

# Pro Sports Player Contract Valuations And The New Tax Law

It's Not Just A GM's Issue Anymore

**Mercer Capital  
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# Mercer Capital's Professional Sports Industry Expertise

## Leaders in Sports Valuation and Related Stadium Advisory Services

In an increasingly competitive professional sports and eSports market, Mercer Capital's team capabilities in valuation, intangible assets, stadium issues, and legal consulting are unsurpassed. We have the depth of knowledge necessary to assist in developing industry best practices.

This knowledge relates not only to the underlying economics to the sports business, which include its escalating cost structure, but most importantly, the future revenue-enhancing aspects of sports that are the key to future success.

This knowledge base has been built over the past 25 years from continuing services, engagements, and relationships in the industry.

## Services

- Valuations (M&A oriented, tax driven, shareholder buyouts, and litigation)
- Valuation of Player Contracts
- Fairness Opinions
- Buy-Side Planning
- Due Diligence Services
- Stadium Lease Consulting (new and existing)
- Legal Transaction Consulting
- Tax Advisory
- Other Services

Our professionals have provided valuation and advisory services to clients in every major U.S. professional sports league. For more information about our services, visit [our website](#) or contact any of our senior professionals.

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As the 2018 calendar year moves towards a close, front offices and league offices across professional sports are at different places:

- **MLB** just finished their year, and teams are taking stock of what happened and planning for winter meetings.
- **MLS** is a few weeks away from the MLS Cup in early December.
- The **NFL** is just past the halfway point as the trade deadline recently past and the playoff race is being run.
- The **NBA** and **NHL** are getting their seasons off the ground and haven't hit the quarter pole yet.

Players are at the heart of all these leagues. Whether a rookie, veteran, all-star, or benchwarmer, these players all have value. Now, as a result of the Tax Cuts and Jobs Act, exactly how much value is a very real question for many player contracts involved in a trade, adding complexity to an already complicated process.

Beginning in 2018, the tax treatment for certain player-for-player trades changed. Player-for-player trades have been treated as a like-kind exchange for decades. However, the appreciation in value of a traded player's contract has now potentially become a taxable event for teams. Considering this, when a taxable event occurs, teams must measure this appreciation in terms of dollars in order to report potential capital gains to the IRS. This is where valuation issues become relevant.

## Contract Valuations: The CFO's Domain Is Now Merging With Team Operations

As important as they are to a sports team, historically player contracts rarely needed to be separately valued. When they did, it was typically when a franchise was bought or sold. In that situation, player contracts (along with other identified intangibles) were allocated as an asset in the purchase price.

Franchise transitions happen relatively infrequently; therefore, some front offices, tax advisors, and valuation firms don't have experience in this area. Mercer Capital is one of very few with deep experience in this area.

Historically, general managers and personnel departments valued player contracts internally which produced a relative valuation result. This value result cannot now be directly used by the tax and finance department to report values. Therefore, it's important to work with professionals who have experience determining the fair market value of player contracts and understand the complexities of each league.

Trades are usually made for (i) other players, (ii) draft pick rights, (iii) cash, or a combination of these. When analyzing the trade deal, only one scenario would appear to directly value player contracts – a cash deal. However, even this can be somewhat deceiving when it comes to fair market value as player development and other hidden costs may need to be included. Indeed, draft picks and draft positioning

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function as a currency in leagues, especially the NFL with larger rosters and shorter playing careers. Trades and player values are often discussed in terms of relative draft pick positioning.

Other factors can come into play as well. What if the teams involved in a trade had rationale for it not directly related to contract value, like salary cap issues? The fair market value of a contract could be only one of many issues at play in a trade under various scenarios.

Therefore, when determining a player contract's fair market value, it's important to have a valuation methodology that comports with a team's internal rationale, as well as having IRS supportability.

## Valuation Approaches And Considerations

Numerous factors impact the fair market value of a player contract, including:

- Historical performance
- Potential future performance
- Position played
- Commercial and media potential
- Off-field behavior
- Age
- Physical characteristics
- Roster and league attrition
- Draft position
- Team performance and constitution
- Length of existing contract
- Other

### Valuation Approaches

There are three approaches to value that could potentially capture the above factors into a single dollar figure: income, market, and cost approaches. The income approach is rarely used because it is difficult to directly trace an individual player's impact on the team's income stream. The market approach and the cost approach, or a hybrid of the two, are more typically employed to value player contracts.

### Valuation Considerations

Due to the nature of the asset, a mix of quantitative and qualitative analyses are used to develop a model to value player contracts and the economic benefit (or detriment) they possess relative to the rest of the team's roster. This is done in comparison to alternatives that a team may have and a player may have under their collective bargaining agreement. Once adjustments are made, a value can be estimated. A hybrid method using both the market and cost approach has the following benefits:

- Data driven
- Consistent
- Tethered to the framework of a league's collective bargaining agreement
- Can ascribe value to draft pick rights as well as player contracts

Of course, values are subject to facts and circumstances. Potential differences in opinions on either side of a trade is an issue that is likely to arise. If teams cannot agree to a value, or appraisals of the same player contract result in different values, there is the potential of an IRS audit situation for both teams on the same trade.

## Conclusion

The change in the tax law brings additional attention to player contract values. It may or may not impact how a team approaches its business of winning championships, but it will impact how leagues and front offices approach valuations of player contracts. Will the leagues, taxpayers, and the IRS find common ground? Perhaps it will depend on how touchdowns, goals, hits, and rebounds translate into value on a tax return.

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## The Mercer Capital Difference

### Deep Experience Valuing Player Contracts

- Mercer Capital is one of a very small group of valuation firms with extensive experience in valuing hundreds of player contracts for dozens of professional sports franchises over the years.
- This deep experience has led to a positive working relationship with teams and league offices.
- Our proprietary methodology has been accepted by the IRS amid direct scrutiny and hours of questioning. To date, our work has not been overturned. Additionally, our work has withstood other types of scrutiny on multiple occasions.

### Cost Effective Fees

- Because of the experience described above, we can pass on very competitive fee structures.

### Easy to Work With

- We recognize this process can intrude on a front office's valuable time and resources. We balance being flexible while fulfilling our important professional obligations.
- We do not need to meet with a General Manager in our process. We can work with other personnel as appropriate.

**If we can help, please don't hesitate to contact us at 214.468.8400.**





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