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RETIRE EARLIER, RETIRE WEALTHIER: A Coach's Use of PSCs and SEP-IRAs to Augment Retirement Benefits[1]

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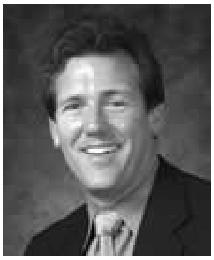
INTRODUCTION

A personal service corporation ("PSC")[2] is defined by the Internal Revenue Service ("IRS") as a corporation whose principal activity is the performance of personal services by the employee-owner of the corporation.[3] While many PSCs are actually limited liability companies,[4] this corporate form has the potential to provide meaningful benefits beyond limited liability, such as additional retirement benefits. As more fully discussed in Part II herein, however, certain risks can accompany these additional benefits; the IRS has attacked PSCs using numerous theories over the past twenty years. Notwithstanding the challenges in this area, PSCs that operate summer basketball camps represent a viable option for a coach to secure additional retirement benefits.

In 2006, Internal Revenue Code section 415 limits annual contributions to $44,000 per employee for qualified, defined contribution plans[5] (a defined contribution plan provides an individual account for each participant with the account benefits based on the amount contributed and adjusted by income, expenses, gains and loses). Universities often provide 403(b) plans to employees and such plans are subject to the $44,000 limit. These qualified 403(b) plans have employee deferral limits of $15,000 in 2006. In addition, universities may match this contribution to varying extents. Under these provisions of the Internal Revenue Code ("IRC"), a coach could contribute $15,000 of his 2006 salary to a 403(b) plan on a pre-tax, tax-

1. The author wishes to thank Phil McKnight and Zach Hemenway for their contributions in preparing this article.
2. For purposes of this article, references to PSCs or corporations are also generally applicable to limited liability companies.
3. I.R.C. § 269A(b)(1) (2006).
4. For a discussion of PSCs in the context of professional athletes, *see* Bret M. Kanis, Comment, *The Utility of Personal Service Corporations For Athletes*, 22 PEPP. L. REV. 629 (1995).
5. *See* I.R.C. § 415(c) (2006).

Author



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deferred basis and the coach's employer could supplement that contribution with another $29,000.

Universities may also offer one or more nonqualified, deferred compensation arrangements to employees that, together with qualified plan contributions, exceed $44,000. This creates an option other than a PSC which can result in increased retirement benefits; however, as a practical matter, most universities maintain only one employee retirement plan (qualified or non-qualified) and rarely match employee contributions in an amount that approaches the annual maximum. Consequently, it is more likely and easier for the University, from a legal, practical and political standpoint, to accommodate a coach's desire for augmented retirement benefits by establishing employment terms that facilitate this goal via a PSC.

Part I of this article provides an example of how a coach can augment existing retirement benefits via the use of a PSC coupled with the establishment of a SEP-IRA. Part II of this article provides an important analysis of Internal Revenue Code Rules and precedent that should be considered when operating a PSC established to provide additional retirement benefits. Part III posits a conclusion for the coach considering a viable method to augment retirement benefits.

PART I

If a coach desires to establish a PSC for purposes of augmenting retirement benefits, the tax law and precedents dictate that, in most circumstances, the coach take the following steps:

STEP 1: Estimate Camp Revenue. Determine whether summer camp revenue is sufficient to provide meaningful retirement benefits. The examples that follow permit estimates based on practical considerations and current law.

STEP 2: Review/Revise Employment Agreement. Assuming the University is agreeable, renegotiate the terms of the coach's employment contract so that the summer camp provision permits (this Step assumes the usual contractual relationship between the University as employer and the coach, in his individual capacity, performing services for his employer):

(a) payments to be received by the coach's PSC directly from campers;

(b) operation of the camp within the coach's discretion and under the coach's name; and

(c) use of University facilities without cost or at favorable rates.

STEP 3: Form a LLC. Establish a single-member limited liability company to operate camp facilities (e.g., Coach, LLC).

STEP 4: Observe Corporate Formalities. Coach, LLC should observe requisite corporate formalities – establish a separate checking account, secure appropriate liability insurance, prepare camp brochures and contracts with appropriate liability disclaimers, etc., all in the name of Coach, LLC. These matters, while relatively simple and straight-forward, are very important.

STEP 5: Contracting. Execute the following:

(a) a contract by and between Coach, LLC and the coach for the operation of the camp and the right (license) to use the coach's name, likeness, voice, etc., in its promotion;

(b) a contract by and between Coach, LLC and the University for the use of the necessary facilities for camp operations;

(c) independent contractor agreements by and between Coach, LLC and each of coach's camp assistants for services to be performed at the camp. The assistants must be considered independent contractors and not employees so that Coach, LLC is neither required to withhold employment taxes from their wages nor make contributions to their retirement plans;[6] and

(d) contracts by and between Coach, LLC and any third party vendors (T-shirt manufacturers, concessionaires, etc.).

STEP 6: Establish a Simplified Employee Pension Plan.

A Simplified Employee Pension Plan, commonly known as a SEP-IRA, is a type of retirement plan that best accommodates a self-employed owner of a PSC. The SEP-IRA is an Individual Retirement Account plan to which employers may make tax-deductible contributions on behalf of eligible employees on a discretionary basis.[7] The employer is allowed a tax deduction for plan contributions, which are made to each eligible employee's SEP-IRA on a discretionary basis. Employees do not pay taxes on SEP contributions, but these contributions are taxed when the employee receives a distribution from the SEP-IRA. Currently, applicable law provides that an employee cannot take distributions (except under special circumstances) until age 59½[8] and must begin taking distributions after age 70½.

SEP-IRAs provide certain tax advantages. For example, eligible employees (e.g., a coach as the sole owner of his PSC) can make tax-deductible deposits to his SEP up to 25% of total compensation[9] not to exceed $44,000.[10] And, just as in a coach's 403 (b) plan sponsored by an employer, these investments (hopefully) grow tax deferred until they are withdrawn.

Establishing a SEP-IRA is simple – a coach would simply complete an IRS Form 5305-SEP and an IRA investment application. The IRS form obviously is readily available, and the IRA application can be supplied by a financial institution. Most financial institutions (e.g., mutual fund companies) do not charge for establishing a SEP.

6. *See* I.R.C. § 3102 (2006); I.R.C. § 3301 (2006); Treas. Reg. 31.3401(c)-1 (2006).
7. *See generally* I.R.C. § 408(k) (2006) (defining simplified employee pension).
8. *See* I.R.C. § 72(t) (2006). People who take taxable distributions from IRA programs before this age, if they do not meet one of the exceptions, are subject to a premature distribution penalty tax.
9. I.R.C. § 404(h)(1)(C) (2006).
10. If the coach is the sole owner of the PSC, the effective amount of this contribution is reduced to approximately 20% of compensation because the coach must pay self-employment tax on his compensation.

Administering the plan is also a simple process. The coach can direct the investments, with assistance if desired, once the account is open and funded. **Note: A coach should be certain to consult a tax professional each year that he desires to make a contribution as the law in this area frequently changes and penalties can be assessed, for example, for exceeding contribution limits.**

STEP 7: Disburse Funds Each Tax Year

After paying all expenses (wages to assistants, facility rental fees, etc.) and applicable taxes (including self-employment taxes), Coach, LLC, makes the maximum allowable contribution to the coach's SEP-IRA plan, then pays the balance of the funds to the coach.

Examples Of the Process:

Assume that a college coach, in his individual capacity, executes a contract with his university to provide coaching services and that college coach operates a summer sports camp at his university-employer's facilities. The coach establishes a limited liability company, Summer Camp, LLC, to run the camps, and in the name of Summer Camp, LLC, sets up a SEP-IRA plan.

The coach is the sole member (owner) of Summer Camp, LLC. Summer Camp, LLC will enter into the following contracts in order to operate the camp: (1) camp participation agreements with each of the campers (including an appropriate liability waiver and release); (2) facilities usage agreements with the University; (3) an employment agreement with the coach for the coach's services at the camp; (4) independent contractor agreements with assistant coaches and officials for their services in conjunction with operating the camp; and (5) various supplier or sponsorship agreements for insurance, concessions, endorsements, etc.

Assume that Summer Camp, LLC generates revenue from the operation of sports camps during the summer of 2006. For purposes of this example, further assume all revenue comes from fees paid by campers to attend camp,[11] and that Coach pays two assistant coaches and his director of operations as independent contractors. Also, officials receive standard rates and modest facilities usage fees will be paid to the university.

Examples A and B assign values to the revenue and expense items described above. Example A demonstrates that, under current law, net earnings of $35,000 can generate a SEP contribution of approximately $6,500. Example B demonstrates that approximately $225,000 in net revenue is needed to generate a contribution near the $44,000 maximum under current law.

For the coach that desires to augment his retirement contribution . . .establishing a PSC to operate profitable summer sports camps represents the most realistic opportunity to secure these benefits without requiring major revisions to his coaching contract or risking an unfavorable IRS audit.

11. Revenue received from the sale of concessions or merchandise would likely be subject to sales tax and require separate business licenses. These issues are beyond the scope of this article.

EXAMPLE A
Contribution Estimate Based on $35,000 Net Camp Revenue

The example below is for illustration purposes only and should not be considered legal, accounting or other professional advice. Individuals should seek the advice of a qualified tax professional to determine whether the establishment and contribution to a SEP-IRA or other qualified retirement plan is appropriate and such decision should be based on such person's personal financial situation.

Assumptions: $60,000 in camp revenue
$25,000 in camp expenses
25% contribution percentage (maximum)

Gross Camp Revenue		$60,000
Camp Expenses	$7,500 Assistant Coach	
	$7,500 Assistant Coach	
	$5,000 Director of Operations	
	$3,000 Officials	
	$2,000 Operating Expenses	$25,000
		$35,000 Net Earnings
Calculate Self-Employment Tax		$2,473*
Adjusted Net Earnings (Net Earnings – Self Employment Tax)		$32,527
Desired Contribution Percentage (Desired contribution percentage of earned income, 0 – 25%, which can vary each year)		0.25
Contribution Factor (Add 1.00 to Desired Contribution Percentage)		1.25
Adjusted Earned Income (AEI) (Divide Adjusted Net Earnings by Contribution Factor)		$26,021
Maximum Earned Income Allowed		$220,000 (2006 Limit)
Final Earned Income (FEI) (The lesser of Maximum Allowed or AEI)		$26,021
Preliminary Contribution Amount (Multiply Contribution Percentage by FEI)		$6,505
Maximum Dollar Contribution Amount Allowed		$44,000 (2006 Limit)
Contribution Amount (The lesser of Maximum Dollar Contribution Amount or Preliminary Contribution Amount)		**$6,505***

*This assumes Coach has no other employment related income. To the extent Coach has other W-2 or self-employment income, this amount could be less, thus resulting in a larger potential SEP contribution amount. Calculation of Self-Employment Tax based on Social Security wage base of $94,200 for 2006.

EXAMPLE B

Contribution Estimate Based on $225,000 Net Camp Revenue

The example below is for illustration purposes only and should not be considered legal, accounting or other professional advice. Individuals should seek the advice of a qualified tax professional to determine whether the establishment and contribution to a SEP-IRA or other qualified retirement plan is appropriate and such decision should be based on such person's personal financial situation.

Assumptions: $275,000 in camp revenue
$50,000 in camp expenses
$25% contribution percentage (maximum)

Gross Camp Revenue		$275,000
Camp Expenses	$15,000 Assistant Coach	
	$15,000 Assistant Coach	
	$10,000 Director of Operations	
	$5,000 Officials	
	$5,000 Operating Expenses	$50,000
		$225,000 Net Earnings
Calculate Self-Employment Tax		$8,853*
Adjusted Net Earnings (Net Earnings – Self Employment Tax)		$216,147
Desired Contribution Percentage (Desired contribution percentage of earned income, 0 – 25%, which can vary each year)		.25
Contribution Factor (Add 1.00 to Desired Contribution Percentage)		1.25
Adjusted Earned Income (AEI) (Divide Adjusted Net Earnings by Contribution Factor)		$172,917
Maximum Earned Income Allowed		$220,000 (2006 Limit)
Final Earned Income (FEI) (The lesser of Maximum Allowed or AEI)		$172,917
Preliminary Contribution Amount (Multiply Contribution Percentage by FEI)		$43,229
Maximum Dollar Contribution Amount Allowed		$44,000 (2006 Limit)
Contribution Amount (The lesser of Maximum Dollar Contribution Amount or Preliminary Contribution Amount)		**$43,229***

**This assumes Coach has no other employment related income. To the extent Coach has other W-2 or self-employment income, this amount could be less, thus resulting in a larger potential SEP contribution amount. Calculation of Self-Employment Tax based on Social Security wage base of $94,200 for 2006.

PART II: TAX ANALYSIS

The IRS employs a number of different strategies to challenge PSCs for tax purposes. It is important to consider that if one of these theories is successfully asserted to challenge a coach's PSC, the coach runs the risks that his SEP-IRA plan will be disallowed. For example, if the IRS were to prevail on some of the theories that are described hereafter (e.g., Assignment of Income theory, IRC § 482 or IRC § 269A) then one of the likely consequences would be that the taxpayer's income and expenses would relate back to the university and the coach's employment relationship. Thus, the summer camp expenses of a general nature (such as independent contractor fees, officials' pay and administrative expenses, etc.) would only be deductible to the extent they exceed 2% of the coach's Adjusted Gross Income and would not be deductible at all for purposes of the Alternative Minimum Tax. Further, the expenses, including contributions, related to the SEP-IRA plan would not be deductible at all, since they would not be attributable to the university and coach's employment relationship.

Notwithstanding the theories by which the IRS has challenged PSCs, each theory is based on the principle of challenging and correcting PSCs that are formed in order to avoid or improperly reduce tax payments otherwise due. Because a coach following the steps outlined above would form his PSC as a limited liability company, such challenges would have little effect on the coach’s tax obligations as LLC owners are already taxed directly on their PSC's income.[12] Moreover, in today's litigious climate, operating a summer camp via the liability protections of a corporate form makes compelling business sense for almost every coach. In other words, in addition to structuring PSCs to avoid IRS scrutiny under these theories, a coach's PSC formed to operate summer camps should be defensible as a legitimate business activity. Consequently, while anyone forming a PSC should be aware of possible IRS theories attacking the form, it is possible for coaches seeking to augment retirement benefits by forming a PSC as a limited liability company to accomplish their goal despite these challenges.

The following are five theories used by the IRS to challenge PSCs:

1. IRC Section 269A Reallocation: PSC Performing Substantially All of Its Services for One Employer

Section 269A of the IRC was created specifically to address tax implications for PSCs. Section 269A(a) reads as follows:

> If (1) substantially all of the services of a personal service corporation are performed for (or on behalf of) 1 other corporation, partnership, or other entity, and (2) the principal purpose for forming, or availing of, such personal service corporation is the avoidance or evasion of Federal income tax by reducing the income of, or securing the benefit of any expense, deduction, credit, exclusion, or other allowance for, any employee-owner which would not otherwise be available, then the Secretary may allocate all income, deductions, credits, exclusions, and other allowances between such personal service corporation and its employee-owners, if such allocation is necessary to prevent avoidance or evasion of Federal income tax or clearly to reflect the income of the personal service corporation or any of its employee-owners.

Thus, in order to avoid application of IRC § 269A, a coach's PSC should not perform “substantially all” of his services on behalf of one other entity. The IRS has not defined “substantially all” of an individual’s services, but generally to avoid IRC § 269A issues a coach's PSC should perform services for entities other than the team or school where he coaches. If the university contracts with the coach's

12. *See supra* note 6 (outlining characteristics of an LLC). The primary ramification if the IRS were successful in one of these challenges would involve expenses in operating the company. These expenses would likely not be deductible if, for example, the PSC was deemed a sham corporation under the tax code.

PSC for the coach's services, the application of IRC § 269A can be avoided by the coach's PSC also contracting directly with each summer camper or high-school team that participates in his camp. Likewise, a coach's PSC may be engaged by other entities or individuals to make appearances or endorse products as such activities are permissible pursuant to his coaching contract. If the coach contracts with the university in his individual capacity and the coach's PSC contracts directly with the coach to perform services and with summer campers to provide services, an IRC § 269A reallocation should not be an issue.

IRC § 269A could create a problem for coaches who create a PSC solely for tax benefits and are unable to find parties other than a university or professional club interested in engaging the coach's services. However, these coaches still can avoid the application of IRC § 269A by demonstrating a valid purpose for establishing the PSC. Coaches who can validly argue their principal purpose of incorporating is augmenting retirement benefits should not have a problem with this section; the principal purpose of obtaining the benefit of a corporate retirement plan has been held to be a valid purpose in a case involving IRC § 269, which contains similar language to IRC § 269A with reference to corporations.[13]

2. Sham Corporation Theory

The IRS sometimes challenges PSCs and other limited liability companies by classifying them as sham corporations. A sham corporation is a corporation that has no meaningful business purpose. If the IRS refuses to recognize the entity as a corporation, the PSC owner is taxed directly on the income and loses part of the benefit of forming a PSC. Again this will not be a problem for coaches who establish LLCs because these coaches will be taxed directly on the income regardless of the classification. Moreover, it is rare for the IRS to successfully classify a company in this way. Courts usually reject the sham corporation theory unless the corporation has no obvious business purpose and is not a viable entity independent from the person who performs services for the PSC.

While the Supreme Court has not ruled specifically on PSCs and this theory, it has dealt with the sham corporation theory generally. In *Moline Properties, Inc. v. Comm'r*,[14] the entity in question was created by a taxpayer to assume mortgages related to a business deal. The Supreme Court determined that it was indeed a separate entity, holding, "[t]he doctrine of corporate entity fills a useful purpose in business life . . . so long as that purpose is the equivalent of business activity or is followed by the carrying on of business by the corporation, the corporation remains a separate taxable entity."[15]

A case involving the boxer Floyd Patterson further illustrates the sham corporation concept, particularly the egregious circumstances necessary for the IRS to be successful in these kinds of challenges. Patterson's PSC was formed to deal with the ancillary rights to his matches. The corporation had a phone number, but its office was not separate from Patterson's, the corporation owned no equipment or furniture, and the corporation kept very few records. Additionally, it was difficult to argue that the PSC's purpose was dealing with these rights because Patterson's agent had made deals for ancillary rights without incident prior to the PSC's formation. The tax court held that because Patterson's PSC had not managed the activities relating to its purpose and had failed to perform the daily activities of a normal corporation, it was a sham corporation and Patterson was taxed directly on the PSC income.[16]

The sham corporation issue can be avoided by following corporate formalities. These formalities are key

13. *See* Achiro v. Comm'r, 77 T.C. 881, 900-01 (1981).
14. 319 U.S. 436 (1943).
15. *Id.* at 438-39.
16. All facts are from *Patterson v. Comm'r*, 25 T.C.M. (CCH) 1230 (1966), *aff'd*, 22 A.F.T.R.2d (P-H) P 5810 (2d. Cir. 1968).

to making the corporation an entity separate from the person who reaps its benefits. The most important aspect of these corporate formalities is for the PSC to enter into a contract with the coach for his services and contract out those services to an employer, event, or other entity desiring the coach's services.

Other corporate formalities concern the practical operation of the corporation; a PSC should have its own checking account, keep records of income and expenses, and file tax returns as a separate entity. Activities such as holding organizational meetings (with minutes taken), adopting by-laws, and electing officers and directors can also work in a coach's favor. Finally, maintaining an office for the PSC with a separate telephone number, office equipment, corporate logo, etc. will strengthen the PSC's independence. All these activities help to defend against an IRS claim that the PSC lacks a legitimate business purpose.

3. Assignment of Income Doctrine

Another IRS theory attempting to limit the utility of PSCs is called the assignment of income doctrine. The basic idea of assignment of income is that the actual earner of income should pay the taxes; a person cannot assign their earned income to another person to avoid paying taxes on it. The IRS argues that the coach who performs the services should be taxed directly on the income. If the IRS is successful in this argument the coach is taxed on the entire amount paid to the PSC, rather than the smaller amount distributed to the coach as compensation by the PSC.

The assignment of income doctrine will only apply if the coach is considered an employee of the university he works for, as opposed to an employee of his PSC. There are two necessary elements for a coach to be considered an employee of his PSC and thus avoid the application of this doctrine. First, the PSC must have the right to control the coach's activities as one of its employees. Second, there must be a contract or agreement between the PSC and the organization employing the coach (i.e. a university) recognizing this right to control.[17] This right to control allows the coach to be considered an employee of the PSC, rather than the university, for tax purposes. If a university is unwilling to contract with a coach's PSC, this may result in the assignment of income and expenses directly to the coach. Here again, the LLC form already contemplates such an assignment of income and expenses and the potential application of this doctrine may only deter the taxpayer seeking taxation at corporate rates.

4. Section 482 and Reallocation of Income

The IRS might challenge a PSC by "reallocating" a portion of the income from the corporation to the coach. Some courts have held that this rule, described in IRC § 482, should be applied to PSCs instead of the assignment of income doctrine.[18] IRC § 482 reads, in pertinent part, as follows:

> In any case of two or more organizations, trades, or businesses . . . owned or controlled directly or indirectly by the same interests, the Secretary may distribute, apportion, or allocate gross income, deductions, credits, or allowances between or among such organizations, trades, or businesses, if he determines that such distribution, apportionment, or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any of such organizations, trades, or businesses.

17. *See* Johnson v. U.S., 698 F.2d 372, 374 (9th Cir. 1982). Johnson was a professional basketball player who entered into a contract with a corporation in which he agreed to give the corporation his yearly salary of $100,000 per year in return for the corporation's promise of $18,000 per year for the rest of his life. But the corporation did not deal directly with the basketball team, nor was there a contract of exclusivity. The court held that because there was not an exclusive contract between the two parties (Johnson and his PSC), Johnson had to pay taxes on the $100,000.

18. *See, e.g.,* Rubin v. Comm'r, 429 F.2d 650 (2nd Cir. 1970).

The services of a coach should be considered a trade or business. Thus, if the coach owns a PSC, the coach could be deemed to control two entities; the PSC and the coach's own services. But this is only a problem if the coach does not work exclusively for the PSC. For example, if a university contracts directly with the coach and not with the PSC, then the coach is controlling the trade or business of coaching services (a trade or business) as well as the PSC (the second trade or business). If instead the university contracts with the PSC, the coach is only employed by the PSC, and this section is not an issue. A coach will only have an issue under IRC § 482 if the coach renders services for someone or some entity other than the coach's PSC. This is typically the circumstance, however, as most coaches contract with their employer as individuals. Thus, it is important to consider the potential implications of IRC § 482.

In some situations, it can be difficult for a coach's PSC to avoid running afoul of these IRS challenges. For example, a coach seeking to meet the requirements of IRC § 269A by his PSC providing services to many individuals (e.g., summer campers) or entities necessarily becomes more likely to subject the PSC to IRC § 482s. Notwithstanding, if a coach's PSC is challenged, an IRC § 482 challenge carries relatively innocuous consequences. Even if IRC § 482 applies, its tax effects on the coach are much less punitive than in the other possible IRS challenges. Under IRC § 482, only a portion of the income is reallocated, and this can be only a small portion of total income earned.[19] Also, the IRS generally allows the taxpayer to modify his accounts to reflect the reallocation.[20] These two factors combine to minimize IRC § 482's impact on the benefits of forming a PSC.

5. Section 541 and Personal Holding Company Taxes

The Internal Revenue Service may attempt to deny the PSC some tax benefits by classifying it as a personal holding company. Under IRC § 541, a personal holding company is subject to a special penalty tax of 15% on all undistributed personal service income. This special penalty tax is an additional tax on top of the regular corporate income tax. A coach who forms a PSC should take extra care to avoid this punitive tax.

Pursuant to section 542(a), the IRS has two elements in its definition of a personal holding company. The first requirement is that "(a)t least (sixty) percent of (the corporation's) adjusted ordinary gross income . . . for the taxable year is personal holding company income," while the second element is that "(a)t any time during the last half of the taxable year more than (fifty) percent in value of (the corporation's) outstanding stock is owned, directly or indirectly, by or for not more than (five) individuals."[21] If both elements are met, the PSC can be subject to the personal holding company tax.

A PSC usually meets the adjusted ordinary gross income requirement. Personal service contracts are only personal holding income "if the individual who is to perform the services is designated . . . in the contract" and that person owns, either directly or indirectly, at least 25% of the value of the outstanding stock.[22] College coaching contracts almost as a rule designate the coach as the one who must perform the services. And a coach with a PSC will be either the sole shareholder/member or the majority shareholder/member of his corporation/LLC. Consequently, because a PSC has little gross income from sources outside its personal service contracts, the first requirement is usually met in a coaching contract situation.

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19. In context of professional athletes, this amount would generally equal the compensation the athlete would have received if the parties were dealing in an arm's length transaction. *See* Kanis, *supra* note 4, at 657.
20. *See* Rev. Proc. 99-32, 1999-2 C.B. 296.
21. I.R.C. § 542(a) (1)-(2) (2006).
22. I.R.C. § 543(a)(7) (2006).

Because of the makeup of PSCs – the coach is usually the sole shareholder, and the companies rarely have more than two or three shareholders – the second element of a personal holding company will also almost always be met.

Because both elements are usually met, most PSCs will be considered personal holding companies by the IRS, and this classification can diminish some of the benefits of incorporating a PSC. But this classification only affects *undistributed* income.[23] The tax ramifications can be avoided if the PSC distributes all of its gross income each year, using it to pay expenses, fund retirement programs, and compensate the coach.

A. Other Issues

Although minimal, there are costs associated with incorporation including legal fees for establishing the corporation (e.g. filing and document preparation fees), annual expenses in maintaining a corporate form,[24] and taxes levied against the corporation that are normally paid by the employer, such as unemployment and social security taxes.

B. Risk and Cost Summary

A coach's unique set of circumstances must be evaluated against the risks and costs identified in Part II. Fortunately, however, the advice of experienced legal counsel and tax professionals should be able to readily evaluate a given coach's potential to realize the value of a PSC to augment retirement benefits.

PART III. CONCLUSION

Considering the typical circumstances attendant to a coach's employment and the applicable tax law, a prime candidate for establishing a PSC to provide additional retirement benefits is a coach with substantial summer camp income and/or income from other non-university sources that are permissible under the coach's contract. The threshold issue is whether the net revenue projections for these other income sources make this option worthwhile compared to alternative investments of time and money.

The benefits derived from forming a PSC must also be considered relative to the alternative benefits currently provided to coaches through universities as well as the risks discussed herein. In addition to retirement plans, universities typically offer benefits that are similar or identical to the benefits that may be achieved through incorporation. For example, most universities provide high quality health and welfare benefits to employees. However, most universities provide a relatively small matching contribution to their employees' 403(b) plans if they match at all. And as the examples herein demonstrate, a coach operating a PSC has the potential to contribute the maximum amount permitted by law to a retirement plan instead of relying on a matching contribution from an employer, which, in most cases, is unable to modify matching amounts for highly compensated employees.

For the coach that desires to augment his retirement contribution beyond the current $15,000 deferral limit, establishing a PSC to operate profitable summer sports camps represents the most realistic opportunity to secure these benefits without requiring major revisions to his coaching contract or risking an unfavorable IRS audit.

23. I.R.C. § 541(2006) ("[t]here is hereby imposed . . . a personal holding company tax equal to 15 percent of the undistributed personal holding company income.").
24. In addition to the aforementioned corporate expenses (e.g. maintaining an office and separate phone, maintaining records, etc.), the *Sargent* case suggests that the coach should enter into a contract with the personal service corporation, and the personal service corporation should enter into a contract with the university, media personnel, and others contracting for the coach's services. Sargent v. C.I.R., 929 F.2d 1252 (8th Cir. 1991).

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MARK YOUR CALENDARS!!

INDIVIDUAL PERFOMER SPORTS: CURRENT LEGAL & BUSINESS ISSUES

On Friday, October 6, 2006, the NSLI will host its annual conference, which will focus on current legal & business issues in individual performer sports. Five conference panels will address cutting edge legal and business issues related to tennis, golf, track and field, poker, swimming and other individual performer sports. Information about conference registration and other details now available at http:// law.marquette.edu/jw/2006conf.

National Sports Law Institute
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