinterested, 'no strings' educational grants, with no requirements of any substantial quid pro quo from the recipients."); see also Hoeflich, *supra* note 80, at 591 (noting the significance of the *Bingler* court upholding the quid pro quo test).

239. See Prop. Treas. Reg. § 1.117-6(d)(2), 53 Fed. Reg. 21688 (Jun. 9, 1988); see also Larkins, *supra* note 96, at 70.

240. See Ken Berry, *College Athletes Could Be Sacked with High Taxes on Scholarships*, CPA PRACTICE ADVISOR (Apr. 13, 2014), <http://www.cpapracticeadvisor.com/news/11393197/college-athletes-could-be-sacked-with-high-taxes-on-scholarships>.

241. *Id.* (citing Dee DeScherer, a NJ-based tax publisher, who notes that while the *Bingler* decision exposes student-athletes to the threat of tax liability, such exposure to federal taxation is not a certainty).

242. See AndersenTax, *Student-Athlete/Athlete-Employee: Tax Consequences, for Sure*, FOR THE RECORD (Sept. 2014), <http://www.andersentax.com/publications/newsletter/september-2014/student-athlete-athlete-employee-tax-consequences-for-sure>.

243. See *supra* note 1 and accompanying text.

244. *Id.*

play are ineligible to compete in collegiate varsity athletic sports.<sup>245</sup>

A secondary impact entails the potential tax consequences facing student-athletes should they be deemed employees of their institutions someday.<sup>246</sup> To date, student-athletes receiving qualified scholarships have not been taxed on scholarship money received.<sup>247</sup> However, if student-athletes are eventually characterized as employees of the institutions they play for, it is viable that the IRS may reconsider whether certain student-athletes are receiving part or all of their scholarship money in exchange for services rendered.

The language of the IRC entails that a student may not exclude amounts received from gross income if their institution requires services in exchange for a grant or stipend.<sup>248</sup> Further, the U.S. Supreme Court in *Bingler* noted the importance of applying the quid pro quo test, finding that students who provide services in exchange for scholarships may not exclude their awards from gross income.<sup>249</sup> Should the IRS eventually reevaluate its stance on the taxability of student-athletes' scholarship funds, it would likely utilize its own twenty-factor common law test to determine the proper characterization of student-athletes from a federal income tax perspective.<sup>250</sup>

The ultimate query hinges on whether the IRS will proactively elect to reexamine the taxability of student-athletes' scholarship money in the future. Given that the IRS recently published a letter confirming the federal tax treatment of athletic scholarships as it has been employed historically, it could be argued that student-athletes' scholarship money is safe from the threat of federal taxation.<sup>251</sup> However, given the fact that future contracts between student-athletes and their institutions may involve additional cash or royalties and that student-athletes may now earn a share of revenue from the use of their names and likenesses, the IRS may be hard pressed to evaluate whether athletic scholarships are part of a greater overall compensation package which is subject to taxation.<sup>252</sup> Alternatively, it could be argued that at least a portion of the money paid to certain student-athletes should be included in gross income.

Finally, the ultimate determination of the taxability of athletic scholarships will likely hinge on the application of the *Bingler* quid pro

---

245. See *supra* notes 2-4 and accompanying text.

246. See *supra* notes 9-10 and accompanying text.

247. See *supra* note 114 and accompanying text.

248. IRC § 117(c) (LEXIS 2015).

249. See *Bingler v. Johnson*, 394 U.S. 741, 751 (1969).

250. See *supra* notes 145-155 and accompanying text.

251. See *supra* notes 228-232 and accompanying text.

252. See *supra* notes 233-238 and accompanying text.

quo test.<sup>253</sup> This U.S. Supreme Court decision exposes student-athletes to the possibility that grants-in-aid may eventually be taxable based on the overall contractual opportunities that may become part of their negotiable package deals.<sup>254</sup> For scholarship or grant recipients, to include student-athletes, any form of compensation received in exchange for services rendered will invalidate the tax-exempt nature of scholarship funds.<sup>255</sup>

From a federal tax perspective the historical significance of the NLRB's 2014 *Northwestern* case as an archetype for student-athletes seeking mobilized unionization, combined with decision in the *O'Bannon* case, might one day redefine the notion that student-athletes are not mere amateurs receiving qualified scholarships but instead are employees of their institutions earning funds in exchange for services rendered on the playing field.<sup>256</sup> Intrinsically, the IRS may have to reevaluate whether qualified scholarships received by student-athletes are excludable from gross income in the future. Defining student-athletes as employees of their universities may likely cultivate a new era in taxing qualified scholarships.

---

253. See *supra* notes 88-98 and 239-243 and accompanying text.

254. See *supra* notes 233-243 and accompanying text.

255. See *supra* notes 78-82 and accompanying text.

256. See *supra* notes 15-18 and accompanying text.