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Taxing Trades: Proposals to Keep Moneyball Out of Tax Law

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TAXING TRADES: PROPOSALS TO KEEP MONEYBALL OUT OF TAX LAW

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ABSTRACT

Ever since professional sports first captivated the hearts and minds of American fans, team scouts have scoured the land for athletic talent. Upon discovery, scouts must gauge the discovered player's worth to their team, which is done through both observation and statistical analysis commonly known as "Moneyball." However, as economists note, such valuation methods often fall short. Nonetheless, following the Tax Cuts and Jobs Act of 2017 (TCJA), current tax laws require that Internal Revenue Service (IRS) agents engage in the same player valuation conundrum to assess the tax consequences of trades between teams.

Before the TCJA, § 1031 of the Internal Revenue Code allowed trades of player contracts and future draft picks to go untaxed. Section 1031 allowed this because such trades constituted a like-kind exchange, which prevented any gain or loss from being recognized for tax purposes. Now, the TCJA has limited the non-recognition treatment afforded by § 1031 to real property, forcing IRS agents to ascertain the fair market value of player contracts and future draft picks to assess the tax consequences of trades. Adding to the conundrum facing the IRS, the Treasury Department has created a safe harbor permitting teams to treat player contracts and future draft picks as having a zero value for tax purposes; however, the Treasury Department has not released guidance addressing how valuations are to occur when teams avoid the safe harbor.

This article seeks to resolve the valuation conundrum by proposing the reformation of current tax laws such that trades are taxed in the same manner as before the TCJA. Congress may do so legislatively, or the Treasury Department may do so through reliance on the open-transaction doctrine. Not returning to the pre-TCJA manner of taxation is illogical for two reasons. First, the IRS is not capable of measuring the value of player contracts or future draft picks, making the administration of current tax laws infeasible. Second, applying current tax laws to trades is likely to reduce tax revenue because the current tax laws invite teams to reduce their tax liabilities without fundamentally changing their economic position, a process known as tax arbitrage.

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I. INTRODUCTION

EVER since professional sports first captivated the hearts and minds of American fans, team scouts have scoured the land for athletic talent.[1] Professional sports are a business after all, and

1. *See* J.C. Bradbury, Hot Stove Economics 69 (2011). In 1871, baseball became the first commercialized major league sport in the United States. David Q. Voigt, *Reflections on Diamonds: American Baseball and American Culture*, 1 J. Sport Hist. 3, 8 (1974).

team owners are keenly aware that fans prefer teams that win over those that lose.[2] Yet, contrary to what a coach may say, winning is not everything.[3] Profits matter too.[4] Therefore, upon discovery, scouts must put a "dollar sign on the muscle" to ensure that a player's value to a team is equal to or, even better, exceeds the compensation being offered for that player's services.[5]

Scouts traditionally made educated guesses about a player's potential value to a team through mere observation of a player's talent.[6] Over time, the reliance on mere observation has faded away, and many teams have adopted the Moneyball method.[7] The term "Moneyball," taken from the title of Michael Lewis's bestseller, describes a team's use of player performance statistics to analyze and assess a player's potential contribution to the team.[8] The benefits a team may gain from adopting the method is perhaps best illustrated by the success of the Oakland Athletics, despite their relatively small budget.[9] However, Moneyball is imperfect, and economists quickly noted that teams in the National Football League (NFL), Major League Baseball (MLB), the National Basketball Association (NBA), the National Hockey League (NHL), and Major League Soccer (MLS) are bad at making player valuations.[10]

Nonetheless, following the revision of § 1031 of the Internal Revenue Code (the Code) by the Tax Cuts and Jobs Act of 2017 (TCJA), current tax laws require that Internal Revenue Service (IRS) agents engage in the

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2. *See* BRADBURY, *supra* note 1, at 69; *see also* Walter C. Neale, *The Peculiar Economics of Professional Sports: A Contribution to the Theory of the Firm in Sporting Competition and in Market Competition*, 78 Q.J. ECONOMICS 1, 2 (1964) ("The first peculiarity of the economics of professional sports is that receipts depend upon competition among the sportors or the teams . . . .").

3. *See* Joel Sayre, *He Flies on One Wing*, SPORTS ILLUSTRATED, Dec. 26, 1955, at 29, 48 (UCLA Bruin football coach Henry Sanders stated, "Sure, winning isn't everything . . . . It's the only thing.").

4. *See* Rodney Fort & James Quirk, *Cross-Subsidization, Incentives, and Outcomes in Professional Team Sports Leagues*, 33 J. ECON. LITERATURE 1265, 1266–67 (1995).

5. BRADBURY, *supra* note 1, at 69; *see also* PAUL DICKSON, THE DICKSON BASEBALL DICTIONARY 262 (Skip McAfee ed., 3d ed. 2009) (defining "putting [a] dollar sign on the muscle" to mean "[a] money code expressing an ultimate evaluation of a ballplayer," and noting "it is indeed a risky business to put the dollar mark on the individual muscle").

6. *See, e.g.*, MICHAEL LEWIS, MONEYBALL: THE ART OF WINNING AN UNFAIR GAME 3 (2004) (describing baseball scouts as carrying checklists for the five "tools" that should be assessed in a baseball player: "the abilities to run, throw, field, hit, and hit with power").

7. *See id.* at 17, 33–34; *see also* David Leonhardt, *PRO BASKETBALL; Mavericks' New Math May Be an Added Edge*, N.Y. TIMES (Apr. 27, 2003), https://www.nytimes.com/2003/04/27/sports/pro-basketball-mavericks-new-math-may-be-an-added-edge.html [https://perma.cc/UH7M-DMWC] (noting that the owner of the Dallas Mavericks, Mark Cuban, purchased a player valuation method developed by a professor of decision sciences and a professional sports statistician).

8. *See* Bill Gerrard, *Is the* Moneyball *Approach Transferable to Complex Invasion Team Sports?*, 2 INT'L J. SPORT FIN. 214, 214 (2007).

9. *See* BRADBURY, *supra* note 1, at 131–32.

10. DAVID J. BERRI ET AL., THE WAGES OF WINS 9–10, 92 (2006) (noting that "across all the major North American sports, payroll and wins do not have a high correlation," and explaining that "it is entirely possible that mistakes are made when people in sports evaluate player value").

same player valuation conundrum that continues to plague scouts.[11] Before the TCJA, § 1031 allowed trades of player contracts and future draft picks to go untaxed.[12] Section 1031 allowed non-taxation because such trades constituted a like-kind exchange, which prevented any gain or loss from being recognized for tax purposes.[13] While a benefit to teams, this treatment also conveniently allowed IRS agents to avoid the arduous task of ascertaining the fair market value of player contracts and future draft picks.[14] Now, the TCJA has limited the non-recognition treatment afforded by § 1031 to real property.[15] To add to the valuation conundrum facing the IRS, the Department of the Treasury has created a safe harbor permitting teams to treat player contracts and future draft picks as having a zero value for tax purposes; however, the Treasury has not released guidance addressing how valuations are to occur when teams avoid the safe harbor.[16]

This article seeks to resolve the valuation conundrum by proposing the reformation of current tax laws such that trades are taxed in the same manner as before the TCJA. Congress may do so legislatively, or the Treasury may do so through reliance on the open-transaction doctrine. Not returning to the pre-TCJA manner of taxation is illogical for two reasons. First, the IRS is not capable of measuring the value of player contracts or future draft picks, making the administration of current tax laws infeasible. Second, applying the current tax laws to trades is likely to reduce tax revenue because the current tax laws invite teams to reduce their tax liabilities without fundamentally changing their economic posi-

11. *See* Budget Fiscal Year, 2018, Pub. L. No. 115-97, § 13303, 131 Stat. 2054, 2123 (2017) (codified as amended at I.R.C. § 1031). Section 1031 states in relevant part: "No gain or loss shall be recognized on the exchange of *real property* held for productive use in a trade or business or for investment if such *real property* is exchanged solely for real property of like kind . . . ." I.R.C. § 1031(a)(1) (2017) (emphasis added).

12. Rev. Rul. 71-137, 1971-1 C.B. 104 (recognizing trades of football player contracts as exchanges of like-kind property); Rev. Rul. 67-380, 1967-2 C.B. 291 (recognizing trades of baseball player contracts as exchanges of like-kind property); INTERNAL REVENUE SERV., MARKET SEGMENT SPECIALIZATION PROGRAM GUIDELINE: SPORTS FRANCHISES ch. 12 (Aug. 1999), 1999 WL 1221150, at *72 [hereinafter IRS MSSP GUIDELINE] (IRS treated player-for-draft-picks exchanges as like-kind). These rulings are assumed to apply to the NBA, NHL, and MLS. *See* Joseph Mona, *Amortization and Valuation of Intangibles: The Tax Effect Upon Sports Franchises*, 12 LOY. L.A. L. REV. 159, 162 n.27 (1978); Howard Zaritsky, *Taxation of Professional Sports Teams After 1976: A Whole New Ballgame*, 18 WM. & MARY L. REV. 679, 696 (1977).

13. *See* Rev. Rul. 71-137, 171-1 C.B. 104.

14. *See* H.R. REP. NO. 73-704, at 13 (1934) (justifying the non-recognition treatment for like-kind exchanges because, "[i]f all exchanges were made taxable, it would be necessary to evaluate the property received in exchange in thousands of horse trades and similar barter transactions each year").

15. *See id.* at 22–23.

16. Rev. Proc. 2019-18, 2019-18 I.R.B. 1077 §1. *But see* Beate Erwin, *A Fundamental Change of the Professional Sports Landscape Under the 2017 U.S. Tax Reform? The End of Like-Kind Exchanges for U.S. Sports Trades*, 9 GLOBAL SPORTS L. & TAX'N REP. 49, 53 (2018); Jim Tankersley, *A Curveball From the New Tax Law: It Makes Baseball Trades Harder*, N.Y. TIMES (Mar. 19, 2018), https://www.nytimes.com/2018/03/19/us/politics/baseball-tax-law-.html [Permalink unavailable].

tion, a process known as tax arbitrage.[17] These issues are exacerbated by the planning opportunity presented through the zero-value safe harbor.[18] Teams may exploit the safe harbor when it benefits them and avoid the safe harbor when it does not.

To best understand these issues, Part II begins this article by explaining the reason that player contracts and future draft picks are highly valued intangible assets. Next, Part III discusses the tax implications of trading such assets by first summarizing the relevant federal income tax laws. Part III then explains the potential breadth of "gross income" and limits placed on the term—such as by § 1031—in light of principles of equity, efficiency, and administrability. Afterward, Part III offers a brief history of § 1031 and the justification for the provision. Finally, Part III concludes by describing the tax laws applicable to trades between teams, both before and after the TCJA. Then, Part IV critiques the application of current tax laws to trades. Specifically arguing that applying current tax laws to trades is not administrable and invites teams to partake in tax arbitrage, likely resulting in the collection of lower tax revenues because of the TCJA. Part V presents two methods for resolving these issues, either legislatively or through reliance on the open-transaction doctrine. Finally, Part VI concludes this article.

II. PLAYER CONTRACTS AND FUTURE DRAFT PICKS ARE VALUABLE ASSETS

For tax purposes, the Treasury Department views trading players and future draft picks as trading intangible assets. Trading players amounts to trading player contracts,[19] which provides the team that holds the contract the right to receive services from the player.[20] Similarly, trading future draft picks amounts to trading the right to future services from a player.[21] Both types of assets offer teams considerable value.

Teams attach great value to certain player contracts and future draft picks because of the unique economies that exist in each professional sports league.[22] Player contracts create value for a team when the revenue generated by the player exceeds the player's employment costs.[23] Future draft picks create value for a team because they provide the holding team with the sole right to contract with the drafted player.[24] In a free

17. *See* Daniel N. Shaviro, *Selective Limitations on Tax Benefits*, 56 U. CHI. L. REV. 1189, 1244 (1989).

18. *See* Rev. Proc. 2019-18, 2019-18 I.R.B. 1077 § 2.02(3).

19. Rev. Rul. 71-137, 1971-1 C.B. 104; Rev. Rul. 67-380, 1967-2 C.B. 291.

20. Rev. Rul. 67-379, 1967-2 C.B. 127.

21. *See* Charles Dickenson & Zook Sutton, *The Effect of the 1976 Tax Reform Act on the Ownership of Professional Sports Franchises*, 1 HASTINGS COMM. & ENT. L.J. 227, 257–58 n.131 (1977).

22. *See* Paul L.B. McKenney & Eric M. Nemeth, *Tax Law: The Purchase and Sale of a Sports Team: Tax Issues and Rules*, 80 MICH. B.J. 54, 56 (2001).

23. *See* BRADBURY, *supra* note 1, at 9.

24. *See* Cade Massey & Richard H. Thaler, *The Loser's Curse: Decision Making & Market Efficiency in the National Football League Draft*, 59 MGMT. SCI. 1479, 1480 (2013).

market, one would expect that employees would command that their salaries be equal to their worth.[25] Thus, if teams contracted with players in a free market, the player contracts would have no value.[26] However, the markets for signing players in the United States' five major professional sports leagues are not free. Those markets are replete with restraints on player compensation, which cause player contracts and future draft picks to be valuable assets.[27]

All five leagues have created their own economies to promote competitive balance.[28] Competitive balance is essential to team profits because fans become disinterested when certain teams dominate a league.[29] One way leagues promote competitive balance is through collective bargaining agreements, which "govern the employer-employee relationships between the owners of professional sports teams and players' associations."[30] The substance of the agreements vary by league, but a recurrent theme is the goal of preventing teams from being able to "buy wins."[31]

The need to prevent teams from buying wins is a concern to leagues because some teams enjoy revenue that greatly exceeds that of other teams in their league.[32] Teams generate revenue through gate receipts, concessions, parking, broadcasting rights, and advertising.[33] Each source of revenue is a function of the team's fan base, which is a function of the team's location.[34] Teams in large metropolitan areas have a larger potential fan base to pull from, and other teams have become so entrenched in their city's culture that fan support is extraordinary.[35] Without restraints, this disparity could allow the teams with the highest revenues to obtain the best players by offering salaries that exceed what lower revenue teams can afford.[36] Such a scenario would disrupt competitive balance, and league-wide revenue could decrease.[37]

Leagues have enacted many mechanisms to prevent the buying of wins in their respective collective bargaining agreements. Those most relevant

25. *See* Wayne J. Morse, *A Note on the Relationship Between Human Assets and Human Capital*, 48 ACCT. REV. 589, 593 n.6 (1973).

26. *See* BRADBURY, *supra* note 1, at 9.

27. *See* Sherwin Rosen & Allen Sanderson, *Labour Markets in Professional Sports*, 111 ECON. J. F47, F53 (2001).

28. *See id.* at F53–F57.

29. *See* Neale, *supra* note 2, at 2.

30. Paul M. Lopez et al., *Valuation of the Professional Sports Franchise in Bankruptcy: It's a Whole Different Ballgame*, 18 LEWIS & CLARK L. REV. 299, 319 (2014).

31. *See, e.g.*, Lewie Pollis, *Explaining Spending: How the Market Sets the Price of a Win*, BASEBALL PROSPECTUS (Apr. 10, 2014), https://www.baseballprospectus.com/news/article/23269/explaining-spending-how-the-market-sets-the-price-of-a-win/ [https://perma.cc/F6HH-R5SG].

32. For example, the New York Yankees generated approximately $668 million in revenue in 2018, while the Oakland Athletics generated $218 million. *The Business of Baseball*, FORBES, https://www.forbes.com/mlb-valuations/list/#tab:overall [https://perma.cc/9DL9-7BX6] (last visited Sept. 10, 2019).

33. *See* Zaritsky, *supra* note 12, at 685.

34. *See* Lopez et al., *supra* note 30, at 333–34.

35. *Id.* at 334.

36. *See* BERRI ET AL., *supra* note 10, at 9.

37. *See* BRADBURY, *supra* note 1, at 7.

to this article are team salary caps, restraints on player free agency, and maximum salary caps for individual players. All five major professional sports leagues employ some variation of a salary cap, which serves to set a maximum amount that teams can pay the players that make up their rosters.[38] The NFL, NHL, and MLS have "hard" salary caps that forbid teams from going over the set amount.[39] The NBA has a "soft" salary cap that allows teams to exceed the cap in certain circumstances but, outside of those circumstances, the team will incur a "luxury tax."[40] The MLB imposes a luxury tax on teams when the total salary that the team owes its players for the year exceeds a set amount.[41]

Additionally, all five leagues restrict a player's ability to negotiate a salary by limiting the player's right to negotiate to a single team until the player has reached "free agent" status.[42] For example, an MLB player cannot freely negotiate his salary until after serving six years in the league because a single team holds his right to play in the MLB.[43] Thus, if the player is unhappy with the salary offered, league rules limit his choices to either accepting the salary or not playing professional baseball.[44] The NBA and NHL further restrict player compensation by imposing a limit on the maximum amount that a team can pay an individual player.[45]

Together, these restrictions on player salaries contribute to the high possibility that teams will pay players less than the revenue they generate for their team, giving rise to player contracts and future draft picks with

38. *See* Helmut M. Dietl et al., *Salary Cap Regulation in Professional Team Sports*, 30 CONTEMP. ECON. POL'Y 307, 307 (2012); *see also* Jim Pagels, *Are Salary Caps for Professional Athletes Fair?*, PRICEONOMICS (Aug. 19, 2014), https://priceonomics.com/are-salary-caps-for-professional-athletes-fair/ [https://perma.cc/XEM2-P3AK] (explaining the various salary cap mechanisms in each professional sports league).

39. NAT'L HOCKEY LEAGUE & NAT'L HOCKEY LEAGUE PLAYERS' ASS'N, COLLECTIVE BARGAINING AGREEMENT BETWEEN NATIONAL HOCKEY LEAGUE AND NATIONAL HOCKEY LEAGUE PLAYERS' ASSOCIATION: SEPTEMBER 16, 2012–SEPTEMBER 15, 2022, art. 50, § 50.5 (Feb. 15, 2013), https://www.nhlpa.com/the-pa/cba [https://perma.cc/3PAU-4LGR] [hereinafter NHL COLLECTIVE BARGAINING AGREEMENT]; NAT'L FOOTBALL LEAGUE & NAT'L FOOTBALL LEAGUE PLAYERS ASS'N, COLLECTIVE BARGAINING AGREEMENT, art. 12, § 6 (Aug. 4, 2011), https://nfllabor.files.wordpress.com/2010/01/collective-bargaining-agreement-2011-2020.pdf [https://perma.cc/2TL3-3L7M]; *MLS Roster Rules and Regulations 2018*, MLS: COMMS. (Mar. 2, 2018), https://www.mlssoccer.com/league/official-rules/mls-roster-rules-and-regulations [https://perma.cc/84WH-TLQ7] [hereinafter *MLS Roster Rules*].

40. NAT'L BASKETBALL ASS'N & NAT'L BASKETBALL PLAYERS ASS'N, 2017 NBA-NBPA COLLECTIVE BARGAINING AGREEMENT (EFFECTIVE AS OF 7/1/2017), art. 7, § 2(a) (Jan. 19, 2017), https://nbpa.com/cba/ [https://perma.cc/EG7X-ZSP6] [hereinafter NBA COLLECTIVE BARGAINING AGREEMENT].

41. MAJOR LEAGUE BASEBALL & MAJOR LEAGUE BASEBALL PLAYERS ASS'N, COLLECTIVE BARGAINING AGREEMENT 2017-2021, art. 23 (2017), http://www.mlbplayers.com/ViewArticle.dbml?DBOEM_ID=34000&ATCLID=211078089 [https://perma.cc/8YZP-SENG] [hereinafter MLB COLLECTIVE BARGAINING AGREEMENT].

42. *See* Jonathan B. Goldberg, *Player Mobility in Professional Sports: From the Reserve System to Free Agency*, 15 SPORTS L.J. 21, 41–56 (2008) (providing an overview of free agency rules in professional sports leagues).

43. *See* BRADBURY, *supra* note 1, at 6–8.

44. *See id.*

45. NBA COLLECTIVE BARGAINING AGREEMENT, *supra* note 40, at art. 2, § 7; NHL COLLECTIVE BARGAINING AGREEMENT, *supra* note 39, at art. 50, § 50.6.

considerable value.[46] However, the potential also exists for a player contract with a negative value.[47] Player contracts have a negative value when a player's salary exceeds the player's worth.[48] Releasing the player may relieve a team from any non-guaranteed salary obligations.[49] Yet, releasing a player with guaranteed salary obligations would give rise to "dead money," an obligation to pay players that are no longer on a team's roster.[50] Unlike player contracts, future draft picks cannot have a negative value because a team can always choose not to draft or contract with certain players.[51]

III. FEDERAL INCOME TAX LAWS AND THEIR APPLICATION TO TRADES BETWEEN TEAMS

Sales or exchanges of property with considerable value may lead to considerable tax consequences. Before the TCJA, taxes posed no obstacle to trades between sports teams, which was a good thing considering a team general manager would likely balk at needing to consult tax counsel before each trade.[52] Now, such consultation should occur because every trade could cause considerable tax consequences.[53] The frequency of trades heightens the need for consultation. In 2018, teams in the United States' five professional sports leagues engaged in 441 trades, involving 875 players and 249 future draft picks or similar assets.[54] Thus, team own-

46. *See* McKenney & Nemeth, *supra* note 22, at 56.
47. *See* BRADBURY, *supra* note 1, at 16.
48. *See id.* at 15–16.
49. *See id.* at 16.
50. *See* Scott Croker, *15 Biggest Dead Money Salaries in MLB*, BUS. PUNDIT (May 23, 2016), http://www.businesspundit.com/15-biggest-dead-money-salaries-in-mlb-05-2016/ [https://perma.cc/F89S-3KK5]; *see also* LEWIS, *supra* note 6, at 150 (describing the deal in which the New York Yankees paid half of David Justice's $3.5 million-dollar salary for him to play for the Oakland Athletics).
51. *See* Matthew Murphy, *How Much is a Draft Pick Worth in 2014?*, HARDBALL TIMES (May 21, 2014) https://tht.fangraphs.com/how-much-is-a-draft-pick-worth-in-2014/ [https://perma.cc/KG94-Q2CD].
52. *See Inquiry into Professional Sports: Hearings Before the H. Select Comm. on Prof. Sports*, 94th Cong. 209 (1976) (statement of Robert O. Swados, Special Tax Counsel, NHL) (speaking as an owner of an NHL team: "I, personally, would not relish informing my general manager . . . that he must consult tax counsel every time he seeks to . . . trade a player.").
53. *See* Becky Sullivan & Alisa Chang, *Tax Change Delivers a Blow to Professional Sports*, NPR (Mar. 21, 2018), https://www.npr.org/2018/03/21/595610804/professional-sports-leagues-go-head-to-head-with-new-tax-code [https://perma.cc/4Y7D-N5UC].
54. *MLB Transactions*, SPOTRAC, https://www.spotrac.com/nhl/transactions/2018/trade/ [https://perma.cc/W6ZL-RUZM] (last visited Sept. 10, 2019) (MLB teams engaged in 199 trades involving 423 players, 4 future draft picks, and 24 future considerations); *MLS Transactions*, SPOTRAC, https://www.spotrac.com/mls/transactions/2018/trade/ [https://perma.cc/Q6L9-528N] (last visited Sept. 10, 2019) (MLS teams engaged in 39 trades involving 50 players, 15 future draft picks, 1 future consideration, and 3 international roster spots); *NBA Transactions*, SPOTRAC, https://www.spotrac.com/nba/transactions/2018/all/trade/ [https://perma.cc/E283-VMEY] (last visited Sept. 10, 2019) (NBA teams engaged in 51 trades involving 126 players, 55 future draft picks, 2 draft rights to specific players, and 1 future consideration); *NFL Transactions*, SPOTRAC, https://www.spotrac.com/nfl/transactions/2018/trade/ [https://perma.cc/V63J-YCG5] (last visited Sept. 10, 2019) (NFL teams engaged in 62 trades involving 71 players, 99 future draft picks, and 1 "future considera-

ers and general managers would be well-served by reviewing the basic rules of federal income taxation. This part of the article does just that.

A. Federal Income Tax Fundamentals

The United States federal government levies taxes on income.[55] More specifically, the federal government taxes "taxable income," which the Code defines to mean "gross income minus the deductions allowed by this chapter."[56] The Code defines gross income as "all income from whatever source derived."[57] Neither the Code nor the Treasury Regulations define income, but the Supreme Court has explained that income includes all "instances of undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion."[58] The Treasury Regulations add that "[g]ross income includes income realized in any form, whether in money, property, or services."[59] In sum, all clearly realized accessions to wealth are taxable, regardless of form, unless excluded by law.[60]

Tax laws slightly complicate the process of determining tax liabilities associated with dealings in property because not all money, property, or services received in exchange for property necessarily result in gross income.[61] A taxpayer must first recover the cost of the property before any increase in wealth is realized and, further, that increase must be recognized for tax purposes.[62] The Code refers to the increase or decrease in wealth from the disposition of property as a gain or loss.[63] A gain is "the excess of the amount realized [from the disposition] over the [property's] adjusted basis . . . ."[64] A loss is "the excess of the [property's] adjusted basis . . . over the amount realized" from the disposition.[65]

The Code further defines both "amount realized" and "basis."[66] "Amount realized" is defined as "the sum of any money received plus the fair market value of the property (other than money) received."[67] A property's "fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being

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tion"); *NHL Transactions*, Spotrac, https://www.spotrac.com/nhl/transactions/2018/trade/ [https://perma.cc/HM7S-QPTA] (last visited Sept. 10, 2019) (NHL teams engaged in 90 trades involving 200 players, 71 future draft picks, and 4 future considerations).

55. *See* Nancy H. Kaufman, *Fairness and the Taxation of International Income*, 29 Law & Pol'y Int'l Bus. 145, 152 (1998).

56. I.R.C. § 63(a) (2017).

57. *Id.* § 61(a).

58. Comm'r v. Glenshaw Glass Co., 348 U.S. 426, 431 (1955).

59. Treas. Reg. § 1.61-1(a) (1957).

60. *See* I.R.C. § 63(a); Treas. Reg. § 1.61-1(a) (1957).

61. *See* I.R.C. §§ 61(a)(3), 1001(a).

62. *See* Bryan T. Camp, *Play's the Thing: A Theory of Taxing Virtual Worlds*, 59 Hastings L.J. 1, 15 (2007).

63. I.R.C. § 1001(a).

64. *Id.*

65. *Id.*

66. *Id.* §§ 1001(b), 1012(a).

67. *Id.* § 1001(b).

under any compulsion to buy or sell and both having reasonable knowledge of relevant facts."[68] Determining the fair market value is a question of fact, and in "rare and extraordinary" circumstances, the law may deem that a property does not have a fair market value.[69] If a seller receives services in an exchange, those services have a value consistent with the retail prices normally charged for such services[70] and the fair market value of the property transferred.[71]

The term "basis" essentially "refers to the way in which the tax system tracks what part of the value of a piece of property will not constitute gross income."[72] The Code describes a property's basis to "be the cost of such property,"[73] which may change because of additional investments or allowable deductions.[74] A taxpayer's cost basis in a property varies according to how the taxpayer obtained the property.[75]

Relevant to trades between teams, the basis in property received in an exchange is generally the fair market value of that property.[76] If the fair market value of the property received "cannot be determined with reasonable accuracy," then the fair market value of the property transferred may be used, so long as the transaction is at arms-length.[77] If the fair market value of each property cannot "be ascertained with a reasonable degree of accuracy, the taxpayer is entitled to carry over the [basis of the property transferred] as the cost basis of the [property received]."[78] A taxpayer's cost basis in a property may then be increased "for expenditures, receipts, losses, or other items, properly chargeable to capital account."[79] The cost basis may also be decreased to account for "exhaustion, wear and tear, obsolescence, amortization, and depletion."[80]

An amount realized that exceeds the property's adjusted basis does not necessarily result in a taxable gain.[81] As a general rule, the Code recognizes all gains or losses for tax purposes unless stated otherwise.[82] How-

68. Treas. Reg. § 1.170A-1 (as amended in 2018).
69. *Id.* § 1.1001-1(a) (as amended in 2017).
70. *See* Rooney v. Comm'r, 88 T.C. 523, 528 (1987).
71. *See* United States v. Davis, 370 U.S. 65, 72 (1962). *But see* Seas Shipping Co. v. Comm'r, 371 F.2d 528, 529–30 (2d Cir. 1967) (noting the "dangers in evaluating the consideration involved in one side of a barter by determining the worth of the consideration on the other side").
72. Camp, *supra* note 62, at 16.
73. I.R.C. § 1012(a) (2017).
74. *Id.* §§ 1011(b), 1016(a)(1)–(2).
75. *See generally* U.S. DEP'T OF THE TREASURY, INTERNAL REVENUE SERV., PUB. 551, BASIS OF ASSETS 2 (2018), https://www.irs.gov/pub/irs-pdf/p551.pdf [https://perma.cc/HCA2-2T5U] (providing a detailed explanation for determining a taxpayer's basis in an asset).
76. *See Davis*, 370 U.S. at 73; Phila. Park Amusement Co. v. United States., 126 F. Supp. 184, 188 (1954).
77. *Phila. Park*, 126 F. Supp. at 189.
78. *Id.*
79. I.R.C. § 1016 (a)(1).
80. *Id.* § 1016 (a)(2).
81. *See, e.g.*, *id.* § 1031.
82. *See id.* § 1001(c).

ever, non-recognition provisions exist throughout the Code,[83] each serving certain policy objectives.[84] Although, after the TCJA, a non-recognition provision pertaining to trades between teams does not exist, unless the opposing team owners also happen to be spouses.[85]

Since marriage between the owners of opposing teams seems unlikely, teams will probably incur tax consequences whenever a gain or loss is realized in a trade. The exact tax consequences vary according to the character of the recognized gain or loss. Thus, teams must characterize gains to determine the rate at which they will be taxed. This is a complex topic, but broadly speaking, gains from dealings in property are either taxed as ordinary income, with the current maximum tax rate being 37%,[86] or at a preferential rate.[87]

Gain incurred from trades between teams may receive preferential treatment because player contracts are § 1231 assets if held for over one year.[88] However, the gain may also be subject to the recapture rules of § 1245.[89] Section 1245 recaptures gain attributed to depreciation or amortization deductions and taxes that amount as ordinary income.[90] Section 1231 provides the rules for any uncharacterized gain that may remain. If all of a taxpayer's § 1231 gains exceed the § 1231 losses for the taxable year, then the gains and losses become long-term capital gains and losses,[91] which results in net gains from player contracts being taxed at a maximum rate of 23.8%.[92] If all of a taxpayer's § 1231 losses exceed the

83. *See, e.g.*, *id.* §§ 351(a), 751(a).

84. For example, "the purpose of § 721 is to facilitate the flow of property from individuals to partnerships that will use the property productively . . . [by preventing] the mere change in form from precipitating taxation." Superior Trading, LLC v. Comm'r, 137 T.C. 70, 86 (2011) (quoting United States v. Stafford, 727 F.2d 1043, 1048, 1053 (11th Cir. 1984)).

85. *See* I.R.C. § 1041(a)(1) ("No gain or loss shall be recognized on a transfer of property from an individual to . . . a spouse.").

86. *Id.* §§ 1(a)–(d), (j)(2).

87. *Compare* I.R.C. §§ 1(a)–(d), (j)(2) (providing tax rates for ordinary income through 2025), *with* I.R.C. §§ 1(h), (j)(5) (providing tax rates for capital gains through 2025).

88. Rev. Rul. 71-137, 1971-1 C.B. 104; Rev. Rul. 67-380, 1967-2 C.B. 291; *see also* I.R.C. § 1231(a) (providing rules for when a taxpayer's gains and losses derived from all dealings in § 1231 assets for the taxable year are treated as long-term capital gain and losses or as an ordinary gains and losses); Hollywood Baseball Ass'n v. Comm'r, 423 F.2d 494, 497 (9th Cir. 1970) ("[T]he Tax Court properly held that . . . the player contracts were not primarily held for sale to customers in the ordinary course of business.").

89. The recapture rules of § 1245 require a taxpayer to characterize gain as ordinary income when it is attributable to depreciation or amortization of property. *See* I.R.C. § 1245(a). The section does not explicitly include intangible property that is amortized ratably over the life of the property in its definition of § 1245 property. *See id.* §§ 1245(a)(3), (b)(8). However, the inclusion of both all depreciable tangible property and all § 197 intangible property makes the inclusion of depreciable contracts likely. *See id.* §§ 1245(a)(3), (b)(8).

90. *Id.* § 1245(a).

91. *Id.* § 1231(a)(1).

92. *Id.* §§ 1(h)(3), 1411. However, individual taxpayers with taxable income of less than $452,800 are currently taxed at a rate of 15% on adjusted net capital gains. *Id.* § 1(j)(5)(B)(ii).

§ 1231 gains for the taxable year, then the gains and losses become ordinary gains and losses.[93]

B. The Potential Breadth of "Gross Income" and Some Limits

The existence of non-recognition provisions in the Code illustrates that not all accessions to wealth are gross income, despite the term's broad definition. Nonetheless, most tax scholars agree that the Haig-Simons definition of income is the ideal definition of income.[94] Under the Haig-Simons definition, "[p]ersonal income may be defined as the algebraic sum of (1) the market value of rights exercised in consumption and (2) the change in the value of the store of property rights between the beginning and end of the period in question."[95] In other words, income is the change in a person's ability to consume during a given period.[96] The Constitution gives Congress the power to tax the full reach of the Haig-Simons definition of income by stating, "Congress shall have power to lay and collect taxes on incomes, from whatever source derived."[97] Indeed, Congress intended its definition of gross income to be as broad as constitutionally allowed.[98] However, the potential breadth of gross income commonly gives way to promote competing policy, which includes addressing issues of equity, efficiency, and administrability.[99]

1. Required Deviations from the Haig-Simons Definition of Income

Deviations from the Haig-Simons definition of income often occur because tax laws must be administrable.[100] This requirement likely explains the most significant deviation of Haig-Simons in the United States' federal income tax system: the realization doctrine.[101] The realization doctrine prevents accessions to wealth from being taxed until an objective, identifiable event has taken place.[102] The doctrine eliminates the need to value property periodically and makes many accessions to wealth easier to measure because sellers often dispose of property for money.[103]

Administrability also justifies why the IRS sometimes deviates from

93. *Id.* § 1231(a)(2).

94. *See* Christopher H. Hanna, *Tax Theories and Tax Reform*, 59 SMU L. Rev. 435, 436 (2006).

95. Henry C. Simons, Personal Income Taxation: The Definition of Income as a Problem of a Fiscal Policy 50 (1938).

96. *See* Molly F. Sherlock & Donald J. Marples, Cong. Research Serv., R45145, Overview of the Federal Tax System in 2018, at 2 (2018).

97. U.S. Const. amend. XVI.

98. *See* H.R. Rep. No. 83-1337, at A18–19 (1954); S. Rep. No. 83-1622, at 168 (1954).

99. *See* Hanna, *supra* note 94, at 436–37.

100. *See* Camp, *supra* note 62, at 25.

101. *See* Hanna, *supra* note 94, at 436–37; *see also* Camp, *supra* note 62, at 24 ("This economic view of income does not translate well into tax law because it ignores the practical requirement that income be something that can be reliably measured, reported, and paid.").

102. *See* Camp, *supra* note 62, at 29–30.

103. *See* Deborah L. Paul, *Another Uneasy Compromise: The Treatment of Hedging in a Realization Income Tax*, 3 Fla. Tax Rev. 1, 18 (1996).

Congress's broad proclamation that "gross income means all income."[104] Examples of such deviations include the non-taxation of imputed income[105] and the receipt of frequent flyer miles derived from business travel.[106] Imputed income is the "investment of capital or performance of services for one's own personal or family use."[107] A person that buys a house outright and lives in the house has imputed income equal to the house's rental value.[108] Likewise, a person that consumes goods created through the person's own efforts or that provides a service to themselves has imputed income equal to their value.[109] The federal government taxes neither type of imputed income.[110] Tax scholars rationalize this treatment by noting the reporting problems that would plague taxpayers and the IRS's inability to enforce compliance or measure accessions to wealth.[111] Similar reasoning justifies the IRS's decision to not assert an understated federal tax liability when a taxpayer does not report the "receipt or personal use of frequent flyer miles . . . attributable to the taxpayer's business or official travel."[112]

Administrability and potential public backlash explain why the IRS does not enforce a tax on fans that catch a home run baseball, at least until the fan sells the ball.[113] When a fan catches a home run ball, they have experienced an undeniable accession to wealth, clearly realized, and over which they have complete dominion.[114] The IRS's enforcement of such a tax would be equitable because a taxpayer that similarly comes into possession of found property is taxed on gain equal to the property's value.[115] Taxing the fan would also be economically efficient because taxing accessions to wealth equally does not encourage certain behaviors over others.[116] Still, to the IRS, administrability trumps equity and efficiency because of enforcement and valuation issues.[117]

Further, the IRS knows of the public backlash likely to occur should baseball fans incur a tax liability at the moment of catching a home run

104. I.R.C. § 61(a) (2017); Alice G. Abreu & Richard K. Greenstein, *Defining Income*, 11 FLA. TAX REV. 295, 344 (2011).

105. Morris v. Comm'r, 9 B.T.A. 1273, 1278 (1928); WILLIAM D. ANDREWS, BASIC FEDERAL INCOME TAXATION 68–71 (5th ed. 1999).

106. I.R.S. Announcement 2002-18, 2002-10 I.R.B. 621 (2002).

107. ANDREWS, *supra* note 105, at 68.

108. *Id.*

109. Hanna, *supra* note 94, at 437 n.19.

110. *See Morris*, 9 B.T.A. at 1278.

111. Steve R. Johnson, *Imputed Rental Income: Reality Trumps Theory*, *in* CONTROVERSIES IN TAX LAW: A MATTER OF PERSPECTIVE 65, 79–89 (Anthony C. Infanti ed., 2015).

112. I.R.S. Announcement 2002-18, 2002-10 I.R.B. 621 (2002).

113. *See* I.R.S. News Release IR-98-56 (Sept. 8, 1998); *see also* Tom Herman, *The Big Catch Could Have a Big Catch*, WALL ST. J. (July 25, 2007), https://www.wsj.com/articles/SB118532191532076935 [https://perma.cc/2SZF-YFS7] (noting that no formal IRS guidance addresses taxation of home run baseballs and that, while tax scholars disagree on the issue, "it's highly unlikely that the IRS would be willing to risk the wrath of a baseball-loving nation by taxing the fan right away").

114. *See* Comm'r v. Glenshaw Glass Co., 348 U.S. 426, 431 (1955).

115. *See* Cesarini v. United States, 428 F.2d 812, 813–14 (6th Cir. 1970).

116. *See* Abreu & Greenstein, *supra* note 104, at 344 n.175.

117. *See id.* at 344.

ball.[118] In September 1998, an IRS spokesperson became disdained by baseball fans everywhere when he stated that a fan would incur a gift tax by catching Mark McGwire's record-setting home run ball and promptly returning it to McGwire.[119] One congressman stated that taxing a fan for catching a record-setting baseball is "a prime example of what is wrong with our current tax code."[120] Another congressman introduced a bill "[t]o clarify the income and gift tax consequences of catching and returning record home run baseballs."[121] Congress did not enact the bill, likely because the IRS quickly reversed its position by stating that a fan "who catches a home run ball and immediately returns it . . . would not have taxable income."[122] In doing so, the IRS carefully noted that the tax consequences could be different if the fan sold the ball[123] but has issued no further guidance on the issue.[124]

2. Desired Deviations from the Haig-Simons Definition of Income

Congress intentionally deviates from the Haig-Simons definition of income to include tax expenditures in the Code.[125] Tax expenditures are "revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability."[126] The purpose of their existence is to promote certain policy objectives.[127] Exclusions from the Code's definition of gross income are types of tax expenditures that most blatantly deviate from the Haig-Simons definition of income.[128]

Non-recognition provisions are a tax expenditure that deviate less blatantly from the Haig-Simons definition of income.[129] This tax expenditure is less evasive because a taxpayer will generally be taxed on the unrecog-

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118. *See* Herman, *supra* note 113.

119. Heidi Glenn, *IRS Hits Foul Ball in Middle of Home Run Race*, TAX NOTES (Sept. 9, 1998), https://www.taxnotes.com/tax-notes-today-federal/budgets/irs-hits-foul-ball-middle-home-run-race/1998/09/09/11vg3?highlight=IRS%20hits%20foul%20ball%20in%20mid [https://perma.cc/DT43-ZA2U].

120. Andrew D. Appleby, *Ball Busters: How the IRS Should Tax Record-Setting Baseballs and Other Found Property Under the Treasure Trove Regulation*, 33 VT. L. REV. 43, 47 (2008).

121. H.R. 4522, 105th Cong. (1998).

122. I.R.S. News Release IR-98-56 (Sept. 8, 1998).

123. *Id.*

124. *See* Appleby, *supra* note 120, at 48.

125. *See* DONALD J. MARPLES, CONG. RESEARCH SERV., R44012, TAX EXPENDITURES: OVERVIEW AND ANALYSIS 2 (2015). For a list and the predicted cost of every tax expenditure for 2017 through 2018, see STAFF OF JOINT COMM. ON TAX'N, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2017–2021, 115TH CONG., JCX-34-18, at 5 (Comm. Print 2018).

126. 2 U.S.C. § 622 (2017).

127. *See* MARPLES, *supra* note 125, at 12.

128. *See* SHERLOCK & MARPLES, *supra* note 96, at 2. For a list of items specifically excluded from gross income, see I.R.C. §§ 101–139G (2017).

129. *See* Boris I. Bittker, *A "Comprehensive Tax Base" as a Goal of Income Tax Reform*, 80 HARV. L. REV. 925, 980, 981 (1967).

nized gain in the future.[130] One example of such a tax expenditure is § 1031, which affords non-recognition treatment to exchanges of "like-kind" property.[131] Like other non-recognition provisions, § 1031 allows a taxpayer to defer any realized gain beyond the year of the exchange.[132] Congress desires the deviation because it promotes exchanges of property that may not occur in the presence of a tax.[133]

C. A Brief History of § 1031 and Justification for Like-Kind Treatment

Section 1031 of the Code allows taxpayers to exchange qualifying "like-kind" property that has been "held for productive use in a trade or business or for investment" without gain or loss being recognized.[134] The Treasury views properties as like-kind when they have the same "nature or character" without regard to their individual "grade or quality."[135] The Code does not prevent the gain or loss involved in a like-kind exchange from ever being recognized.[136] Instead, the unrecognized gain or loss is merely deferred until taxpayers sell acquired property because their basis in acquired property becomes that of the property transferred.[137]

1. Section 1031 Before the TCJA

A section concerning the non-recognition treatment of like-kind exchanges has existed in the Code since 1921.[138] In that year, a depression plagued the United States, and Congress became concerned with maintaining a balanced federal budget.[139] Congress evidenced this concern by explaining the special treatment afforded to like-kind exchanges will "increase the revenue by preventing taxpayers from taking colorable losses in wash sales and other fictitious exchanges."[140] Now that the United States is no longer in a depression, some commentators have argued that a fear of overwhelming loss recognition is an unpersuasive justification for the special treatment afforded like-kind exchanges.[141] Still, tax laws should not permit taxpayers to significantly reduce their tax liability with-

130. *See, e.g.*, I.R.C. § 1031(d).
131. *Id.* § 1031.
132. *See* U.S. Dep't of the Treasury, Like-Kind Exchanges 2 (2014), https://www.treasury.gov/resource-center/tax-policy/tax-analysis/Documents/Like-Kind-Exchange-2014.pdf [https://perma.cc/6986-UTEG] [hereinafter U.S. Dep't of the Treasury, Like-Kind Exchanges].
133. *See* H.R. Rep. 67-350, at 10 (1921); S. Rep. No. 67-275, at 11 (1921).
134. I.R.C. § 1031(a)(1).
135. Treas. Reg. § 1.1031(a)-1 (as amended in 1991).
136. *See* Erik M. Jensen, *The Uneasy Justification for Special Treatment of Like-Kind Exchanges*, 4 Am. J. Tax Pol'y 193, 196 (1985).
137. *See* I.R.C. § 1031(d).
138. Revenue Act of 1921, Pub. L. No. 67-98, § 202(c)(1), 42 Stat. 227, 230 (1921).
139. *See* James Grant, The Forgotten Depression 71–72 (2015).
140. H.R. Rep. No. 67-350, at 10 (1921); S. Rep. No. 67-275, at 11–12 (1921). Congress reiterated this concern when declining to repeal the like-kind provision in 1934. H.R. Rep. No. 73-704, at 564 (1934) ("If all exchanges were made taxable . . . claims for theoretical losses would probably exceed any profits.").
141. *See, e.g.*, Jensen, *supra* note 136, at 212–13.

out fundamentally changing their economic position.[142]

Other policy considerations explain why the provision has remained mostly unchanged from 1924,[143] until the TCJA limited like-kind treatment to real property.[144] Specifically, administrative considerations, the promotion of economic efficiency, and the continuity of investment explain the special treatment afforded like-kind exchanges.[145] Congress and courts have cited administrative considerations, since 1934, when Congress declined to eliminate the provision from the Code.[146] There, Congress feared the difficulty of valuing property that taxpayers had exchanged for similar property would cause administrative costs to exceed potential revenue.[147]

Some courts and commentators have argued that administrative difficulty is not a proper justification for § 1031 on grounds that parties to an exchange necessarily value the property before the exchange occurs.[148] This criticism is unfounded. Parties engage in exchanges because "each side wants the specific goods the other side offers."[149] In fact, exchanges often occur without regard to the value of goods involved; instead, the crux of the exchange is that the goods being received have a higher marginal utility to the recipient than the goods being transferred.[150]

Moreover, Congress has cited the promotion of economic efficiency as justification for the special treatment afforded like-kind exchanges.[151] Congress believed removing tax obstacles from certain transactions

142. *See* discussion *infra* Part IV.B.

143. Revenue Act of 1924, Pub. L. No. 68-176, § 203(b)(1), 43 Stat. 253, 256; *see also* Marjorie E. Kornhauser, *Section 1031: We Don't Need Another Hero*, 60 S. CAL. L. REV. 397, 405 (1987) (explaining Congress's changes to the like-kind rules).

144. Budget Fiscal Year, 2018, Pub. L. No. 115-97, § 13303(a), 131 Stat. 2054, 2123 (2017) (codified as amended at I.R.C. § 1031). For a detailed summary of the legislative history of § 1031, see John R. Dorocak, *Protecting Real Estate Investors: The Fight to Maintain the Like-Kind Standard for Exchanges under I.R.C. Section 1031—"You Don't have to Call Me Darling, Darling"*, 33 SANTA CLARA L. REV. 571, 592–94 (1993); Kornhauser, *supra* note 143, at 400–07 nn.8–19.

145. *See* Jensen, *supra* note 136, at 199.

146. H.R. REP. NO. 73-704, at 6 (1934); *see also* STAFF OF JT. COMM. ON TAX'N, 98TH CONG., GENERAL EXPLANATION OF THE REVENUE PROVISIONS OF THE DEFICIT REDUCTION ACT OF 1984, JCS-41-84, at 245 (Comm. Print 1985) ("The special treatment of like-kind exchanges has also been justified from an administrative standpoint because of the difficulty of valuing property which is exchanged solely or primarily for similar property."); Century Elec. Co. v. Comm'r, 192 F.2d 155, 159 (8th Cir. 1951) ("[Congress] was concerned with the administrative problem involved in the computation of gain or loss in transactions of the character with which the [now § 1031] deals." In such transactions "the market value of the properties of like kind involved in the transfer does not enter into the question.").

147. *See* H.R. REP. NO. 73-704, at 13.

148. *See* Leslie Co. v. Comm'r, 539 F.2d 943, 948–49 (3d Cir. 1976); Jordan Marsh Co. v. Comm'r, 269 F.2d 453, 456 (2d Cir. 1959); Jensen, *supra* note 136, at 208 n.74.

149. George Dalton, *Barter*, 16 J. ECON. ISSUES 181, 181 (1982).

150. *See* Caroline Humphrey & Stephen Hugh-Jones, *Introduction* to BARTER, EXCHANGE AND VALUE: AN ANTHROPOLOGICAL APPROACH 1, 9 (Caroline Humphrey & Stephen Hugh-Jones eds., 1992) ("[I]n barter . . . [e]ven if some notion of monetary value hovers in the background, . . . it would be a mistake to think that the consumption or use values of the objects are measurable by some common, abstract standard held in the heads of the two parties.").

151. *See* H.R. REP. NO. 67-350, at 10 (1921).

would "permit business to go forward with the readjustments required by existing conditions."[152] Taxing like-kind exchanges could cause taxpayers to hold onto assets they would normally sell, locking in capital and preventing it from being used in an economically efficient manner.[153] After all, reinvestment after the disposal of property may not occur when taxes make the taxpayer unable to purchase property of comparable value.[154]

The strongest justification for the non-recognition treatment of like-kind exchanges is continuity of investment.[155] This theory justifies § 1031 because "the taxpayer's economic situation after the exchange is fundamentally the same as it was before the transaction occurred."[156] In other words, Congress believed it would be unfair to impose a tax when the taxpayer's original investment remains invested in a substantially similar property.[157]

2. Section 1031 After the TCJA

Congress likely considered the justifications for § 1031 when deciding to limit like-kind treatment to real property as part of the TCJA.[158] The official reason for the change is that the "increased and expanded expensing under sections 168(k) and 179 for tangible personal property and certain building improvements" makes like-kind treatment for non-real property unnecessary.[159] Section 168(k) provides taxpayers with an additional deduction allowance for qualifying property,[160] and § 179 allows taxpayers to expense the cost of qualifying property subject to a dollar amount limitation.[161] Notably, § 168(k) allows a 100% deduction allowance for the year qualifying property is placed in service until January 1, 2023.[162] Increased expensing justifies the repeal of non-recognition for *certain* like-kind exchanges because the expensing will help offset any incurred tax liabilities and will encourage investment in all types of prop-

152. *Id.* at 176; S. REP. NO. 67-275, at 189 (1921).

153. *See* Kornhauser, *supra* note 143, at 408. *But see* Jensen, *supra* note 136, at 214 (arguing that the non-recognition treatment of like-kind exchanges is actually inefficient because it "encourages overinvestment in property suitable for such exchanges").

154. U.S. DEP'T OF THE TREASURY, LIKE-KIND EXCHANGES, *supra* note 132, at 2.

155. Jensen, *supra* note 136, at 199.

156. Koch v. Comm'r, 71 T.C. 54, 63 (1978); *see also* Leslie Co. v. Comm'r, 539 F.2d 943, 949 (3d Cir. 1976) (adopting continuity of investment as justification for § 1031); Jordan Marsh Co. v. Comm'r, 269 F.2d 453, 456 (2d Cir. 1959) ("Congress was primarily concerned with the inequity . . . of forcing a taxpayer to recognize a paper gain which was still tied up in a continuing investment of the same sort."); Portland Oil Co. v. Comm'r, 109 F.2d 479, 488 (1st Cir. 1940) ("It is the purpose of [now § 1031] to [prevent] recognition of a gain, or . . . loss, in certain transactions where gain or loss may have accrued in a constitutional sense, but where in a popular and economic sense there has been a mere change in the form of ownership.").

157. H.R. REP. NO. 73-704, at 13 (1934).

158. *See* Budget Fiscal Year, 2018, Pub. L. No. 115-97, § 13303(a), 131 Stat. 2054, 2123 (2017) (codified as amended at I.R.C. § 1031); H.R. REP. NO. 115-409, at 255 (2017).

159. H.R. REP. NO. 115-409, at 255.

160. I.R.C. § 168(k) (2017).

161. *Id.* §§ 179(a)–(b).

162. *Id.* § 168(k)(6)(A)(i).

erty, rather than only property that qualifies for like-kind exchanges.[163]

However, Congress's reason for limiting like-kind treatment to real property does not justify the reason for excluding property that falls outside the scope of § 168(k) or § 179 from non-recognition treatment.[164] In fact, most types of intangible property do not qualify for increased expensing under those sections.[165] This leaves intangible property owners with pre-TCJA depreciation schedules and no ability to make like-kind exchanges.[166]

Congress may not have considered exchanges of like-kind intangible property when revising § 1031.[167] This oversight seems likely considering an overwhelming majority of like-kind exchanges before the TCJA involved real estate and vehicles,[168] the latter falling within the purview of § 168(k) and § 179.[169] Still, teams engage in hundreds of trades each year,[170] involving hundreds of intangible assets that do not qualify for increased expensing.[171]

D. Taxing Trades Between Teams

For tax purposes, teams that trade players and future draft picks are trading intangible assets. Like dispositions of other types of property, teams must first recover the cost of the player contract or future draft pick before any increase in wealth is realized and, further, that increase must be recognized for a tax liability to result.[172] The cost of a player contract includes the "(a) amounts paid or incurred upon the purchase of a player contract, and (b) bonuses paid to players for signing player contracts."[173] Teams must capitalize such cost because the contract provides a benefit that extends for the duration of the contract. The team may then recover the cost over the contract's term, unless the contract is obtained

163. *See* Emily L. Foster, *Advocates Aim to Preserve Like-Kind Exchange in Tax Reform*, Tax Notes (May 3, 2017), https://www.taxnotes.com/editors-pick/advocates-aim-preserve-kind-exchange-tax-reform [https://perma.cc/8MU2-ZW2N].

164. *See* H.R. Rep. No. 115-409, at 255; *see also* I.R.C. §§ 168(k)(2), 179(d)(1) (excluding most types of intangible property from their scope).

165. *See* I.R.C. §§ 168(k)(2), 179(d)(1).

166. *See* Nathan J. Richman, *Proposed Like-Kind Exchange Limitation Raises Mismatch Concerns*, Tax Notes (Nov. 7, 2017), https://v6k8u5d3.stackpathcdn.com/wp-content/uploads/2017/11/Proposed-Like-Kind-Exchange-Limitation-Raises-Mismatch-Concerns_Richman_TaxNotes-11-7-17.pdf [https://perma.cc/2EG3-BL23].

167. *See* Paul Jacobs, *A Legislative Error to Open Baseball Season*, Palisades Hudson Fin. Group (Mar. 29, 2018), https://www.palisadeshudson.com/2018/03/a-legislative-error-to-open-baseball-season/ [https://perma.cc/9VSP-PXKU].

168. *See* U.S. Dep't of the Treasury, Like-Kind Exchanges, *supra* note 132, at 1, 3.

169. *See* I.R.C. §§ 168(k)(2), 179(d)(1); *see also* Hertz Global Holdings, Inc., Annual Report (Form 10-K), at 72 (Mar. 19, 2014) ("[R]ecognized tax gains on vehicle dispositions resulting from the [Like-Kind Exchange] suspension were more than offset by 100% tax depreciation on newly acquired vehicles.").

170. *See supra* note 54 and accompanying text.

171. *See* I.R.C. §§ 168(k)(2), 179(d)(1).

172. *See* Camp, *supra* note 62, at 15.

173. Rev. Rul. 71-137, 1971-1 C.B. 104.

through the purchase of a sports franchise.[174] In that case, the team may recover the cost ratably over fifteen years.[175] Unlike player contracts, future draft picks that a league awards to a team do not have an initial cost separate from the sport franchise asset.[176] Nonetheless, teams may have a cost basis in future draft picks that have been acquired through trade.[177]

1. Taxing Trades Before the TCJA

Before the TCJA, the IRS treated the trading of player contracts and future draft picks as a like-kind exchange.[178] By analogy, this treatment also could extend to other intangible assets involving the right to receive services from players,[179] such as the draft rights to certain players,[180] the right to participate in expansion drafts,[181] and the right to international roster slots.[182] When trades between teams occurred, the teams would recognize any gain or loss realized from the exchange only if teams received money or property other than like-kind property, known as "boot."[183] Any unrecognized gain or loss would then be deferred until the team sold or exchanged the player contract for non-like-kind property.[184] However, teams could avoid the taxing of deferred gain by retaining the player for the contract's entire duration.[185]

Treating assets involving the right to receive services from players as like-kind property meant that teams could engage in a variety of trades without incurring a tax liability. Even trades involving players to be named later[186] would not result in taxable gain so long as the teams satisfied certain timing limitations.[187] Moreover, when taxable gain did occur because of the receipt of boot, the taxable gain would not exceed the value of the non-like-kind property received.[188]

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174. Rev. Rul. 67-379, 1967-2 C.B. 127; *see also* Treas. Reg. § 1.167(a)-14(c)(2)(ii) ("The basis of a right to an unspecified amount over a fixed duration of less than 15 years is amortized ratably over the period of the right.").

175. I.R.C. §§ 197(a), (d)(1)(C)(i).

176. IRS MSSP GUIDELINE, *supra* note 12, at *68.

177. *Id.*

178. *See id.*

179. *See* Dickenson & Sutton, *supra* note 21, at 257 n.131.

180. *See* Riley Moore, *How It Works: Draft Rights and Signing Draft Picks*, MOORE BASKETBALL (May 30, 2016), https://moorebasketball.com/2016/05/30/how-it-works-draft-rights-and-signing-draft-picks/ [https://perma.cc/37EU-FGXE].

181. *See* Satchel Price, *2017 NHL Expansion Draft Results: All the Golden Knights' Trades*, SBNATION (June 21, 2017), https://www.sbnation.com/2017/6/21/15835324/nhl-expansion-draft-2017-trades-vegas-golden-knights-roster [https://perma.cc/JZG4-284M].

182. *See MLS Roster Rules*, *supra* note 39.

183. *See* Treas. Reg. § 1.1031(b)-1(a)(1) (as amended in 1967).

184. *See* I.R.C. § 1031(d) (2017).

185. *See* Adam B. Thimmesch, *Transacting in Data: Tax, Privacy, and the New Economy*, 94 DENV. L. REV. 145, 177 n.162 (2016) (recognizing that tax deferral may result in no taxation when the asset obtained in an exchange is consumed).

186. "When clubs consent to include a player to be named later . . . in a trade, they agree to decide upon . . . the final player involved in that trade at a later date." *Player to Be Named Later (PTBNL)*, MLB, http://m.mlb.com/glossary/transactions/player-to-be-named-later [https://perma.cc/Y6XQ-5HW5] (last visited Sept. 10, 2019).

187. *See* I.R.C. § 1031(a)(3).

188. *Id.* § 1031(b).

Fortunately for teams, the relief of salary owed to a player involved in an exchange did not constitute boot to the transferring team.[189] This is because a player's salary is a deductible expense,[190] preventing it from being considered when determining a team's amount realized.[191] Thus, when the Minnesota Twins traded Dave Winfield to the Cleveland Indians in exchange for a "nice dinner,"[192] the Twins realized and recognized gain only if the fair market value of the dinner exceeded their adjusted basis in Winfield's contract.[193] Had the Twins traded Winfield for a nice dinner and another player, the tax consequences would have been the same.

2. Applying Current Tax Law to Trades

After the TCJA, all trades between sports teams are taxable events because a trade is a realization event sufficient to incur taxation,[194] and there is generally no applicable non-recognition provision.[195] According to the rules governing dispositions of property, in a simple player-for-player trade, a team's amount realized in the transaction will be the fair market value of the player contract received,[196] which will also be the team's basis in the received contract.[197] Notably, a recently released revenue procedure creates a safe harbor that permits teams to treat the fair market value of a player contract or future draft pick as having zero value.[198]

The team will realize a gain if the amount realized in the transaction exceeds the team's adjusted basis in the player contract transferred, and the team will realize a loss should any of the adjusted basis not be recovered.[199] This is simple enough, when teams treat the assets as having zero value. However, when teams avoid the zero-value safe harbor, the tax consequences are far from simple because player contracts and future draft picks do not have an ascertainable fair market value, unless a team exchanges the player contract purely for money or a team retains partial liability for a transferred contract's salary obligations.[200] Even then, those

189. *See* Crane v. Comm'r, 331 U.S. 1, 5 n.6 (1947); Treas. Reg. § 1.1001-2(a)(3) (1980).
190. I.R.C. § 162(a)(1).
191. *See Crane*, 331 U.S. at 5 n.6; Treas. Reg. § 1.1001-2(a)(3) (1980). *But see* IRS MSSP GUIDELINE, *supra* note 12, at *68–71 (considering the relief of salary obligations when determining a team's gain from trading player contracts).
192. Chris Landers, *Celebrate the Madness of the Trade Deadline with Eight of the Weirdest Trades in MLB History*, MLB (July 31, 2017), https://www.mlb.com/cut4/trade-deadline-the-weirdest-trades-in-mlb-history/c-244576290 [https://perma.cc/ZLW7-4QBH].
193. *See* I.R.C. § 1031(b).
194. *See* Phila. Park Amusement Co. v. United States, 126 F. Supp. 184, 188 (1954).
195. *See* I.R.C. § 1001(a).
196. *See id.* § 1001(b).
197. *See Phila. Park*, 126 F. Supp. at 188.
198. *See* Rev. Proc. 2019-18, 2019-18 I.R.B. 1077.
199. *See* I.R.C. § 1001(a).
200. The chief legal officer of the MLB, Daniel R. Halem, has been quoted as saying, "There is no fair-market value of a baseball player. There isn't." Tankersley, *supra* note 16. *But see* MERCER CAPITAL, PRO SPORTS PLAYER CONTRACT VALUATIONS AND THE NEW TAX LAWS 1–2 (Nov. 2018), https://mercercapital.com/assets/Mercer-Capital-Pro-Sports-

circumstances offer little help to the IRS's valuation conundrum.[201]

IV. CRITICIZING THE APPLICATION OF CURRENT TAX LAWS TO TRADES

When one considers the justification for § 1031 and examples of deviations of the Haig-Simons definition of income, the need to return to the pre-TCJA manner of taxing trades between teams is apparent. Applying current tax laws to trades presents an insurmountable administration burden when teams avoid the zero-value safe harbor. Furthermore, the possibility of tax arbitrage is likely to reduce, rather than increase, tax revenue. This part of the article explains the unique aspects of both the professional sports industry and the intangible assets traded between teams that gives rise to these issues. In doing so, the necessity of returning to the pre-TCJA manner of taxation is made clear.

A. Applying Current Tax Laws to Trades Is Not Administrable

The IRS is not capable of applying current tax laws to trades between teams because the fair market value of player contracts and future draft picks is rarely ascertainable. Professional scouts have attempted to value players accurately since the dawn of professional sports, and yet, they still frequently fall short.[202] Surely, if the expert judgment of professional scouts paired with the statistical analysis known as Moneyball fails to overcome the player valuation conundrum, then tax law should not force IRS agents to step into the shoes of scouts. To do so is likely to result in high administration costs without reliable valuations. Moreover, the two limited circumstances where valuation is possible do not make the application of current tax laws to trades administrable because those circumstances rarely occur and administration costs will likely exceed the potential revenue.

1. Ascertaining the Fair Market Value of Player Contracts and Future Draft Picks Is Infeasible

Player contracts and future draft picks have value to teams, but that does not mean the assets have an ascertainable fair market value. As mentioned, an asset's fair market value is the hypothetical price at which the asset "would change hands between a willing buyer and a willing seller."[203] That price depends on the specific economic market in which the transaction occurred.[204] The market relevant to this article is the

Player-Contract-Valuations-and-the-New-Tax-Law.pdf [https://perma.cc/TY4F-SSFZ] (offering player contract valuation services).

201. *See* discussion *infra* Part IV.A.2.

202. *See* Berri et al., *supra* note 10, at 92.

203. Treas. Reg. § 1.170A-1(c)(2) (as amended in 2018).

204. *See* Selig v. United States, 565 F. Supp. 524, 527 (E.D. Wis. 1983), *aff'd*, 740 F.2d 572, 578 (7th Cir. 1984).

"player market," which "is the one in which individual players are bought, sold, and traded."[205] However, the distinct economies that exist in each league limit the ability to determine the fair market value of player contracts to only two circumstances, neither of which apply to future draft picks.

Courts declare that an asset has an unascertainable fair market value when the situation presents "elements of value so speculative in character as to prohibit any reasonably based projection of worth."[206] Such situations exist when there is an absence of markets in which comparable assets are sold or when the asset's value is "contingent upon facts and circumstances not possible to foretell with anything like fair certainty."[207] In those cases, courts defer taxation until the taxpayer subsequently sells the asset under the open-transaction doctrine, rather than impose a tax based on a guess of the asset's worth.[208] This is because it would be unfair to impose a tax on a taxpayer that cannot convert the asset to the money necessary to satisfy the tax liability.[209]

Any professional scout will tell you that determining an individual player's value to a team is speculative at best.[210] Such valuations require not only assessing a player's current performance but also predicting a player's future performance.[211] Yet, accurately predicting an individual player's impact on a team's revenue is impossible because statistical measures cannot fully capture a player's contribution.[212] Assessing the player's future contribution is further complicated by the unique circumstances of the team,[213] the difficulty in accounting for inconsistencies in a player's performance over time,[214] and the inability to assess a player's star appeal with any degree of certainty.[215] Not surprisingly, there is no consensus regarding how a player should be valued by teams in the

205. *Id.* at 529.

206. Fisher v. United States, 82 Fed. Cl. 780, 794 (2008) (quoting Campbell v. United States, 661 F.2d 209, 215 (1981)).

207. *Id.* (quoting Burnet v. Logan, 283 U.S. 404, 413 (1931)).

208. *See* Mothe Funeral Homes, Inc. v. United States, No. 94-1147, 1995 U.S. Dist. LEXIS 5125, at *15–16 (E.D. La. Mar. 29, 1995).

209. *See id.*

210. *See* DICKSON, *supra* note 5, at 262.

211. *See* BRADBURY, *supra* note 1, at 37.

212. *See* Gerrard, *supra* note 8, at 229.

213. *See* BRADBURY, *supra* note 1, at 108; *see also* Benjamin Aaron Campbell et al., *Resetting the Shot Clock: The Effect of Comobility on Human Capital*, 40 J. MGMT. 531, 548 (2014) (recognizing the disruptions that adding a new player to an existing roster may cause).

214. *See* BERRI ET AL., *supra* note 10, at 172–200.

215. *See* Rosen & Sanderson, *supra* note 27, at F49 ("Some star athletes develop personal followings that go well beyond their contribution to the quality of specific competitions. 'Star quality' is often elusive and harder to extract from simple statistics.").

NFL,[216] the MLB,[217] the NBA,[218] the NHL,[219] or the MLS.[220]

A player's value varies from team to team. One commentator has noted that "the contest aspects of sports imply that the value of one player depends on the services rendered by others."[221] Football fans understand this concept well. A great quarterback will not have great performance statistics unless he has linemen to block for him and receivers to catch his passes.[222] Similarly, basketball fans understand that the offensive performance of a team's players must shift when the team changes its player roster.[223] The shifting occurs because basketball rules permit one ball in games, and players must possess the ball to be offensively productive.[224] Thus, a player likely offers a greater contribution to one team over another, and the exact contribution will be different for every team.

Additionally, the revenue a player generates varies from team to team because a team's revenue is a function of the team's location.[225] Players contribute to a team's revenue by contributing to team wins and through their star appeal.[226] Yet, the amount of revenue that each team generates per win is at least partially dependent on the team's location and that location's characteristics, including its "population, wealth, weather, infrastructure, and fan loyalty."[227] The team's fans may also be loyal to a specific player.[228] That loyalty may cause significant merchandise sales for the player's team in one location,[229] which may not occur in another location.

Another reason that the fair market value of a player contract is not reliably ascertainable is because of the myriad of motivations behind team trades.[230] In barter transactions, "each side wants the specific goods

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216. *See* Ronald Yurko et al., nflWAR: A Reproducible Method for Offensive Player Evaluation in Football 3–6 (July 13, 2018) (unpublished manuscript) (on file with Cornell University), https://arxiv.org/pdf/1802.00998.pdf [https://perma.cc/RPN8-D9W5].

217. *See* Tankersley, *supra* note 16; *see also* BRADBURY, *supra* note 1, at 69–91 (explaining different methods for valuing baseball players); LEWIS, *supra* note 6, at 28–42 (detailing the many disagreements between the Oakland Athletics' former head coach, Billy Beane, and the team's scouts when deciding players to choose in the 2002 MLB draft.).

218. *See* BERRI ET AL., *supra* note 10, at 92–97, 196; Robert Lyons Jr. et al., *Determinants of NBA Player Salaries*, SPORT J. (May 29, 2015), http://thesportjournal.org/article/determinants-of-nba-player-salaries/ [https://perma.cc/942M-CLZN].

219. *See* Daniel S. Mason & William M. Foster, *Putting* Moneyball *on Ice?*, 2 INT'L J. SPORTS FIN. 206, 208–11 (2007).

220. *See* Rory Smith, *Soccer's Confounding Calculation: What's a Player Worth?*, N.Y. TIMES (June 22, 2017), https://www.nytimes.com/2017/06/22/sports/soccer/premier-league-transfers.html [https://perma.cc/CCL2-EFGF].

221. Rosen & Sanderson, *supra* note 27, at F49.

222. BERRI ET AL., *supra* note 10, at 184.

223. *Id.* at 117.

224. *Id.* at 115.

225. *See* Lopez et al., *supra* note 30, at 333–34.

226. *See* Rosen & Sanderson, *supra* note 27, at F48–F49.

227. BRADBURY, *supra* note 1, at 109.

228. Rosen & Sanderson, *supra* note 27, at F49.

229. *See* Pat Doney, *'Luka-Mania' Fuels Mavs' Apparel Sales Boost*, NBC DFW (Jan. 25, 2019), https://www.nbcdfw.com/news/sports/Luka-Mania-Fuels-Mavs-Apparel-Sales-Boost-504884012.html [https://perma.cc/4C9X-5HQD].

230. *See* Treas. Reg. § 1.170A-1(c)(2) (as amended in 2018).

the other side offers."[231] In the sports context, teams do not want a certain player contract or future draft pick because of some abstract standard of the asset's worth but, rather, because the trade confers a benefit to them.[232] For example, teams may engage in a trade to meet immediate roster needs, to bring their outgoing salary in line with their league's salary cap, to increase team wins, to increase team profits, or for the ego boost that comes by obtaining a certain player.[233] The value derived from each benefit is impossible to determine with any certainty. For that matter, the exact benefit received may be unclear.[234]

The following example illustrates the differences in value that teams may place on a given player. In 2008, the Calgary Vipers of the Golden Baseball League signed a contract with minor league pitcher John Odom.[235] Unfortunately, Odom had an "unspecified charge on his juvenile record" that prevented him from entering Canada.[236] This meant that Odom could not practice with the Vipers or participate in any games that took place in Canada, leaving the Vipers with a negatively valued player contract.[237] However, the Vipers struck a deal with the Laredo Broncos to trade Odom for $650 worth of baseball bats.[238] Accordingly, the Broncos valued Odom's worth at $650 more than his salary, despite the Viper's belief that he was vastly overpaid.[239]

Moreover, existing player valuation techniques do not apply well to the valuation of future draft picks.[240] Trades between teams often involve future draft picks that leagues will award years into the future, even though a team does not know the order of awarded draft picks until the end of each season.[241] This makes determining the fair market value of a draft pick impossible. Instead, teams trade draft picks based on the understanding that an earlier pick in the draft is worth more than a later pick, without assigning some abstract standard of value.[242]

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231. Dalton, *supra* note 149, at 181.

232. *See* Humphrey & Hugh-Jones, *supra* note 150, at 9.

233. *See* First Nw. Indus. v. Comm'r, 70 T.C. 817, 855 n.43 (1978), *rev'd on other grounds*, 649 F.2d 707, 709–710 (9th Cir. 1981) (recognizing that an "ego factor" exists in transactions within the sports industry).

234. *See* Aaron W. Clopton, *Profit-Maximizing and Win-Maximizing in the National Football League*, 7 J. CONTEMP. ATHLETICS 209, 209–10 (2013) (noting that increasing wins or profits do not necessarily require the same decision and that economists disagree as to which goal teams prioritize).

235. Associated Press, *Traded for Bats, Self-Worth Intact*, N.Y. TIMES (June 1, 2008), https://www.nytimes.com/2008/06/01/sports/baseball/01trade.html [https://perma.cc/K2HB-WY95].

236. *Id.*

237. *See* BRADBURY, *supra* note 1, at 16.

238. Associated Press, *supra* note 235.

239. *See id.*

240. *See* Aaron Barzilai, *Assessing the Relative Value of Draft Position in the NBA Draft*, 82GAMES, http://www.82games.com/barzilai1.htm [https://perma.cc/D8SU-VUD6] (last visited Sept. 10, 2019).

241. *See id.*

242. *See, e.g.*, *id.* (providing an analysis of the relative value of a draft pick in the NBA).

Proponents of applying current tax laws to trades between teams may argue that administrative difficulties do not justify returning to a pre-TCJA manner of taxation because teams value assets before engaging in trades.[243] This argument is without merit for two reasons. First, teams likely engage in trades because the asset received in the trade has a higher marginal utility to the recipient than the asset being transferred, not because of some common abstract standard of value.[244] Second, cases in which courts have arbitrarily allocated a portion of the purchase price of a professional sports team to player contracts illustrate the highly speculative nature of such valuations.[245]

Before the American Jobs Creation Act of 2004, disputes between the IRS and teams often occurred regarding the portion of the purchase price that teams could allocate to player contracts versus the franchise itself.[246] These disputes occurred because teams could amortize the cost to acquire player contracts in connection with a professional sports franchise but could not amortize the cost of the franchise or some other intangibles.[247] Teams allocated large portions of the purchase price to player contracts, and in response, the IRS would contest the team's allocation.[248]

When resolving these disputes, courts were "called upon to measure the worth of men, not machinery, a task of no small proportions."[249] Not surprisingly, courts either reached compromise valuations[250] or sided with valuations provided by general managers of other teams within the applicable league.[251] In reaching their decisions, courts found statistical methods of valuing player contracts, similar to Moneyball, to be highly speculative, calling them "unreliable,"[252] "ridiculous,"[253] and "thoroughly unpersuasive."[254] Instead, courts often relied on independent, expert testimony based on professional judgment.[255] The inability to value player contracts reliably caused the IRS to decide player valuations no longer

243. *See* Erwin, *supra* note 16, at 53.

244. *See supra* note 150 and accompanying text.

245. *See* Selig v. United States, 740 F.2d 572, 573–80 (7th Cir. 1984); Laird v. United States, 556 F.2d 1224, 1237–42 (5th Cir. 1977); P.D.B. Sports v. Comm'r, 109 T.C. 423, 426, 443–46 (1997); First Nw. Indus. v. Comm'r, 70 T.C. 817, 850–58 (1978), *rev'd on other grounds*, 649 F.2d 707, 709–10 (9th Cir. 1981).

246. Erwin, *supra* note 16, at 52.

247. American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 886, 118 Stat. 1418, 1641.

248. *See* H.R. Rep. No. 108-548, at 359 (2004).

249. *Laird*, 556 F.2d at 1241.

250. *See, e.g.*, *id.* at 1237–38; *First Nw. Indus.*, 70 T.C. at 850–57.

251. *See, e.g.*, Selig v. United States, 740 F.2d 572, 576–80 (7th Cir. 1984); P.D.B. Sports v. Comm'r, 109 T.C. 423, 426, 447 (1997).

252. Selig v. United States, 565 F. Supp. 524, 539 (E.D. Wis. 1983), *aff'd*, 740 F.2d 572, 578 (7th Cir. 1984).

253. *First Nw. Indus.*, 70 T.C. at 854.

254. *Laird*, 556 F.2d at 1238 n.22.

255. *See id.* at 1237–38; *Selig*, 565 F. Supp. at 533–34; *P.D.B. Sports*, 109 T.C. at 426, 447; *First Nw. Indus.*, 70 T.C. at 850–55.

merited "serious litigation investment."[256] Eventually, Congress ended the possibility of such disputes by allowing ratable amortization deductions over a fifteen-year period for all intangible assets acquired in connection with a sports franchise.[257] Congress did so because spending "taxpayer and government resources disputing [player contract valuations] is an unproductive use of economic resources."[258]

The characteristics of the professional sports industry make ascertaining the fair market value of player contracts and future draft picks generally impossible to do with any accuracy. Doing so for a simple player-for-player trade is overwhelmingly complex. Now, try to imagine the complexity of evaluating a trade involving a combination of eighteen player contracts and future draft picks, such as a trade that once occurred between the Dallas Cowboys and the Minnesota Vikings.[259]

2. The Two Circumstances in Which the Fair Market Value of Player Contracts Is Ascertainable Do Not Overcome the Administration Burden

The fair market value of a player contract is ascertainable both when a team exchanges a contract purely for money and when a team retains partial liability for a transferred contract's salary obligations. The ability to determine a fair market value in these circumstances is best understood by first recalling that, in arms-length barter transactions, the values of the assets exchanged are presumed to be equal.[260] Accordingly, when an exchange involves assets with unequal value, one side will probably demand that the other side offset the difference in value with money or other property.[261] In trades between teams, money may take the form of partially retained salary obligations[262] or, in some leagues, of a simple transfer of money.[263] The two forms differ because a team that retains

256. Stephen A. Zorn, *"Couldna Done It Without the Players:" Depreciation of Professional Sports Player Contracts Under the Internal Revenue Code*, 4 SETON HALL J. SPORTS L. 337, 390 (1994).

257. American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 886, 118 Stat. 1418, 1641.

258. H.R. REP. NO. 108-548, at 360 (2004).

259. *The NFL's Largest Trade*, PRO FOOTBALL HALL OF FAME, https://www.profootballhof.com/news/the-nfl-s-largest-trade/ [https://perma.cc/N59Q-MFRX] (last visited Sept. 10, 2019).

260. *See* United States v. Davis, 370 U.S. 65, 72 (1962).

261. *See id.*; *see also* Dalton, *supra* note 149, at 181 ("[T]erms of trade are determined by familiar supply and demand forces, both parties to the transaction seeking to economize or maximize, to receive the most for what they pay.").

262. *See* Croker, *supra* note 50; *see also* MLB COLLECTIVE BARGAINING AGREEMENT, *supra* note 41, at art. 23 § (C)(2)(b)(iii) (providing guidance for when a MLB team retains salary obligations in a transferred contract).

263. *See, e.g.*, James C. O'Leary, *Red Sox Sell Babe Ruth for $100,000 Cash*, BOS. GLOBE (Jan. 6, 1920), https://www.bostonglobe.com/sports/1920/01/06/red-sox-sell-babe-ruth-for-cash/muYGoMdAzCl8WlRHK2LumI/story.html [https://perma.cc/E4RG-RPCH]; *see also* MAJOR LEAGUE BASEBALL, THE OFFICIAL PROFESSIONAL BASEBALL RULES BOOK § 12(e) (2018), https://registration.mlbpa.org/pdf/MajorLeagueRules.pdf [https://perma.cc/864M-AY5A] [hereinafter OFFICIAL PROFESSIONAL BASEBALL RULES BOOK] (requiring that consideration, including cash, for trades be stated in definite terms).

salary obligations would not be liable for those obligations if the player were to breach the terms of the contract, which is not the case with a simple transfer of money. Further, retaining salary obligations in a transferred contract impacts that team's total salary for purposes of the league's salary cap.[264]

When a team exchanges a contract purely for money, the fair market value of the player contract is the amount of money received.[265] Nonetheless, such circumstances offer little towards administering current tax laws because they rarely occur: in 2018, only fifty-seven pure player-for-money trades occurred across the five professional sports leagues in the United States.[266] In fact, the NHL has banned such transactions,[267] and the NBA limits the yearly aggregate amount of money that a team may pay or receive in trades to $5.1 million.[268] Moreover, leagues flat out prohibit the exchange of cash for future draft picks.[269] Further, even when exchanges involving money do occur, the pre-TCJA manner of taxation accounts for them because they are not like-kind.[270]

When a team retains partial liability for a transferred contract's salary obligation, the fair market value of that contract is zero. Three reasons justify this valuation. First, the fair market value is not less than zero because, in an arms-length transaction, no team would accept a player contract that would cost them money. Second, the fair market value is not greater than zero because no team would retain salary obligations to provide the receiving team with a player that is worth more than his salary. Third, teams are unlikely to retain salary obligations to compensate another team for the difference in value of assets in an exchange. This is because the receiving team may not receive full payment if they released the player or if the player breached the terms of that contract. Thus, an agreement to retain a contract's salary obligations supplements the otherwise negatively valued contract, bringing its fair market value to zero. Again, this offers little to the valuation conundrum because the gain or loss from the exchange will be zero, meaning that no tax revenue is collected to offset the cost of administration.

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264. *See, e.g.*, MLB COLLECTIVE BARGAINING AGREEMENT, *supra* note 41, at art. 23 § (C)(2)(b)(iii).

265. *See Davis*, 370 U.S. at 72.

266. SPOTRAC, *MLB Transactions*, *supra* note 54 (MLB teams engaged in 46 player-for-money trades); SPOTRAC, *MLS Transactions*, *supra* note 54 (MLS teams engaged in 9 player-for-money trades); SPOTRAC, *NBA Transactions*, *supra* note 54 (NBA teams engaged in 2 player-for-money trades); SPOTRAC, *NFL Transactions*, *supra* note 54 (NFL teams engaged in 0 player-for-money trades); SPOTRAC, *NHL Transactions*, *supra* note 54 (NHL teams engaged in 0 player-for-money trades).

267. NHL COLLECTIVE BARGAINING AGREEMENT, *supra* note 39, at art. 50, §§ 50.5(e)(iii), 50.8(b)(ii).

268. NBA COLLECTIVE BARGAINING AGREEMENT, *supra* note 40, at art. VII § 8(a).

269. *See, e.g.*, OFFICIAL PROFESSIONAL BASEBALL RULES BOOK, *supra* note 263, §§ 4(k)(3)(A)–(B).

270. *See* I.R.C. § 1031 (2017); Treas. Reg. § 1.1031(a)-1 (as amended in 1991).

B. Current Tax Laws Invite Teams to Partake in Tax Arbitrage

Administrative costs aside, taxing trades between sports teams is likely to result in less tax revenue being collected than before the TCJA because of the opportunity for tax arbitrage. Tax arbitrage is a process in which taxpayers reduce their tax liability without fundamentally changing their economic position.[271] One way taxpayers may partake in tax arbitrage is by recognizing the time value of money and exploiting the different tax rates associated with ordinary income and capital gains.[272] Applying current tax laws to trades allows teams to do just that because teams may exploit the zero-value safe harbor when it benefits them and avoid the safe harbor, in favor of tax arbitrage, when it does not.

Since the Code entitles teams to amortize and deduct the basis of player contracts received in a trade,[273] the true net tax affect to teams is simply that caused by the time value of money.[274] These amortization deductions are meant to offset the cost of obtaining a player contract.[275] Accordingly, amortization deductions offset ordinary income, resulting in tax savings equal to the amount of the deduction multiplied by the taxpayer's effective tax rate.[276] However, the monopoly that teams have in contracting with non-free agent players and the salary restrictions unique to professional sports means that, by engaging in trades of player contracts, teams could obtain a much higher basis in the acquired contract than their actual out-of-pocket expense. This, combined with the preferential tax treatment that trades between teams are likely to receive when the asset is held for more than one year,[277] will often result in future tax savings that have a higher present value than the amount of tax owed after the trade.

This peculiar result is best illustrated with an example. Suppose that on January 1st of year one, a team trades a player contract with one year remaining on its term, an adjusted basis of $0, and a fair market value of $1,000,000 for another player contract that also has one year remaining on its term and a fair market value of $1,000,000. Assume also that the teams obtained the contracts without a signing bonus, making the ordinary income recapture rule embodied in § 1245 inapplicable.[278] Before the TCJA, the net tax effect to the teams would be $0, so long as they held onto to the acquired contracts for their duration. This is because the teams would not realize any gain until disposing of the contracts in ex-

271. *See* Shaviro, *supra* note 17, at 1244.
272. *See* Ethan Yale, *Investment Risk and the Tax Benefit of Deferred Compensation*, 62 Tax L. Rev. 377, 387–88 (2009).
273. Rev. Rul. 67-379, 1967-2 C.B. 127.
274. *See* Erwin, *supra* note 16, at 54.
275. *See* Rev. Rul. 71-137, 1971-1 C.B. 104.
276. *See* I.R.C. § 161 (2017).
277. *See supra* notes 88–93 and accompanying text. Gain on player contracts held for more than one year will be taxed at a maximum rate of 23.8% subject to the recapture rules of § 1245. *See supra* notes 88–93.
278. *See* I.R.C. § 1245(a).

change for non-like-kind property. Also, the teams would not be entitled to any additional amortization deductions since each teams' basis in the acquired contract would be zero.

Following the TCJA, each team would realize and recognize $1,000,000 in gain, resulting in a tax bill of $230,000 for year one, at a preferential tax rate of 23.8%. Each team could then amortize the entire $1,000,000 basis of the contract received in year one since that is the life of the contract. The amortization deduction of $1,000,000 results in $370,000 in tax savings, at the ordinary income tax rate of 37%. Thus, each team would reduce its tax liability by $132,000 for year one without fundamentally changing its economic position.

The same post-TCJA opportunity for tax arbitrage exists when teams trade player contracts with over one year remaining on their terms. For example, suppose a team trades a player contract it obtained without a signing bonus that has two years remaining on its term, an adjusted basis of $0, and a fair market value of $2,000,000 for another player contract that also has two years remaining on the contract and a fair market value of $2,000,000. Following the TCJA, the team would realize and recognize $2,000,000 in gain, resulting in a tax bill of $476,000 at a preferential tax rate of 23.8%. The team could then amortize the $2,000,000 basis of the contract received over the life of the contract, resulting in two yearly deductions of $1,000,000, and $370,000 in yearly tax savings at the ordinary income tax rate of 37%. The present value of the future tax savings at a 7% discount rate—the historical stock market rate of return[279]—is approximately $668,996. Thus, the team would reduce its tax liability by $192,996 without fundamentally changing its economic position. Any future gain from a sale of the contract would be recaptured as ordinary income under the principles of § 1245,[280] but teams can easily avoid this result by not engaging in such a transaction for the remainder of the player contract.

Some tax scholars may argue this opportunity for tax arbitrage is not any different from that allowed by the increased expensing associated with § 168(k) and § 179 of the Code.[281] This argument does not consider the unique characteristics of both the professional sports industry and the intangible assets traded between teams. As mentioned, § 168(k) allows a 100% deduction allowance for the year qualifying property is placed in service until January 1, 2023.[282] This deduction offsets the taxpayer's ordinary income for the year, resulting in tax savings.[283]

Unlike player contracts, the property facilitating a § 168(k) or § 179 deduction is likely to still have value beyond the point of the taxpayer's

279. J.B. Maverick, *What Is the Average Annual Return for the S&P 500?*, INVESTOPEDIA, https://www.investopedia.com/ask/answers/042415/what-average-annual-return-sp-500.asp [https://perma.cc/5AJ3-9XR6] (last updated May 21, 2019).
280. *See* I.R.C. § 1245(a)(1).
281. *See* H.R. REP. NO. 115-409, at 255 (2017).
282. I.R.C. § 168(k)(6)(A)(i).
283. *See id.* § 161.

basis in the property reaching zero. When this occurs, the owner of § 168(k) or § 179 property is likely to realize income from the property in the form of increased revenue from either using or selling the property. The entirety of this income will be taxed because there are no deductions to offset it. Therefore, the taxation of future income realized from the property should, in most cases, offset the immediate expensing allowed under § 168(k) or § 179.[284] This eventual offset cannot occur with the large deductions allowed by taxing trades between teams, because a player contract simply ceases to exist once its term ends.

Moreover, while not every trade will cause the present value of future tax savings to be greater than the tax liability incurred, teams are likely to plan accordingly. The zero-value safe harbor presents one notable planning opportunity.[285] In addition, teams may entirely avoid the realization event necessary to incur taxation. For example, in the MLS, teams may engage in cross player loans to avoid such a realization event.[286] No other league allows for intra-league loans. However, this could change because the leagues and player associations are themselves responsible for governing their teams.

V. TWO OPTIONS FOR RETURNING TO THE PRE-TCJA MANNER OF TAXATION

Considering the overwhelming administrability issues and the possibility of decreased revenue associated with taxing trades between teams, a return to the pre-TCJA manner of taxation is necessary. Affording non-recognition treatment to trades between teams deviates from taxing the Haig-Simons definition of income, but three reasons justify the deviation. First, like the non-taxation of imputed income, frequent flyer miles, and caught home run baseballs before they are sold, administrative concerns justify not taxing trades between teams.[287] Second, the value of player contracts and future draft picks will still be taxed when teams convert the player's services into revenue.[288] Third, while the non-recognition treatment constitutes a tax expenditure favoring professional sports, "[sports are] good for Americans (who can argue with [that])."[289]

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284. *See* Hanna, *supra* note 94, at 439 (the Cary Brown model "holds that immediately deducting the cost of an asset is equivalent to excluding from income the future annual return of the asset").

285. *See* Rev. Proc. 2019-18, 2019-18 I.R.B. 1077.

286. *See* Bradley T. Borden et al., *To Repeal or Retain Section 1031: A Tempest in a $6 Billion Teapot*, NEWSQUARTERLY, Spring 2015, at 1, 22; *see also MLS Roster Rules, supra* note 39, at 15 (providing rules regarding the loaning of players to other teams within the league).

287. *See* Abreu & Greenstein, *supra* note 104, at 344.

288. ORG. FOR ECON. CO-OPERATION & DEV., ADDRESSING THE TAX CHALLENGES OF THE DIGITAL ECONOMY 104 (2015) (the imposition of a tax at the time an exchange of personal data occurs between companies is not critical because the value of the data will be taxed when converted to advertising revenue).

289. Selig v. United States, 565 F. Supp. 524, 528 (E.D. Wis. 1983), *aff'd*, 740 F.2d 572, 578 (7th Cir. 1984).

Tax law may afford non-recognition treatment to trades between teams in one of two ways. First, Congress may pass legislation affording non-recognition treatment to the trading of intangible assets that involve the right to services from players. Second, the Treasury Department, either through its regulations or through the IRS, may reach the same result through reliance on the open-transaction doctrine. Notably, even if Congress were to return the taxation of trades between teams to the pre-TCJA manner through legislation, the Treasury would still need to account for the hundreds of trades that took place in 2018.[290]

A. Through Congressional Legislation

Congress may return the taxing of trades between sports teams to the pre-TCJA manner of taxation by modeling legislation after a recently proposed bill that aims to afford non-recognition treatment to exchanges of virtual currency.[291] Specifically, Congress may add a special rule to § 1031 stating that all intangible assets involving the right to receive present or future services from players shall be treated as like-kind property for purposes of the section.[292] Such a revision will bring player contracts, future draft picks, and other similar assets within § 1031, facilitating a return to the pre-TCJA manner of taxation.

B. Through Reliance on the Open-Transaction Doctrine

The Treasury may afford non-recognition treatment to trades between teams, without congressional intervention, by relying on the open-transaction doctrine. As a general rule, the Treasury, both in its regulations and through the IRS, demands that the fair market value of an asset received in an exchange be determined except in "rare and extraordinary" circumstances.[293] Current tax laws account for those circumstances with the open-transaction doctrine.[294] Thus, the Treasury may facilitate a return to the pre-TCJA manner of taxation by declaring that the trading of intangible assets involving the right to receive present or future services from players constitutes a "rare and extraordinary" circumstance.[295]

Under the open-transaction doctrine, transactions involving assets with no ascertainable fair market value are held open "until they are sold . . . or otherwise reduced to money or property of ascertainable value."[296] The taxpayer's basis in the asset transferred becomes the basis in the

290. *See* sources cited *supra* note 54.
291. *See* H.R. 7361, 115th Cong. (2018).
292. *See id.*
293. Treas. Reg. § 1.1001-1(a) (as amended in 2017); Rev. Rule 58-402, 1958-2 C.B. 15.
294. Thimmesch, *supra* note 185, at 177 n.162.
295. *See* Treas. Reg. § 1.1001-1(a) (as amended in 2017); Rev. Rule 58-402, 1958-2 C.B. 15.
296. Boris I. Bittker & Lawrence Lokken, Federal Taxation of Income, Estates and Gifts ¶ 93.5.3 (2018). For examples of cases allowing and disallowing the open-transaction doctrine, see *id.* at n.19.

property received.[297] A taxpayer will have an amount realized, to the extent that money or property with an ascertainable fair market value is received in the exchange. Further, any property or money received on a subsequent disposition of the asset will be tax free until the taxpayer recovers the asset's basis.[298] Thus, the doctrine results in the same tax consequences as § 1031.

VI. CONCLUSION

In conclusion, Congress dropped the ball when limiting like-kind tax treatment to real property without considering the trading of intangible assets that frequently occurs between sports teams. The Treasury Department has exacerbated the issue by creating a safe harbor permitting teams to treat player contracts and future draft picks as having a zero value for tax purposes without releasing any guidance addressing how valuations are to occur when teams avoid the safe harbor.[299] Nevertheless, to quote one of the winningest college football coaches, "The greatest mistake of all is to continue practicing a mistake."[300] Thus, Congress or the Treasury should return the taxation of trades between teams to the pre-TCJA manner of taxation.

Current tax laws require that IRS agents step into the shoes of professional scouts to ensure teams are assigning accurate values to the intangible assets involved in trades whenever teams avoid the zero-value safe harbor. Even with advanced valuation methodologies such as Moneyball, this requirement presents an insurmountable administration burden. As professional scouts, general managers, and even courts will tell you, assigning a fair market value to a player contract or future draft pick with any accuracy is generally impossible.[301] Indeed, Congress has scrapped other tax laws that required IRS agents to engage in the player valuation conundrum on grounds that administering the law resulted in an unproductive waste of taxpayer and government resources.[302]

Furthermore, a return to the pre-TCJA manner of taxing trades between teams is necessary to preserve tax revenue. Together, the monopoly that teams have on non-free agent players contracts, salary restrictions, preferential tax treatment, and potentially large amortization deductions allow teams to drastically reduce their tax liability without fundamentally changing their economic position. Teams will likely exploit this opportunity for tax arbitrage whenever possible. When it is not, teams are likely to plan accordingly. For example, teams may make ef-

297. Phila. Park Amusement Co. v. United States, 126 F. Supp. 184, 188–89 (1954).
298. *See* BITTKER & LOKKEN, *supra* note 296, at ¶ 93.5.3.
299. *See* Rev. Proc. 2019-18, 2019-18 I.R.B. 1077 § 1.
300. BOBBY BOWDEN, THE BOWDEN WAY: 50 YEARS OF LEADERSHIP WISDOM 249 (2002).
301. *See, e.g.*, Laird v. United States, 556 F.2d 1224, 1241 (5th Cir. 1977); DICKSON, *supra* note 5, at 263; Tankersley, *supra* note 16.
302. *See, e.g.*, American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 886, 118 Stat. 1418, 1641.

forts to minimize—or perhaps avoid—taxes by utilizing the zero-value safe harbor or by engaging in intra-league player loans, such as those currently allowed in the MLS.[303]

While there is an apparent need to return to a pre-TCJA manner of taxing trades between teams, doing so through congressional legislation may be difficult because of the current political climate.[304] Democratic members of Congress may be less than eager to correct mistakes in a largely Republican tax act.[305] Still, if sports alone cannot bring Democrats and Republicans together, this article provides both Congress and the Treasury with the justification and legal basis for returning to the pre-TCJA manner of taxation.

303. *See MLS Roster Rules*, *supra* note 39, at 15.

304. *See* Evan M. Migdail & Melissa Gierach, *Prospects for Tax Policy in a Divided Post-Election Congress*, DLA PIPER (Oct. 23, 2018), https://www.dlapiper.com/en/us/insights/publications/20018/10/prospects-for-tax-policy-in-a-divided-post-election-congress/ [https://perma.cc/TRK2-JPR4].

305. *See id.*