
**UNSPORTSMANLIKE CONDUCT: WHY THE NCAA
SHOULD LOSE ITS TAX-EXEMPT STATUS IF
SCHOLARSHIP ATHLETES ARE CONSIDERED
EMPLOYEES OF THEIR UNIVERSITIES**

Eric Carlson[†]

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[†] J.D. Candidate, Syracuse University College of Law, 2016, M.A. International Relations Candidate, Maxwell School of Citizenship and Public Affairs, 2016. I would like to thank Professor Rob Nassau for his guidance and advice on this note and for cultivating my interest in tax law. I would also like to thank my parents, Tom and Patty, for always loving and encouraging me in everything I do.

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INTRODUCTION

The March 2014 regional National Labor Relations Board (NLRB) decision in *Northwestern University* presented a fresh challenge to the National Collegiate Athletic Association's (NCAA) tax-exempt status.¹ In holding that scholarship Division I football players are compensated employees of Northwestern University, the regional NLRB put the NCAA's tax-exempt status in doubt.²

Under § 501(c)(3), the NCAA is tax-exempt because it is “organized and operated exclusively . . . to foster . . . amateur sports competition.”³ The key term is “amateur.” According to the NCAA's own bylaws, the hallmark of an amateur athlete is being uncompensated.⁴ If scholarship Division I football players are *compensated* employees then by the NCAA's own definition, they are not amateurs.⁵ While the national NLRB dismissed the Northwestern players' petition to unionize, it refused to say whether or not they are employees, leaving the legal question unsettled and ripe for new and further litigation.⁶

This Note argues that should the rationale in the March 2014 NLRB decision be followed in a future decision and be extended to other scholarship athletes in other sports, the NCAA should lose its tax-exempt status. Alternatively, this note argues that if *only* Division I scholarship football players are employees, then the NCAA's football-related revenue should be subject to the unrelated business income tax, while the remaining non-Division I football revenues would remain tax-exempt.

Section I of this Note discusses the history and modern application of tax-exemption for nonprofit charitable organizations, with a focus on

1. See generally (*Nw. Univ. I*), No. 13-RC-121359, 198 L.R.R.M. (BNA) 1837 (N.L.R.B. Region 13 Mar. 26, 2014).

2. *Id.* at 1840.

3. 26 U.S.C. § 501(c)(3) (2012).

4. NAT'L COLLEGIATE ATHLETIC ASS'N, 2013–14 NCAA DIVISION I MANUAL § 12.1.2(a), (d) (2013).

5. See *Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1840.

6. *Nw. Univ. (Nw. Univ. II)*, 362 N.L.R.B. No. 167, 204 L.R.R.M. (BNA) 1001, 1007 (Aug. 17, 2015).

§ 501(c)(3), the provision under which the NCAA is tax exempt.⁷ Section I also explains why the NCAA is tax-exempt under § 501(c)(3) and how past challenges to its tax-exempt status have failed.

Section II discusses the unrelated business income tax and how it is linked to tax-exempt § 501(c)(3) organizations. Section II then analyzes the NCAA and university athletic departments under the unrelated business income tax and why before the March 2014 decision, it would not apply.

Section III explores the concept of amateurism in college athletics. As mentioned previously, the NCAA needs its athletes to be amateurs in order to qualify for tax-exempt status. If its athletes are not amateurs, it must lose its tax-exempt status. Section III discusses amateurism as defined by NCAA bylaws, and how the Internal Revenue Code (IRC) would define amateur within the context of § 501(c)(3).

Section IV discusses the regional and national NLRB decisions in *Northwestern University*.⁸ For the purposes of this note, the key holding in the March 2014 *Northwestern* decision was that scholarship Division I football players are compensated employees of Northwestern University.⁹ The national NLRB in August 2015 opted not to address the question of whether the scholarship players were employees, leaving the matter unsettled.¹⁰ As such, Section IV considers the potential for future litigation on whether scholarship athletes are employees, and the precedential ramifications of such a decision.

Finally, Section V argues that the NCAA should lose its tax-exempt status if scholarship athletes are employees, because it no longer qualifies for § 501(c)(3) status. Section V also argues that it is not feasible for the NCAA to eliminate the athletic scholarship system merely to maintain tax-exempt status. Alternatively, Section V argues that if only Division I scholarship football players are employees, and not all scholarship players in all sports, at a minimum the NCAA's Division I football-related revenue should be subject to the unrelated business income tax. Section V concludes by discussing the practical realities of a non-tax-exempt NCAA.

7. 26 U.S.C. § 501(c)(3).

8. See generally *Nw. Univ. II*, 362 N.L.R.B. No. 167, 204 L.R.R.M. (BNA) 1001; *Nw. Univ. I*, 198 L.R.R.M. (BNA) 1837.

9. *Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1840.

10. *Nw. Univ. II*, 362 N.L.R.B. No. 167, 204 L.R.R.M. (BNA) at 1007.

I. TAX EXEMPTION AND THE NCAA

The March 2014 and August 2015 NLRB decisions in the *Northwestern* case created more questions than answers, particularly regarding the NCAA's tax-exempt status.¹¹ However, before one can understand how the NLRB decisions, or similar future decisions could affect the NCAA's tax-exempt status, it is important to understand why the NCAA exists, why it is tax-exempt, and how its tax exemption operates.

A. Tax-Exempt Organizations Under § 501(c)(3)

Section 501 of the Internal Revenue Code provides an “[e]xemption from tax on corporations, certain trusts, etc.”¹² Further, § 501(a) exempts from taxation, an organization described under subsection (c), provided such exemption is not denied under §§ 502 or 503.¹³ The NCAA is currently a tax-exempt organization described under § 501(c)(3) of the IRC.¹⁴ Section 501(c)(3) provides an exemption from corporate income tax for certain types of nonprofit organizations, including entities “organized and operated exclusively . . . to foster national or international amateur sports competition.”¹⁵ Section 501(c)(3) also qualifies religious, charitable, scientific, and educational organizations as tax-exempt.¹⁶

1. Tax Exemption: A History

Section 501(c)(3) was first established by the Revenue Act of 1954.¹⁷ However, the concept of nonprofit organizations is as old as the United States itself.¹⁸ In the United States' early days, there was no broad government social safety net, but instead charitable or voluntary associations created by private individuals.¹⁹ These voluntary associations were either public-serving or member-serving.²⁰ Public-serving associations, as the name implies, included schools, churches,

11. *Id.* at 1001; *Nw. Univ. I*, 198 L.R.R.M. (BNA) 1837.

12. 26 U.S.C. § 501 (2012).

13. *Id.* § 501(a).

14. John D. Colombo, *The NCAA, Tax Exemption, and College Athletics*, 2010 U. ILL. L. REV. 109, 113 (2010).

15. 26 U.S.C. § 501(c)(3).

16. *Id.*

17. Paul Arnsberger et al., *A History of the Tax-Exempt Sector: An SOI Perspective*, 27 SOI BULL. 105, 106 (Winter 2008).

18. *Id.* at 105.

19. *Id.*

20. *Id.*

and other groups designed to provide services to the population at large.²¹ Member-serving associations, such as fraternal orders, sought to benefit their members and promote their interests.²²

The earliest statutory reference to the tax exemption of charitable or voluntary associations was in the Wilson-Gorman Tariff Act of 1894.²³ The act created a requirement that tax-exempt charitable organizations must operate for charitable purposes.²⁴ Over the next seventy-five years, Congress adopted and refined the modern federal income tax system.²⁵ With regard to tax-exempt charitable organizations, Congress enacted the Revenue Act of 1909, which used similar language to the Wilson-Gorman Act, adding the rule that no portion of a charitable organization's net income may inure to the benefit of any private stockholder or individual.²⁶

Despite the presence of tax-exemptions, until 1913, Congress did not have the power to levy income taxes uniformly across all states.²⁷ Under the Constitution, all "direct [t]axes" must be apportioned to each state based on its population.²⁸ A direct tax is a tax paid by a taxpayer directly to the government.²⁹ These taxes cannot be shifted to another person or entity.³⁰ On the other hand, an indirect tax is a tax which can be shifted to another person or entity.³¹ An example is a business raising the price of its goods or services to pass the cost of the tax onto its customers.³²

Congress first attempted to levy a uniform income tax via an amendment to the Wilson-Gorman Tariff Act of 1894.³³ However, one year later, the Supreme Court held, in *Pollock v. Farmers' Loan & Trust Co.*, the income tax was unconstitutional because it was a direct tax that

21. *Id.*

22. Arnsberger et al., *supra* note 17, at 105.

23. *Id.* at 106 (citing Wilson-Gorman Tariff Act, ch. 349, 28 Stat. 509 (1894), *income tax provision declared unconstitutional by Pollock v. Farmers' Loan & Tr. Co.*, 157 U.S. 429 (1895), *remainder superseded by Dingley Act*, ch. 11, 30 Stat. 151 (1897)).

24. *Id.*

25. *Id.* at 106–07.

26. *Id.* at 107 (citing Payne-Aldrich Tariff of 1909, ch. 6, § 38, 36 Stat. 11, 112 (1909)).

27. Arnsberger et al., *supra* note 17, at 107.

28. U.S. CONST. art. I, § 2, cl. 3.

29. *Tax*, BLACK'S LAW DICTIONARY (10th ed. 2014); *Understanding Taxes*, INTERNAL REVENUE SERV., <http://apps.irs.gov/app/understandingTaxes/index.jsp> (last visited Oct. 8, 2015).

30. *Id.*

31. *Id.*

32. *Id.*

33. Arnsberger et al., *supra* note 17, at 106.

was not apportioned to citizens of the states based on population.³⁴

In response to the *Pollock* decision, the Sixteenth Amendment was ratified eighteen years later, which grants Congress “[the] power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.”³⁵ The Sixteenth Amendment directly overruled *Pollock*, and Congress now had the explicit power to levy a uniform income tax on individuals and corporations.³⁶

The Revenue Act of 1917 established a deduction from federal taxable income for contributions to charitable organizations.³⁷ The Revenue Act of 1950 created the Unrelated Business Income Tax, which levies a tax on revenues derived from business not “substantially related” to the organization’s charitable purposes.³⁸ Section 501(c) was first codified in the Revenue Act of 1954, reflecting the foregoing concepts about tax exemption for charitable organizations.³⁹

2. Section 501(c)(3)

Under § 501(c)(3), as in effect today, there are several different kinds of charitable, religious, and educational entities which are exempt from federal corporate income tax.⁴⁰ Section 501(c)(3) requires an organization to be “organized and operated exclusively” for its charitable or civic purpose.⁴¹ In order to meet these qualifications, two broad requirements must be met: the organizational test and the operational test.⁴² Additionally, there are regulatory requirements which must be met, including limitations on excessive commercialization and business activities unrelated to an organization’s tax-exempt purpose.⁴³

The organizational test generally requires that an entity be organized as a state-law nonprofit, must be limited to charitable activities, and must contain a provision in its founding document that should it go out of business, its assets will be transferred to the government or another

34. 157 U.S. 429, 555–56 (1895).

35. U.S. CONST. amend. XVI.

36. See Arnsberger, *supra* note 17, at 107.

37. *Id.* (citing War Revenue Act, ch. 63, § 1201(2), 40 Stat. 300, 330 (1917)).

38. Colombo, *supra* note 14, at 115–16 (citing Revenue Act of 1950, Pub. L. No. 81-814, § 422(b), 64 Stat. 906, 950 (1950)).

39. Arnsberger, *supra* note 17, at 106 (citing Internal Revenue Code of 1954, Pub. L. No. 83-591, § 501(c), 68A Stat. 3, 163–65 (codified as amended at 26 U.S.C. § 501(c) (2012))).

40. 26 U.S.C. § 501(c)(3).

41. *Id.*

42. Colombo, *supra* note 14, at 114.

43. *Id.* at 114–15.

charity.⁴⁴ This more or less nominal threshold is not difficult to meet so long as due diligence is given during the founding of an entity and the drafting of its charter.⁴⁵

The more important requirement is the operational test.⁴⁶ The operational test requires an entity must engage primarily in charitable activities, which means an entity cannot engage in excessive commercial activity.⁴⁷ Section 501(c)(3) and its related regulations also impose additional restrictions on charitable entities. For example, an entity cannot siphon off assets to insiders, including excessive executive compensation.⁴⁸ This is known as private inurement.⁴⁹ Therefore, in order for the NCAA to be tax-exempt, it must satisfy the organizational and operational tests, along with meeting their related regulatory requirements.⁵⁰

B. The NCAA as a Tax-Exempt Organization

The NCAA is currently a tax-exempt organization under § 501(c)(3).⁵¹ In order to understand its tax-exempt status, it is first important to understand the NCAA's history, and the evolution of college sports into a multi-billion dollar industry. The NCAA's beginnings were grounded in crafting uniform rules for football, but today its scope has expanded to govern many aspects of student-athletes' lives.⁵² Throughout the evolution of college sports, the NCAA has attempted to maintain its core concepts of amateurism and the notion of the "student-athlete."

1. The NCAA

The NCAA was established on March 31, 1906, as the Intercollegiate Athletic Association of the United States, and changed its name to the National Collegiate Athletic Association in 1910.⁵³ The

44. *Id.* at 114.

45. *See id.*

46. *Id.* at 114.

47. Treas. Reg. § 1.501(c)(3)-1(c)(1) (2015); *see also* Colombo, *supra* note 14, at 125.

48. Treas. Reg. § 1.501(c)(3)-1(c)(2).

49. *Id.*

50. Colombo, *supra* note 14, at 125.

51. *See National Collegiate Athletic Association*, PROPUBLICA: NONPROFIT EXPLORER, <https://projects.propublica.org/nonprofits/organizations/440567264> (last visited Oct. 8, 2015).

52. *See generally* Kami Mattioli, *The Most Ridiculous NCAA Violations in College Basketball*, SPORTINGNEWS (Sept. 5, 2014), <http://www.sportingnews.com/ncaa-basketball/story/2014-09-05/most-ridiculous-silly-insane-ncaa-violations-college-basketball>.

53. Kay Hawes, *'Its Object Shall Be Regulation and Supervision': NCAA Born from Need to Bridge Football and Higher Education*, NCAA NEWS (Nov. 8, 1999),

NCAA was founded to address and reduce violence in college football.⁵⁴ In 1905 alone, eighteen deaths occurred during a time period where players did not wear helmets, mouthpieces, or faceguards.⁵⁵ Following the tragic 1905 season, many leaders in higher education began questioning football's role on campus.⁵⁶ Chief among them was then Chancellor of Syracuse University, James Roscoe Day, who declared, "[o]ne human life is too big a price for all the games of the season."⁵⁷

From its formation in 1906 through the end of World War II, the NCAA struggled to effectively regulate college athletics due to an unclear mission and the necessity of potential college athletes going off to war.⁵⁸ Following World War II, in 1951, the NCAA enacted a twelve-point code which enumerated, inter alia, the concepts of amateurism and the student-athlete.⁵⁹ During the subsequent forty years, much of the NCAA's development centered on integrating women's sports and satisfying Title IX requirements.⁶⁰

Today, the NCAA still attempts to ground itself in amateurism and education, but also manages an increasing commercialization of college athletics.⁶¹ NCAA regulations govern a variety of issues such as corporate sponsorship of college athletics, and the influence of professional athletic leagues on college athletes.⁶² As a result of the NCAA's significant and singular power over college athletics, it is a frequent target for litigation over antitrust issues.⁶³ However, despite its issues, the NCAA is the preeminent force in college athletics, and its revenues reflect that reality.⁶⁴

The NCAA is a revenue generating powerhouse. For its fiscal year

<http://fs.ncaa.org/Docs/NCAANewsArchive/1999/19991108/active/3623n27.html>

54. *Id.*

55. *Id.*

56. *Id.*

57. *Id.*

58. Gary T. Brown, *NCAA Answers Call to Reform*, NCAA NEWS (Nov. 22, 1999), <http://fs.ncaa.org/Docs/NCAANewsArchive/1999/19991122/active/3624n24.html>.

59. *Id.*

60. Kay Hawes, *Women's Sports Enter NCAA Arena*, NCAA NEWS (Dec. 6, 1999), <http://fs.ncaa.org/Docs/NCAANewsArchive/1999/19991206/active/3625n32.html>.

61. Lindsay J. Rosenthal, *From Regulating Organization to Multi-Billion Dollar Business: The NCAA Is Commercializing the Amateur Competition It Has Taken Almost a Century to Create*, 13 SETON HALL J. SPORT L. 321, 321, 324 (2003).

62. *Id.* at 325–27.

63. *See, e.g., NCAA v. Bd. of Regents of the Univ. of Okla.*, 468 U.S. 85 (1984) (holding that the NCAA's plan for televising college football games for the 1981–1985 seasons constituted horizontal price fixing and output limitations).

64. *See Revenue*, NCAA, <http://www.ncaa.org/about/resources/finances/revenue> (last visited Oct. 8, 2015).

2011–2012, the NCAA generated \$817.6 million in revenue.⁶⁵ Eighty-one percent of its revenue for fiscal year 2011–2012 was derived from “[t]elevision and marketing rights fees.”⁶⁶ However, these numbers do not include the revenue generated by college athletics programs themselves, which annually generate \$6.1 billion.⁶⁷ According to the NCAA, ninety-six percent of its revenue is returned to member conferences and universities.⁶⁸ Nevertheless, as the sole provider of popular college sports, the NCAA is able to extract very lucrative television contracts from broadcast stations.⁶⁹

2. *The NCAA and Tax-Exemption*

In order to understand the NCAA’s tax-exempt status, it is also important to consider the tax-exempt status of colleges and universities. Under § 501(c)(3), colleges and universities are tax-exempt entities because they are organized and operated exclusively for “educational purposes.”⁷⁰ According to U.S. Treasury regulations, an “educational purpose” involves the “instruction or training of the individual for the purpose of improving or developing his capabilities.”⁷¹ University athletic departments, as part of their tax-exempt colleges and universities, are also tax-exempt.⁷²

As for the NCAA’s tax-exempt status itself, the Internal Revenue Service (IRS) generally affords broad definitions to approved tax-exempt organizations under § 501(c)(3).⁷³ In 1976, Congress amended § 501(c)(3) to include entities that “foster[ed] national or international amateur sports competition.”⁷⁴ Prior to the 1976 amendment, it was unclear whether the NCAA’s acting to promote college athletics, or any other ostensible purpose, would have been a *prima facie* charitable purpose required under the organizational and operational tests.⁷⁵

65. *Id.*

66. *Id.*

67. *Id.*

68. *Id.*

69. Cy Brown, *TV Deals That Changed the Games*, SPORTSONEARTH (Oct. 6, 2014), <http://www.sportsonearth.com/article/97765848/nba-tv-rights-deals-24-million-nine-years-turner-espn>.

70. 26 U.S.C. § 501(c)(3) (2012).

71. Treas. Reg. § 1.501(c)(3)-1(d)(3)(i)(a) (2015).

72. Colombo, *supra* note 14, at 117.

73. *Id.*

74. Tax Reform Act of 1976, Pub. L. No. 94-455, § 1313(a), 90 Stat. 1520, 1730 (codified as amended at 26 U.S.C. § 501(c)(3)).

75. *See* Hutchinson Baseball Enters., Inc. v. Comm’r, 696 F.2d 757, 762 (10th Cir. 1982) (holding that even absent legislative change the furtherance of recreational and amateur

Notwithstanding any potential impact of the NLRB's decisions in the *Northwestern*⁷⁶ case, or any similar future cases, the NCAA has an explicitly defined charitable purpose within § 501(c)(3).⁷⁷ However, the analysis of the NCAA as a tax-exempt organization does not end here.

In order to be tax-exempt, the NCAA must not engage in private inurement, private benefit, or excessive commercial activity.⁷⁸ Under U.S. Treasury regulations, private inurement occurs where net earnings manifest in whole or part to the benefit of private individuals.⁷⁹ The most likely way the NCAA could engage in private inurement is through payment of salaries in excess of fair market value.⁸⁰ The reasonableness of compensation for § 501(c)(3) purposes is governed under § 4958 and its related regulations.⁸¹ The reasonableness of compensation is determined by looking at the total compensation package, and comparing it to the market value for the same or similar services.⁸² However, the IRS has not chosen to apply the private inurement doctrine to the NCAA.⁸³

With regard to private benefit, an entity can lose its tax-exemption if it confers excessive benefit to parties outside of the defined charitable class.⁸⁴ The distinction between private inurement and private benefit is that private benefit can apply to transactions with outside third parties and to transactions based on fair market value.⁸⁵ On its face, the NCAA would appear to be engaging in private benefits because of the benefit it provides to third-party television providers who broadcast games, or because it serves as a de facto minor league system for certain sports such as football and basketball.⁸⁶ However, the IRS has not chosen to apply the private benefit doctrine to the NCAA.⁸⁷

Finally, an entity must not engage in excessive commercial activity, meaning a charitable organization can lose its tax-exempt status if it runs significant commercial businesses notwithstanding significant charitable

sports would be a charitable activity).

76. See generally *Nw. Univ. (Nw. Univ. II)*, 362 N.L.R.B. No. 167, 204 L.R.R.M. (BNA) 1001 (Aug. 17, 2015); *Nw. Univ. (Nw. Univ. I)*, No. 13-RC-121359, 198 L.R.R.M. (BNA) 1837 (N.L.R.B. Region 13 Mar. 26, 2014).

77. Colombo, *supra* note 14, at 118–19.

78. *Id.* at 119.

79. Treas. Reg. § 1.501(c)(3)-1(c)(2) (2015).

80. Colombo, *supra* note 14, at 120.

81. *Id.* (citing 26 U.S.C. § 4958 (2012)).

82. Treas. Reg. § 53.4958-4(b)(ii)(A)–(B) (2015).

83. Colombo, *supra* note 14, at 125.

84. *Id.* at 122.

85. *Id.*

86. *Id.* at 125.

87. *Id.*

activities.⁸⁸ U.S. Treasury regulations govern excessive commercial activity, stating an organization will be treated as operating for tax-exempt purposes if it is *primarily* engaged in activities to that end.⁸⁹ However, an organization will not be treated as operating primarily for tax-exempt purposes if more than an “insubstantial part” of its activities are not engaged in furtherance of tax-exempt purposes.⁹⁰ Unfortunately, what constitutes “more than . . . insubstantial” has not been clarified by the IRS or the courts.⁹¹

Despite a lack of clarity regarding how much commercial activity § 501(c)(3) permits, the IRS has consistently ruled that college athletics themselves are “functionally related” to the educational mission and purposes of their universities, which is the basis for the universities’ tax-exempt status.⁹² However, this does not necessarily cover the NCAA itself, which promotes and governs college athletics.⁹³ Furthermore, because ninety-six percent of the NCAA’s revenue is allocated to its member conferences and schools, its commercial activities are in furtherance of its charitable purpose to foster amateur sports competition.⁹⁴ Thus, under the current IRS doctrine, the NCAA as the governing body of college athletics is not engaged in more than insubstantial commercial activity, notwithstanding the ostensible commercial purpose of college athletic events.

In summary, the NCAA is organized and operated under an explicit charitable purpose under § 501(c)(3); operates without conferring private inurement or benefit; and is not engaged in excessive commercial activity. Thus, the NCAA’s tax-exempt status under § 501(c)(3) is well established, and the IRS and the courts have shown no appetite for eroding its foundations for tax-exemption.⁹⁵

88. Colombo, *supra* note 14, at 126.

89. Treas. Reg. § 1.501(c)(3)-1(c)(1) (2015).

90. *Id.*

91. Colombo, *supra* note 14, at 127.

92. *Id.* at 132.

93. See NAT’L COLLEGIATE ATHLETIC ASS’N, *supra* note 4, § 1.2(a), (f), (h).

94. NCAA, *supra* note 64.

95. See Colombo, *supra* note 14, at 141.

II. THE UNRELATED BUSINESS INCOME TAX

While opponents of the NCAA's tax-exempt status have failed to effectively challenge the foundations of its tax-exemption, an alternative argument has been made, relying on the unrelated business income tax (UBIT).⁹⁶ The UBIT applies to the net income from a "trade or business . . . that is regularly carried on, and . . . is not substantially related to the [tax]-exempt organization's accomplishment of its exempt[ion] purpose."⁹⁷

The term "trade or business" means "any activity which is carried on for the production of income from the sale of goods or the performance of services."⁹⁸ The term "regularly carried on" deals with the frequency of the activity.⁹⁹ The trickier part of the UBIT is the substantially related to tax-exempt purpose element. Under § 511(a)(1)–(2), a tax is imposed on the unrelated business income of any organization described under § 501(c), including § 501(c)(3).¹⁰⁰ Section 513(a) defines "unrelated trade or business" as "any trade or business the conduct of which is not substantially related . . . to the exercise or performance by such organization of its charitable . . . function constituting the basis for its tax-exemption under § 501."¹⁰¹ U.S. Treasury regulations state that a trade or business is substantially related to its tax exempt purpose if it "contribute[s] importantly" to that purpose.¹⁰² The regulation states further that the meaning of "contribute importantly" "depends in each case upon the facts and circumstances involved."¹⁰³ Thus, whether the UBIT applies to the NCAA depends on the circumstances.

A. *The UBIT and the NCAA*

In the context of the NCAA, the UBIT argument is ineffective. The NCAA produces income from many sources, mostly from its television contracts.¹⁰⁴ Additionally, the NCAA's business is regularly carried on, as all sports have set seasons which occur every year.¹⁰⁵ Finally, the NCAA's tax-exempt purpose is "foster[ing] national or international

96. *Id.* at 134–35.

97. *Id.* at 116.

98. 26 U.S.C. § 513(c) (2012); *see also* Treas. Reg. § 1.513-1(b) (2015).

99. Treas. Reg. § 1.513-1(c)(1).

100. 26 U.S.C. § 511(a)(1)–(2).

101. *Id.* § 513(a).

102. Treas. Reg. § 1.513-1(d)(2).

103. *Id.*

104. NCAA, *supra* note 64.

105. *See generally Division I Championships*, NCAA, <http://www.ncaa.org/championships?division=d1> (last visited Oct. 8, 2015).

amateur sports competition” and ninety-six percent of its derived revenue is allocated to its member conferences and schools to help fund their tax-exempt athletic programs.¹⁰⁶ Thus, no matter the source of the NCAA’s revenue, including its lucrative television contracts, virtually all of it is used in furtherance of its charitable purpose of fostering amateur sports competition. Thus, the NCAA meets the “substantially related” test. Therefore, the NCAA does not meet the criteria to be subject to the UBIT.

B. The UBIT and Universities

While the UBIT may not apply to the NCAA, it could be argued the UBIT should apply to university athletic departments. Like the NCAA, colleges and universities derive their tax-exempt status under § 501(c)(3).¹⁰⁷ Specifically, colleges and universities are “organized and operated exclusively for . . . educational purposes.”¹⁰⁸ On their face, university athletic departments do not seem substantially related to the educational purposes from which they derive tax-exempt status. However, the IRS has ruled that college athletic departments are “an integral part of the educational process of a university.”¹⁰⁹ Thus, even college athletic departments meet the substantially related test to their university’s tax-exempt purposes.

Despite the failure to apply the UBIT to the NCAA or universities, the UBIT may be implicated by the NLRB decisions in *Northwestern* or similar future cases. Further discussion on this issue is provided in Section V.

III. AMATEURISM AND COLLEGE ATHLETICS

As discussed in Sections I and II, challenges to the NCAA’s tax-exempt status have fallen flat. However, *Northwestern*, or similar future cases may provide a new avenue of attack. The NCAA relies for its tax-exempt status on “foster[ing] national or international amateur sports competition.”¹¹⁰ The key question is what does “amateur” mean within the context of the statute? Colloquially, amateur can mean someone who does not in engage in an activity as a professional, where he or she would be compensated.¹¹¹ If amateur turns on the notion of doing something as a profession for which you are compensated, then the *Northwestern* case

106. 26 U.S.C. § 501(c)(3) (2012); *see also* NCAA, *supra* note 64.

107. Colombo, *supra* note 14, at 113–14.

108. 26 U.S.C. § 501(c)(3).

109. Rev. Rul. 80-296, 1980-2 C.B. 195.

110. 26 U.S.C. § 501(c)(3).

111. Colombo, *supra* note 14, at 140.

presents a problem. Assuming a broad application of *Northwestern's* rationale in futures cases, any college athlete receiving a scholarship would be a compensated employee of his or her university. If so, they are not amateur athletes. Therefore, the NCAA would be a governing body for non-amateur athletics, and the provision it relies on for its tax-exempt status would no longer be applicable.

A. Amateurism Defined by the NCAA

According to the NCAA, “[s]tudent-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.”¹¹² Ironically, avocation means “‘an activity taken up in addition to one’s regular work or profession, usually for enjoyment’ and ‘one’s regular work or profession.’”¹¹³ This would appear to present a contradiction. However when you consider the term avocation in the context of the entire definition, it speaks more toward the “in addition to one’s regular work” portion of the definition. A student-athlete’s primary function, at least according to the NCAA, is being a student, and athletics are taken up in addition to being a student.

The NCAA protects its definition of amateurism by preventing compensation. College athletes are unpaid, meaning college athletes cannot earn pay directly or indirectly for using his or her athleticism in his or her sport.¹¹⁴ The NCAA bylaws specifically state, “[a]n individual loses amateur status . . . if the individual . . . [u]ses his or her athletics skill (directly or indirectly) for pay in any form in that sport.”¹¹⁵ Additionally, college athletes cannot accept future pay while still a college athlete and cannot receive financial assistance from anyone, with few exceptions.¹¹⁶ Thus, it is clear the NCAA intended by the language of its bylaws that amateurs must not be compensated for their athletic services.

112. NAT’L COLLEGIATE ATHLETIC ASS’N, *supra* note 4, § 2.9.

113. Virginia A. Fitt, *The NCAA’s Lost Cause and the Legal Ease of Redefining Amateurism*, 59 DUKE L.J. 555, 559 (2009) (quoting *Avocation*, AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE (4th ed. 2000)).

114. NAT’L COLLEGIATE ATHLETIC ASS’N, *supra* note 4, § 12.1.2(a), (d).

115. *Id.*

116. *See id.* §§ 12.1.2(b), 12.3.1.1, 12.4–12.5.

B. Amateurism Defined by the Tax Code

The IRC takes a very deferential approach to defining amateur within the context of § 501(c)(3).¹¹⁷ The IRS has in effect adopted the definition of amateur found in the Amateur Sports Act of 1978.¹¹⁸ The Amateur Sports Act defines an amateur athlete as an athlete who meets the eligibility standards established by the national governing body (NGB) for the sport in which he or she competes.¹¹⁹

NGBs are nongovernmental organizations working in conjunction with the United States Olympic Committee to manage national level sports teams to represent the United States at competitions.¹²⁰ The IRS has officially deferred to these NGBs for formulating the definition of amateur.¹²¹

In effect, there is no precise definition of amateur for IRS purposes. Each sport specifically has its own definition of amateur, and the IRS defers to those definitions.¹²² Although the NCAA is not an NGB in the context of the Amateur Sports Act, it is the national governing body of college athletics generally.¹²³ Furthermore, because the IRS has established a deferential standard, it follows that for the NCAA's tax purposes, the IRS will most likely use the NCAA's definition of amateur.¹²⁴ As discussed above, the NCAA's definition of amateur is predicated on college athletes being unpaid for using their athleticism in their sport.¹²⁵ Thus, amateurism, as applied to the NCAA in the context of the IRC, likely hinges on whether college athletes are paid for playing their respective sports. This is why the *Northwestern* decision, or similar future decisions are damaging for the NCAA's tax-exempt status.

IV. THE NORTHWESTERN NLRB DECISIONS

As discussed above, the NCAA's tax-exempt status is well established, and is unlikely to end, but for a significant shift in doctrine. Opponents of tax-exempt college athletics have argued in the past that the NCAA, by its operation, should not qualify for § 501(c)(3) status, or that athletic departments of universities should be subject to the UBIT

117. Fitt, *supra* note 113, at 582.

118. *Id.* (citing 36 U.S.C. § 220501 (2012)).

119. 36 U.S.C. § 220501(b)(1).

120. Fitt, *supra* note 113, at 582.

121. I.R.M. 7.25(26)(7).

122. Fitt, *supra* note 113, at 582.

123. 36 U.S.C. § 220501(b)(1).

124. *See* Fitt, *supra* note 113, at 582.

125. NAT'L COLLEGIATE ATHLETIC ASS'N, *supra* note 4, § 12.1.2(a), (d).

and not be covered by the university's tax-exempt status.¹²⁶ Despite their failure, the landscape may have changed for the NCAA's tax-exempt status in March 2014 and August 2015 with the NLRB's decisions in *Northwestern University*.¹²⁷

One of the most intractable debates in college sports today is whether college athletes should be paid money in addition to any athletic scholarship package received, and whether college athletes should be allowed to profit off their likeness while in school.¹²⁸ A less-known component of the debate over college athletes is their ability to negotiate for better "working conditions."¹²⁹ This is the backdrop of *Northwestern*, which attempted to determine the important question of whether Division I scholarship football players at Northwestern University were employees of Northwestern receiving compensation for their services in the form of an athletic scholarship package.¹³⁰

A. Northwestern University, *March 2014*

A group of football players, known as the College Athletes Players Association, argued that scholarship players on the Northwestern Wildcats football team were employees of Northwestern University within the meaning of the National Labor Relations Act.¹³¹ Furthermore, they argued that because they were employees of Northwestern, they were entitled to choose whether to be represented for collective bargaining purposes.¹³²

The NLRB held that players receiving athletic scholarships from Northwestern were employees of Northwestern under § 152(3) of the National Labor Relations Act.¹³³ The NLRB more importantly held the scholarships the players received were compensation for their athletic

126. See e.g., Richard L. Kaplan, *Intercollegiate Athletics and the Unrelated Business Income Tax*, 80 COLUM. L. REV. 1430 (Nov. 1980).

127. See generally *Nw. Univ. (Nw. Univ. I)*, No. 13-RC-121359, 198 L.R.R.M. (BNA) 1837 (N.L.R.B. Region 13 Mar. 26, 2014).

128. See generally *O'Bannon v. NCAA*, 7 F.Supp.3d 955 (N.D. Cal. 2014), *aff'd in part and vacated in part*, 2015 WL 5712106 (9th Cir. Sept. 30, 2015).

129. See Alex Prewitt, *Large Majority Opposes Paying NCAA Athletes*, *Washington Post-ABC News Poll Finds*, WASH. POST (Mar. 23, 2014), https://www.washingtonpost.com/sports/colleges/large-majority-opposes-paying-ncaa-athletes-washington-post-abc-news-poll-finds/2014/03/22/c411a32e-b130-11e3-95e8-39bef8e9a48b_story.html (asserting that public opinion is split equally about whether college athletes can negotiate working conditions).

130. *Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1839.

131. *Id.*

132. *Id.*

133. *Id.* at 1840 (citing 29 U.S.C. § 152(3) (2012)).

services performed for Northwestern.¹³⁴

The NLRB first addressed the question of whether scholarship football players are employees given the nature of their work and their relationship to the university.¹³⁵ The NLRB detailed the rigorous football-related schedule that the players are engaged in year-round.¹³⁶ During training camp just prior to the season, players spend fifty to sixty hours per week on football activities.¹³⁷ During the season, players devote forty to fifty hours per week to football activities in addition to being full-time students.¹³⁸ During the off-season, players devote fifteen to twenty-five hours per week to football activities.¹³⁹ In addition to the time commitment, all players are required to abide by special rules set forth by the head coach regarding living quarters, class attendance, etc.¹⁴⁰

The employment relationship begins with the signing of a “tender.”¹⁴¹ A tender is a formal scholarship offer which dictates the “terms” of the offer.¹⁴² The NLRB held these tenders effectively serve as employment contracts that include the players’ obligations as an employee and the details regarding their scholarship, which is a form of compensation.¹⁴³ The scholarships represent a transfer of economic value from Northwestern for the players’ athletic services provided year-round.¹⁴⁴ That the players do not receive a traditional paycheck, and that Northwestern does not treat scholarships as taxable income to the players, do not mean the players do not receive compensation.¹⁴⁵

Northwestern argued that scholarship football players should be treated as no more than graduate assistants, who are not employees.¹⁴⁶ However, the NLRB held scholarship football players are not akin to graduate assistants because their relationship to Northwestern is economic in nature, and football-related duties are unrelated to academics; whereas graduate assistants’ relationship to Northwestern are academic in nature, and their job tasks are related to their academic

134. *Id.* at 1848–49.

135. *See Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1840–41.

136. *See generally id.*

137. *Id.* at 1842.

138. *Id.* at 1843.

139. *Id.* at 1845.

140. *Nw. Univ. I*, 198 L.R.R.M. (BNA) 1841–42.

141. *Id.* at 1841.

142. *Id.*

143. *Id.* at 1849.

144. *Id.*

145. *Nw. Univ. I*, 198 L.R.R.M. (BNA) 1849.

146. *Id.* at 1851.

studies.¹⁴⁷ Given the great time commitment to football activities, players are not “primarily students,” and football activities are not a core element of the players’ degree requirements, as they receive no academic credit for football activities.¹⁴⁸ Additionally, the players are not under the supervision of academic faculty, and their scholarships are awarded based on football talent, and not academic talent.¹⁴⁹ As such, scholarships cannot be said to be merely a form of financial aid.¹⁵⁰

Thus, the regional NLRB concluded that the scholarship players were employees within the meaning of the National Labor Relations Act.

B. Northwestern University, August 2015

One month after the *Northwestern* decision, the Northwestern scholarship players held a vote on unionization.¹⁵¹ Concomitantly, the NLRB in Washington agreed to hear Northwestern University’s appeal of the initial NLRB decision.¹⁵² The decision on the appeal was released in August 2015.¹⁵³

In the August 2015 decision, the NLRB held it would not assert jurisdiction in the case.¹⁵⁴ The NLRB reasoned that asserting jurisdiction would “not serve to promote stability in labor relations.”¹⁵⁵ This was due to the fact that Division I football teams come from both public and private universities.¹⁵⁶ The NLRB can only assert jurisdiction over labor matters in the private sector, here, private colleges.¹⁵⁷ It cannot assert jurisdiction over public universities.¹⁵⁸ Thus, any decision it made would only apply to private universities, thus creating separate rules for public and private universities.¹⁵⁹

147. *Id.* at 1851–52.

148. *Id.*

149. *Id.* at 1852–53.

150. *Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1853.

151. Mason Levinson, *Northwestern Players Complete Union Vote; NLRB Review Under Way*, BLOOMBERG (Apr. 26, 2014), <http://www.bloomberg.com/news/2014-04-24/northwestern-football-players-vote-on-union-as-appeal-proceeds.html>.

152. Melanie Trotman, *NLRB to Review Northwestern’s Appeal of Student-Athletes’ Union Decision*, WALL ST. J. (Apr. 24, 2014), <http://www.wsj.com/articles/SB10001424052702304788404579522063428957786>.

153. *Nw. Univ. (Nw. Univ. II)*, 362 N.L.R.B. No. 167, 204 L.R.R.M. (BNA) 1001, 1001 (Aug. 17, 2015).

154. *Id.* at 1001–02.

155. *Id.* at 1002.

156. *Id.* at 1004.

157. *Id.*

158. *Nw. Univ. II*, 362 N.L.R.B. No. 167, 204 L.R.R.M. (BNA) 1004.

159. *Id.* at 1006–07.

Despite the NLRB's unwillingness to assert jurisdiction, it did mention the issue of scholarship athletes as employees.¹⁶⁰ The NLRB explicitly stated it would not address whether scholarship athletes are employees within the meaning of the National Labor Relations Act.¹⁶¹ However, the NLRB did not foreclose the possibility of deciding scholarship athletes are employees in future cases.¹⁶² Thus, the NLRB has left the legal question of scholarship players as employees unsettled and the door for future cases dealing with this question open.

The real effect of the August 2015 decision was to deny the players' petition to unionize.¹⁶³ The NLRB did not take a position on whether they were employees.¹⁶⁴ In fact, the NLRB explicitly stated it was not deciding that question, but that it may in a future case.¹⁶⁵

Regarding the NCAA's tax-exempt status, the key holdings from the March 2014 decision are that scholarship players are "employees" within the meaning of the National Labor Relations Act, and that their scholarships are "compensation" for non-academic services rendered pursuant to an employment contract.¹⁶⁶ This matters because of the concept of "amateurism" embedded in the 501(c)(3) and discussed in Part III. While the August 2015 decision did take away momentum for opponents of the NCAA's tax-exempt status, it does not foreclose the issue, and, if anything, invites future litigation on it.

Following the August 2015 decision, it is clear that *Northwestern* will not cause the NCAA to lose its tax-exempt status. But it does provide the blueprint for that to happen. The NLRB left the issue unsettled, and future cases following a similar rationale could indeed mark the end of the NCAA's tax-exempt status. Regardless, the issue of paying college athletes remains a controversial topic, and the issue will not go away anytime soon.

C. How Future Cases May Affect the NCAA's Tax-Exempt Status

Whether or not the NCAA loses its tax-exempt status depends on whether the rationale in the March 2014 *Northwestern* decision is followed in a future case. A broad use of the rationale could mean all scholarship athletes playing any sport are compensated employees of

160. *Id.*

161. *Id.* at 1008.

162. *Nw. Univ. II*, 362 N.L.R.B. No. 167, 204 L.R.R.M. (BNA) at 1008.

163. *Id.*

164. *Id.*

165. *Id.*

166. *Nw. Univ. (Nw. Univ. I)*, No. 13-RC-121359, 198 L.R.R.M. (BNA) 1837, 1848–49 (N.L.R.B. Region 13 Mar. 26, 2014).

their universities. However, a narrow use could limit its applicability to Division I football players. If so, the NCAA will probably not lose its tax-exempt status, because only scholarship players in one sport at one division level will no longer be amateurs. Either way, the fate of the NCAA's tax-exempt status is predicated on how similar future cases play out.

V. THE NCAA'S TAX-EXEMPT STATUS SHOULD BE ELIMINATED

As discussed in Section III, the NCAA's definition of amateurism is predicated on college athletes not being compensated. Discussed in Section IV, the March 2014 *Northwestern* decision held that scholarship football players are compensated employees. This presents a paradox between how the NCAA claims tax-exempt status under § 501(c)(3), and the potential employment status of scholarship athletes. This section argues that compensated college athletes are not amateurs, and therefore the NCAA should lose its tax-exempt status because it is no longer "fostering . . . amateur sports competition."¹⁶⁷

Despite the uncertainty over *Northwestern*, and the broader question of college athletes as employees, for the purposes of Section V, it will be assumed that a future case holds that all scholarship athletes in all sports are employees of their universities. Although the likelihood of a broad interpretation is probably small given the requisite shift in doctrine, it is useful for analyzing the limits of the NCAA's tax-exempt status.

A. Amateurs or Not Amateurs?

The March 2014 *Northwestern* decision focused on several factors, which in their totality demonstrated scholarship football players were compensated employees.¹⁶⁸ A tender is used to establish a prospective player's commitment to a particular university and details the terms of his or her scholarship offer.¹⁶⁹ The regional NLRB held that by agreeing and abiding by the tender's terms, the scholarship received is compensation because it represents a transfer of economic value to the player.¹⁷⁰ It does not matter that players do not receive traditional paychecks or cannot receive cash payments under NCAA rules.¹⁷¹ The player is an employee receiving compensation.¹⁷²

167. 26 U.S.C. § 501(c)(3) (2012).

168. See *Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1855.

169. NAT'L COLLEGIATE ATHLETIC ASS'N, *supra* note 4, § 13.02.11.

170. *Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1849.

171. *Id.*

172. *Id.*

The regional NLRB characterized tenders as employment contracts due to their quid pro quo nature.¹⁷³ Moreover, the regional NLRB distinguished student-athletes from academic-related quasi-employees.¹⁷⁴ Student-athletes' work is inherently non-academic, unlike graduate assistants, making them contracted non-academic employees who qualify as "employees" under the National Labor Relations Act.¹⁷⁵ As such, if the rationale in the March 2014 *Northwestern* decision is applied broadly, then any college athlete who signs a tender and receives a scholarship would be receiving compensation pursuant to an employment contract.

As discussed in Section III, the NCAA defines amateurs as unpaid individuals.¹⁷⁶ Moreover, the IRS defers to NGBs to define amateurism in their respective contexts.¹⁷⁷ While the NCAA may not be the NGB per se like USA Basketball or USA Soccer, it should still be given deference by the IRS in defining amateur for its own purposes. The NCAA is the national governing organization for college sports, and sets the rules for each sport participating under its authority.¹⁷⁸ The NCAA's very founding was predicated on developing uniform rules and standards for football.¹⁷⁹ In the context of the IRC, the NCAA should be held to its longstanding definition of amateur—meaning unpaid—student-athletes.

By holding the NCAA to its own definition of amateur and given the regional NLRB's rationale, the NCAA would not be fostering amateur sports competition. Quite the contrary, it would be fostering semi-professional sports competition. Its athletes would be employed and compensated for their athletic performances, thus they would not be amateurs.

B. Absent Amateur Athletes, the NCAA Should Not Be Tax-Exempt

As discussed in Section I, a § 501(c)(3) organization must be organized for a charitable purpose.¹⁸⁰ The NCAA's charitable purpose is fostering amateur sports competition.¹⁸¹ Assuming a broad application of the March 2014 *Northwestern* decision's rationale, then all scholarship athletes would not be amateurs. Therefore, the NCAA would fail the

173. *Id.*

174. *Id.* at 1851.

175. *Nw. Univ. I*, 198 L.R.R.M. (BNA) at 1851–52.

176. NAT'L COLLEGIATE ATHLETIC ASS'N, *supra* note 4, § 12.1.2(a), (d).

177. Fitt, *supra* note 113, at 582.

178. *See* NAT'L COLLEGIATE ATHLETIC ASS'N, *supra* note 4, § 1.

179. Hawes, *supra* note 53.

180. 26 U.S.C. § 501(c)(3) (2012).

181. Colombo, *supra* note 14, at 118–19.

organizational test because it is not organized for an acceptable charitable purpose.

The NCAA's tax-exempt status would not be predicated on its distributing ninety-six percent of its revenues back to member schools, because it would simply not be an organization organized nor operated *exclusively* for fostering amateur sports competition.¹⁸² Claiming athletic scholarships are not compensation and college athletes are not employees is nothing more than a semantic contortion. The nature of athletes' work is not academic in nature, but rather akin to hiring a contractor. The contractor provides the customer a service in return for compensation. Here, scholarship athletes provide a service to the university in return for compensation in the form of a scholarship. Moreover, the IRC explicitly defines gross income to individuals, as any income from "whatever source derived," including compensation for services.¹⁸³

In addition to athletic scholarships being compensation for services within the meaning of the IRC, they would also meet the *Commissioner v. Glenshaw Glass Co.* test for income.¹⁸⁴ Under *Glenshaw Glass*, a person has income where there is an "undeniable accession[] to wealth, clearly realized, and over which the [person has] complete dominion."¹⁸⁵ Here, scholarship players have an undeniable accession to wealth, since the scholarships have a quantifiable dollar value and are a fortuitous gain to the recipient. Furthermore, the value of the scholarship is clearly realized, as the players are able to attend class, live on campus, and take full benefit of the value embedded within the scholarship. Finally, the players have complete dominion over the value of the scholarship so long as they meet their prearranged obligations set forth in the tender. Thus, any college athlete receiving an athletic scholarship is deriving income from his or her university.

Despite athletic scholarships meeting the definition of income under § 61 and *Glenshaw Glass*, student-athletes would not include the value of the scholarship in their gross income on their tax returns. Section 117 specifically exempts from gross income any qualified scholarship.¹⁸⁶ For a qualified scholarship, a student-athlete must be a degree candidate at a qualifying educational institution, which universities are, and the funds must be used for qualified tuition and related expenses which include

182. 26 U.S.C. § 501(c)(3).

183. *Id.* § 61(a)(1).

184. *See* 348 U.S. 426, 431 (1955).

185. *Id.*

186. 26 U.S.C. § 117 (2012).

tuition, books, supplies, and fees required for attendance or enrollment.¹⁸⁷ However, this would not include room, board, and travel.¹⁸⁸ That would most likely be included in gross income because that value is derived from their services to the university as an employee.¹⁸⁹

Given the potential evidence against the NCAA as a tax-exempt organization, it would seem to behoove the NCAA to reform itself in order to properly meet the requirement of § 501(c)(3). However, that is not easily accomplished.

C. It Is Unfeasible for the NCAA to Eliminate the Scholarship System

Because scholarship athletes should be considered compensated employees, the logical correction to this problem would be to eliminate the scholarship system altogether. Such a move would return the NCAA to pure amateur sports competition; however, reality makes this unfeasible. Scholarship athletes make up a disproportionate amount of student-athletes, and dismantling the scholarship system would have disastrous effects on student-athletes.

Division I football teams are allowed to have a maximum of 105 players with up to eighty-five of those players on scholarship.¹⁹⁰ The ratio of scholarship players to players per team is similarly high in other sports as well.¹⁹¹ Assuming all scholarships are utilized, eighty percent of a college football team would be comprised of non-amateurs. The NCAA cannot claim it is fostering amateur sports competition if eighty percent of every Division I football team is not composed of amateurs. Removing the scholarship system would eliminate eighty percent of every Division I team instantly. Teams would have to force their scholarship players to forego their scholarship in order to remain on the team. However, that is impractical given the financial realities of student-athletes.

Student-athletes are awarded athletic scholarships based on their skill level at their given sport. The better the player, the more likely he or she will get a scholarship. For many athletes, that scholarship is a necessity to escape poverty. Eighty-six percent of student-athletes live below the poverty line.¹⁹² Thus, because scholarships are a financial necessity to nearly all student athletes, it is not feasible or humane for the

187. *Id.* § 117(a)–(b).

188. *Id.*

189. *Id.* § 61(a)(1).

190. NAT'L COLLEGIATE ATHLETIC ASS'N, *supra* note 4, §§ 15.5.6.1, 17.10.2.1.2.

191. *See generally* NAT'L COLLEGIATE ATHLETIC ASS'N, *supra* note 4, §§ 15, 17.

192. Matt Hayes, *Report Concludes 86 Percent of Student Athletes Live in Poverty*, SPORTING NEWS (Jan. 16, 2013), <http://www.sportingnews.com/ncaa-football/story/2013-01-15/student-athletes-poverty-paid-scholarships-nca-texas-duke>.

NCAA to abandon the scholarship system simply to maintain amateurism. If anything, that statistic bolsters the argument that college athletes should be paid *in addition* to their scholarships.

The truth is, the NCAA has amassed a sports-media empire reflected by its large yearly revenues.¹⁹³ These revenues have been the result of the commercialization of college athletes and their respective sports. Without the athletes' performances, there would be no revenue. College athletes are therefore conferring economic value to the NCAA. However, the best, most marketable athletes are not doing this out of charity. They are also receiving economic value in return for their services in the form of a scholarship which has monetary value. The NCAA needs the scholarship system to recruit and retain top talent, and given the cost of college and the percentage of student-athletes living in poverty, student-athletes cannot afford to compete without a scholarship.

Should scholarship athletes be considered employees, the NCAA will not be able to maintain the status quo and keep its tax-exempt status. With such a high percentage of athletes on scholarship, the NCAA cannot reasonably argue the amount is so insubstantial. As such, the NCAA would no longer be an organization fostering amateur sports competition, but rather fostering professional or quasi-professional sports competition. Therefore, it would not be able to rely on § 501(c)(3) for its tax exemption because it would not have a charitable purpose within the meaning of the statute.¹⁹⁴

D. Alternatively, the NCAA's Tax-Exempt Status Should Be Restricted

Section V assumed a broad applicability of the *Northwestern* rationale; however, it may be too broad. The facts of the case are football-centric, and it is possible that any future decision will only apply in the Division I football context.¹⁹⁵ As such, for the purposes of this subsection, it will be assumed a future case following the *Northwestern* rationale would only be applicable to Division I football scholarship players.

Even assuming that scholarship Division I football players are non-amateurs, every other student-athlete would still be an amateur. In other words, the NCAA's Division I football activities would be taxable commercial activity, and the activities of every other sport would still be in furtherance of its charitable purpose.¹⁹⁶ This raises the important

193. NCAA, *supra* note 64.

194. 26 U.S.C. § 501(c)(3) (2012).

195. *See generally* Nw. Univ. (*Nw. Univ. I*), No. 13-RC-121359, 198 L.R.R.M. (BNA) 1837 (N.L.R.B. Region 13 Mar. 26, 2014).

196. 26 U.S.C. § 501(c)(3).

question of whether the NCAA's Division I football revenue would be subject to the UBIT while the rest of the NCAA's net income would remain tax-exempt.

1. Division I Football Revenue Should Be Subject to the UBIT

As discussed above, the UBIT applies to the net income from a "trade or business . . . that is regularly carried on, and . . . is not substantially related to the exempt organization's accomplishment of its exempt purpose."¹⁹⁷ This would seem to apply to Division I football revenues because they would not be substantially related to the NCAA's tax-exempt purpose of fostering amateur sports competition. Compensated Division I football players would not be amateurs, so the revenue, and ultimately net income they generate, would not be in furtherance of the NCAA's charitable purpose, nor is it substantially related.

Division I football would be a business within the context of the UBIT, because it generates income.¹⁹⁸ Division I football is only regularly carried on with the college football season occurring every year in the fall. Thus, Division I football would meet all of the criteria to be subject to the UBIT. The IRS has the capacity and authority to separate revenue streams from an entity for tax purposes.¹⁹⁹ Here, it could do so by parsing football related revenues from non-football revenues. The football related revenue would be subject to corporate income tax. However, the NCAA would then be able to take advantage of numerous deductions and other provisions to reduce its tax liability, possibly to zero.

2. All Non-Division I Football Sports Should Remain Tax-Exempt

As discussed in Section II, the pre-*Northwestern* NCAA is not subject to the UBIT. Even with an erosion of amateurism in the football context, it would remain for all other sports. Thus, revenue derived from those other sports would still be commensurate with the NCAA's charitable purpose of fostering amateur sports competition and would continue to be tax-exempt.

It is possible that, in the future, scholarship players in other sports would be found to be compensated employees of their universities. The most likely candidate is men's basketball, given its status as a major

197. Colombo, *supra* note 14, at 116.

198. Kristi Dosh, *College Football Revenue: Running the Numbers*, SMARTYCENTS (Sept. 24, 2014), <http://smartycents.com/articles/college-football-revenue/>.

199. Colombo, *supra* note 14, at 116.

revenue generating sport.²⁰⁰ However, given that *Northwestern* dealt solely with Division I football and its singular features, it is possible that any use of *Northwestern's* rationale will be limited to that context.

E. The Reality of a Non-Tax-Exempt NCAA

If the NCAA loses its tax-exempt status, it will not be a windfall of tax revenue for the federal government. Even subject to corporate income tax, the NCAA will be able to utilize various tax deductions and provisions to minimize or eliminate its tax liability. Nevertheless, it is still a victory for proper tax code application and represents a symbolic step toward nonprofit tax-exempt reform.

As discussed above, the NCAA distributes ninety-six percent of its revenues to member schools and conferences.²⁰¹ As such, these distributions can be construed as deductible business expenses under § 162.²⁰² Because these payments are made every year, it is likely they qualify as “ordinary and necessary” within the meaning of the statute.²⁰³ Nevertheless, the extent to which the NCAA will pay any taxes is beyond the scope of this note.

What is true, if the NCAA loses its tax-exempt status, is that it is a victory for reformers of the nonprofit tax-exempt sector. The tax code always seeks to uncover the truth of what is before it. The NCAA may argue that it meets the literal or semantic definition of a tax-exempt organization under § 501(c)(3), but the truth is that it does not if scholarship athletes are employees. Despite the NCAA's claims about scholarship student-athletes being uncompensated amateurs, the truth beneath the surface is that they are not. And because the tax code's ultimate goal is to seek the truth of the substance of the matter, the tax code should compel that the NCAA loses its tax-exempt status.

CONCLUSION

The NCAA's tax-exempt status depends on its athletes being amateurs; however, it is no longer the case that these athletes are amateurs. The NCAA defines amateurs as unpaid individuals, and the IRS gives deference to the NCAA on what amateur means in the context

200. See Mark Alesia, *NCAA Approaching \$1 Billion per Year amid Challenges by Players*, INDYSTAR (Mar. 27, 2014), <http://www.indystar.com/story/news/2014/03/27/ncaa-approaching-billion-per-year-amid-challenges-players/6973767/>.

201. NCAA, *supra* note 64.

202. 26 U.S.C. § 162 (2012).

203. *Id.*

of § 501(c)(3).²⁰⁴ Thus, it is likely the IRS would hold the NCAA to its own definition of amateur. The NLRB held in *Northwestern* that scholarship football players are employees of their university and their scholarships are compensation for their athletic services.²⁰⁵ Thus, by being compensated, these athletes are no longer amateurs and the NCAA is not an entity organized and operated *exclusively* for the purpose of fostering amateur sports competition.²⁰⁶ Therefore, the NCAA should no longer be tax-exempt.

This Note has argued that the NCAA has drifted away from being a purely amateur sports organization on its journey to becoming a sports-media powerhouse. Today, the student-athlete is heavily marketed for the NCAA's benefit and is subject to numerous and sometimes arbitrary rules under the guise of not being an employee.²⁰⁷ However, the NLRB's finding that scholarship athletes are compensated employees has finally provided the conduit for the IRC to identify the truth regarding the NCAA. The truth is, the NCAA neither qualifies nor needs American taxpayers to subsidize it in the form of a tax-exemption. As such, not only should the NLRB decision be upheld, but the NCAA should be stripped of its § 501(c)(3) status.

204. NAT'L COLLEGIATE ATHLETIC ASS'N, *supra* note 4, § 12.1.2(a), (d); *see also* Fitt, *supra* note 113, at 582.

205. Nw. Univ. (*Nw. Univ. I*), No. 13-RC-121359, 198 L.R.R.M. (BNA) 1837, 1840 (N.L.R.B. Region 13 Mar. 26, 2014).

206. 26 U.S.C. § 501(c)(3).

207. *See generally* Mattioli, *supra* note 52.