Stemkowski v. Commissioner, 76 T. C. 252 (1981)

The salaries of nonresident alien professional athletes are allocable only to the regular season of play, not to off-season, training camp, or playoff activities.

Summary

Stemkowski and Hanna, nonresident alien professional hockey players, contested the allocation of their U. S. income and claimed deductions for off-season conditioning, away-from-home expenses, and other miscellaneous costs. The Tax Court ruled that their salaries were allocable only to the regular season, not to training camp, playoffs, or off-season activities. The court also denied deductions for conditioning expenses, as they were related to income earned in Canada, and disallowed other expenses due to lack of substantiation or connection to U. S. income.

Facts

Stemkowski and Hanna, Canadian citizens, played professional hockey for U. S. teams in 1971. Their contracts specified a 12-month term, but the salary was for services during the regular season only. Stemkowski played for the New York Rangers, with some games in Canada, while Hanna played for the Seattle Totems, all games in the U. S. Both players engaged in off-season conditioning in Canada to meet contractual fitness requirements.

Procedural History

The Commissioner determined deficiencies in the players' U. S. income taxes and denied their claimed deductions. The players petitioned the U. S. Tax Court, which consolidated their cases and heard them as a test case for other similar disputes. The court's decision addressed the allocation of income and the deductibility of various expenses.

Issue(s)

1. Whether the stated salaries in the employment contracts covered services beyond the regular season, such as off-season, training camp, and playoffs, allowing allocation to non-U. S. sources?
2. Whether off-season physical conditioning expenses were deductible as ordinary and necessary business expenses under section 162?
3. Whether various expenses incurred in 1971 were deductible as "away-from-home" traveling expenses under sections 62 and 162?
4. Whether miscellaneous expenses claimed for 1971 were deductible, and if so, were they adequately substantiated?

Holding

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1. No, because the salaries were paid only for the regular season of play, and thus only days spent in Canada during the regular season were excludable from U. S. income.
2. No, because the off-season conditioning expenses were allocable to income earned at training camps in Canada, which was not subject to U. S. tax.
3. No, because the players' tax homes were the cities where their teams were located, and they failed to substantiate their expenses.
4. No, because the miscellaneous expenses were either not ordinary and necessary or not adequately substantiated.

Court's Reasoning

The court analyzed the employment contracts and found that the salaries were intended to cover only the regular season, based on the contract language and testimony from hockey league officials. The off-season conditioning requirement was viewed as a condition of employment, not a service for which the salary was paid. The court applied Treasury Regulation section 1. 861-4(b) to allocate income based on time spent performing services in the U. S. during the regular season. The players' failure to substantiate expenses under section 274(d) precluded deductions for away-from-home and miscellaneous expenses. The court also found that the players' tax homes were their team cities, not their Canadian residences, following the principle from Commissioner v. Flowers.

Practical Implications

This decision clarifies that nonresident alien athletes' salaries are taxable in the U. S. based on the time spent playing in the U. S. during the regular season. It establishes that off-season conditioning is not a deductible business expense for U. S. tax purposes if related to income earned outside the U. S. Practitioners should advise clients to carefully document and substantiate all claimed deductions, as the court strictly enforced the substantiation requirements of section 274. The ruling also reinforces the principle that an athlete's tax home is typically the location of their team, affecting the deductibility of living expenses. Subsequent cases have followed this precedent in determining the allocation of income and deductibility of expenses for nonresident alien athletes.

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