

The Navigator



Wealth
Management

RBC Wealth Management Services

Financial planning and tax checklist for the sport professional

Young athletes who join professional sports teams face a variety of unique tax and financial planning issues. This article provides a checklist (not exhaustive) of potential strategies that sports professionals, their families and/or agents should consider to help preserve the player's financial success and ensure that it continues in the future.

Please contact us for more information about the topics discussed in this article.

The information provided in this article is based on the tax law (current or proposed) in effect as of the date of this article. The information is not intended to provide legal or tax advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified cross-border tax and/or legal advisor before acting on any of the information in this article.

- Tax residency
- Signing bonus planning
- Retirement compensation planning
- Endorsement income planning
- Charitable foundation
- Will and Power of Attorney planning
- Life and disability insurance planning
- Family income splitting strategies
- U.S. estate tax
- Probate tax planning
- Tax deductibility of mortgage interest
- Family law
- Asset preservation planning
- Retirement and investment planning
- Qualified cross-border tax advisor
- Credit planning



The country where a sports professional resides for income tax purposes can have a dramatic impact on the overall taxes they will pay on income earned (including signing bonus and employment income).

Tax residency

The country where a sports professional resides for income tax purposes can have a dramatic impact on the overall taxes they will pay on income earned (including signing bonus and employment income). Normally, a sports professional who plays for a U.S. or Canadian team will be resident, for tax purposes, in the U.S. state or Canadian province in which their team plays home games.

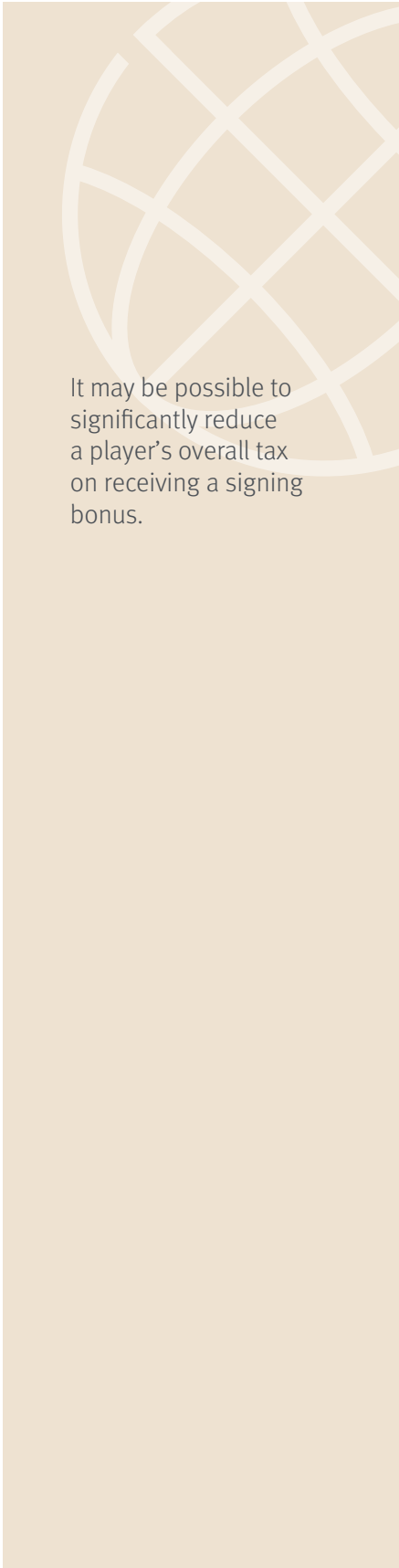
Alternatively, a player may be resident in a U.S. state or Canadian province different to the one in which their team plays home games if they have greater residential ties (home, family, days present, etc.) to that state or province. In some cases, players coming from a country outside North America that has a tax treaty with Canada or the U.S. could potentially remain a resident of that foreign country if the player has substantial ties there. Such a scenario could result in significant tax savings, depending on the circumstances.

Due to the differences in top marginal tax rates between some provinces, a player who is resident in Canada should consider provincial tax residency as carefully as Canadian tax residency. For example, a player may be able to take steps to achieve residency for tax purposes in a lower-tax province, such as Alberta. Similarly, if a player living in the U.S. is a U.S. citizen, green-card holder or U.S. resident (i.e. "U.S. person") the player may be able to achieve residency for tax purposes in a U.S. state that has either low or no state income tax.

Athletes may also be subject to income tax in more than one country.

For example, when a game is played in a country other than the player's country of residence, the player may be subject to tax in their country of residence and in the country where they earned employment income relating to those games. Also, a player who is a U.S. person and establishes residency in another country for tax purposes is generally required to file a U.S. income tax return to report their global income. It is generally possible to avoid double taxation when income is taxed by more than one country due to the ability to claim foreign tax credits. Also, for U.S. income tax purposes, the taxable income of a player who is a U.S. person resident in a foreign country can be reduced by the foreign earned income exclusion (income relating to games played) in that foreign country, subject to limitations.

The player's professional tax advisor can run a comparative analysis to determine which residency status is preferential from a tax standpoint. If a particular residency status is shown to be beneficial for this purpose, and the player is willing to make the necessary lifestyle changes, the player may have to take certain steps to remain or become a resident of a particular jurisdiction. This may involve purchasing a home, moving to or having their spouse/children remain in a specific location or spending a significant number of days in a location. However, tax residency is based on facts and circumstances. In many cases, when the player establishes significant ties to the U.S. state or Canadian province where their home team is located, it may not be possible to choose the location where the player will be resident for tax purposes.



It may be possible to significantly reduce a player's overall tax on receiving a signing bonus.

Signing bonus planning

When an athlete enters into a contract to play on a professional sports team, in many cases, a signing bonus is included as part of the contract. When the player receives the signing bonus, if the contract is structured properly, it will be subject to tax in the country (including the state or province) where the player is resident for tax purposes. If the signing bonus is paid by a professional sports team located in a different country, that country may also impose tax on the payment of the bonus. If proper planning is done, it may be possible to significantly reduce a player's overall tax on receiving a signing bonus.

Under the Canada-U.S. tax treaty, a signing bonus is subject to a maximum U.S. tax rate of 15% if the bonus is paid by a U.S. team to a Canadian resident (other than a U.S. citizen). Similarly, a signing bonus is subject to a maximum Canadian tax rate of 15% if the bonus is paid by a Canadian team to a U.S. resident. This rule represents a significant tax planning opportunity, particularly if a U.S. team pays a signing bonus to a Canadian resident and then, after receiving the bonus, the player becomes a U.S. resident for the remainder of the year. In this case, the U.S. tax rate on the signing bonus is limited to 15% and it is possible to reduce or eliminate the Canadian tax on the signing bonus with foreign tax credits.

If the professional sports team agrees, it may be worthwhile to structure a contract to include a signing bonus to take advantage of this preferential tax treatment. If you would like more information on the tax benefits that may be achieved by planning the

receipt of a signing bonus, ask your RBC advisor for a copy of the article titled "Signing Bonus Planning for Sports Professionals."

Retirement Compensation Arrangements (RCAs)

If a Canadian-resident sports professional is playing for a Canadian-based team, they may wish to consider asking the team to contribute to a Retirement Compensation Arrangement (RCA) on their behalf. This is suitable for sports professionals where there is a distinct possibility that they may become a non-resident of Canada in the future when their playing days are over. If the RCA is structured correctly, withdrawals from the RCA as a non-resident of Canada can potentially be taxed at only 15-25%.

The following are some other issues to keep in mind relating to the RCA:

- For the RCA to be worthwhile, it is important to determine how the RCA withdrawals will be taxed in the country where the recipient will be resident when they receive a distribution.
- An RCA may be an effective strategy for a U.S. citizen playing in Canada who is expected to retire back in the U.S.
- There may be some tax savings with an RCA for a player who plays in Canada, outside Alberta, but who expects to retire in Alberta.
- It is important to get an actuarial report certifying that contributions to the RCA are reasonable based on the player's salary, age and expected years in retirement.

It is a good idea for sports professionals to have their Wills and Powers of Attorney (POA) updated in the jurisdiction where they are resident.

RBC has considerable experience in RCA planning and RCA investing. Ask your RBC advisor for more information.

Endorsement income planning

A Canadian-resident sports professional who is receiving endorsement revenue should consider speaking to their tax advisor to determine if there is a benefit to setting up a Canadian corporation to receive the endorsement revenue rather having it paid to them directly. The endorsement revenue could be considered “active business income” and taxed at lower Canadian corporate tax rates. If a sports professional is married, they could also potentially income split with their spouse by paying dividends from the corporation to the spouse.

This kind of strategy may not be as effective for U.S. tax purposes, so it is important to consult with a qualified U.S. tax advisor to discuss this possibility.

Charitable foundation

In the past, some sports professionals have set up charitable foundations in their own name to raise funds, donate to charitable causes and reduce their income taxes. A sports professional has the option to set up either a private foundation, which may provide more control, or a public foundation, which may mean less administration. RBC can assist such individuals in setting up a Canadian public foundation through the RBC Charitable Gift Program. Ask your RBC advisor for more information.

Will and Power of Attorney planning

It is a good idea for sports professionals to have their Wills and Powers of Attorney (POA) updated in the jurisdiction where they are resident. Furthermore, if the player owns real estate or other assets in another country (e.g. Canadian-resident player with U.S. real estate or vice versa) they may wish to consider having another Will and Power of Attorney in the U.S. state or Canadian province where their real estate or other assets are located.

If you require a referral to a qualified cross border lawyer to draft a Will and/or a POA, ask your RBC advisor for assistance.

Life and disability insurance planning

Although no one likes to think about death or disability, it is important that players and their families consider their life and disability insurance requirements. Some forms of life insurance can also provide tax-free investment growth that the player may want to consider as a potential vehicle for any surplus savings. Due to the cross-border nature of professional athletes' careers, it may be prudent to consider both the Canadian and U.S. tax treatment of certain life insurance policies when initially structuring the policy.

Although it may be difficult for the player to get disability insurance, there are some insurance companies that specialize in providing disability insurance to professional sports players. The player should also consult their players' association. They may be able to provide a list of companies that are able to offer disability insurance to athletes.

The player may want to consider certain probate minimization strategies for certain assets.

Family income splitting strategies

If an athlete is married and has a lower-income spouse and/or lower-income children, there are various family income splitting tax strategies they could consider that may reduce tax on investment income. Since everyone in Canada files separate tax returns, family income splitting is more relevant for Canadian tax purposes than it is for U.S. tax purposes. Spousal loans and family trusts are common family income splitting strategies that may be effective in Canada to reduce the family tax burden resulting from investment income.

Please speak with your RBC advisor if you require information about setting up a spousal loan or a family trust and contact a qualified tax advisor for advice. If you are a U.S. person who lives in Canada, it is important to speak to a qualified cross-border tax advisor to consider the potential U.S. tax implications.

U.S. estate tax

U.S. citizens, U.S. green-card holders and domiciled U.S. residents (“U.S. persons”) are subject to U.S. estate tax on the fair market value of their worldwide assets upon death. U.S. estate tax is levied based on graduated tax rates with a maximum tax rate of 40%. Individuals who are not U.S. persons are potentially subject to U.S. estate tax only on their U.S. situs assets (generally U.S. real estate, U.S. stocks, U.S. retirement plans and deferred compensation from a U.S. company) at death regardless of where they lived in the world.

U.S. estate tax is only applicable if the value of the worldwide assets of

a U.S. citizen or Canadian resident at death is greater than the U.S. estate tax exemption threshold applicable in the year of death. For deaths in 2016, the U.S. estate tax threshold is US \$5.45 million. In some cases the U.S. estate tax exemption can be as low as US\$60,000. For example, this low exemption amount would occur if a Canadian player is resident in the U.S., but is not domiciled in the U.S.

There are a number of strategies that may be considered to minimize or defer U.S. estate tax. Ask your RBC advisor for information and speak to a qualified cross-border tax advisor.

If you or your spouse is a U.S. person then it is important to have your Will reviewed by a qualified cross-border lawyer, as there are specific Will planning strategies to minimize U.S. estate tax.

Probate tax planning

Provinces such as British Columbia and Ontario levy a flat probate tax (i.e. estate administration fee) on the value of the estate assets upon death. The probate fees in Alberta and Quebec are much lower than that of the other provinces.

Real estate assets may also be subject to probate tax even if the player is not resident in the jurisdiction where the real estate is located. Probate tax is charged in addition to any U.S. estate tax or Canadian income taxes at death. Obtaining probate in relation to assets located in the U.S. may involve burdensome legal and administrative challenges. To avoid these potential complications, the player may want to consider certain probate minimization strategies for certain assets. These could include



Given the limited number of earning years for sports professionals, they should have a plan to save and preserve some of their earnings in a prudently managed investment portfolio.

holding assets in joint tenancy or through living trusts. Revocable living trusts are common vehicles to hold U.S. real estate assets to minimize U.S. state probate tax.

In some cases, strategies to minimize probate tax may jeopardize other more beneficial tax and estate planning strategies. For this reason it is important to work with a qualified cross-border tax and estate advisor to resolve any potential issues.

Tax deductibility of mortgage interest

In our experience there is some confusion regarding the tax deductibility of mortgage interest. For Canadian tax purposes, interest paid on a mortgage to purchase a Canadian or U.S. personal residence is not tax-deductible. The mortgage interest may only be tax-deductible for Canadian tax purposes if the property is used for investment purposes. In addition, interest may be deducted for Canadian tax purposes on loans used to purchase investments that have the potential to pay income (i.e. stocks, bonds, mutual funds, etc.).

For U.S. tax purposes, a U.S. person can deduct interest paid on a mortgage secured on a principal residence or on a second home; but there are limits. The loan may be a mortgage to buy a home, a second mortgage, a line of credit secured by the property, or a home equity loan.


The following are some limits on tax deductibility of mortgage interest for U.S. tax purposes:

- If the mortgage was taken out to buy, build or improve a home, then interest on up to US\$1,000,000 of the mortgage is tax deductible for U.S. tax purposes
- If the mortgage was taken out for reasons other than to buy, build or improve a home, then interest on up to an additional US\$100,000 of the mortgage is tax-deductible for U.S. tax purposes
- In addition to the above limits, high-income taxpayers must scale back all their itemized deductions, including mortgage interest expenses. U.S. persons should consult with their tax advisor to determine whether the scale-back will reduce the benefit of the mortgage interest deduction.

Family law

Although it may be a difficult subject to discuss, a player may want to consider signing a marriage contract to ensure that their assets are protected from division should a marriage breakdown occur in the future.

Players who are getting married or are married should consult a legal professional who specializes in family law in the applicable jurisdiction for additional information. Note that players living in common-law relationships may also be impacted financially by a breakdown in their common-law relationship and should also seek legal advice before entering into common-law relationships.



It is important to have a qualified cross-border tax advisor who is familiar with both Canadian and U.S. tax issues.

Asset preservation planning

High-income and high-net-worth individuals are generally more likely to be the subject of lawsuits. Therefore, over time, as sports professionals increase their net worth, they should consider strategies to protect their wealth from creditors. Assuming there are no existing or foreseeable claims, a common solution is to transfer some part of the net worth into a domestic or foreign trust (potentially subject to U.S. gift tax and/or Canadian deemed disposition tax), thereby changing the legal owner of the assets, and reducing the value of the assets that will be available to satisfy legal claims made by creditors.

Retirement and investment planning

A sports professional has the potential to earn a significant amount of money at a young age in a short period of time. As a result, there will likely be some expensive purchases (homes, cars, vacations, etc.) made at a young age and the temptation for additional big-ticket purchases. There could also be many financial requests from friends, acquaintances and family members for loans, gifts and business investments. However, given the limited number of earning years for sports professionals, they should have a plan to save and preserve some of their earnings in a prudently

managed investment portfolio. That is, after their playing career ends (generally late 20s to late 30s), players may require income from the pool of savings to support their lifestyles for an unusually long period of time (40-60 years).

As a result, sports professionals should consider speaking to their RBC advisor about preparing a financial plan to determine a savings and spending strategy during the high-earning years to ensure that they are on track and financially stable after their career ends.

Qualified cross-border tax advisor

Due to the complex cross-border tax issues and multiple tax filing requirements that can affect professional athletes, it is important to have a qualified cross-border tax advisor who is familiar with both Canadian and U.S. tax issues. If you require a referral to a qualified cross-border tax advisor, speak to your RBC advisor.

Credit planning

Credit is a very important tool for managing and leveraging a sports professional's wealth and can enhance overall tax planning strategies – in all stages of the player's career. However, it is essential that players constantly manage their credit and ensure it is paid off on a regular basis.



If you have any questions or require clarification of any of the issues discussed in this document, do not hesitate to contact your RBC advisor or discuss them with your own tax advisor.

Planning in advance is crucial

The tax and financial planning requirements of sports professionals require careful consideration at various stages in the player's career, particularly before the signing of the player's first professional contract. Planning in advance is also important before a transfer to another professional sports team and in anticipation of retirement. Speak to an RBC advisor about the tax and financial planning strategies highlighted in this article to ensure planning is tailored to individual circumstances.



**Wealth
Management**

This document has been prepared for use by the RBC Wealth Management member companies, RBC Dominion Securities Inc. (RBC DS)*, RBC Phillips, Hager & North Investment Counsel Inc. (RBC PH&N IC), RBC Global Asset Management Inc. (RBC GAM), Royal Trust Corporation of Canada and The Royal Trust Company (collectively, the "Companies") and their affiliates, RBC Direct Investing Inc. (RBC DI) *, RBC Wealth Management Financial Services Inc. (RBC WMFS) and Royal Mutual Funds Inc. (RMFI). *Members-Canadian Investor Protection Fund. Each of the Companies, their affiliates and the Royal Bank of Canada are separate corporate entities which are affiliated. "RBC advisor" refers to Private Bankers who are employees of Royal Bank of Canada and mutual fund representatives of RMFI, Investment Counsellors who are employees of RBC PH&N IC and the private client division of RBC GAM, Senior Trust Advisors and Trust Officers who are employees of The Royal Trust Company or Royal Trust Corporation of Canada, or Investment Advisors who are employees of RBC DS. In Quebec, financial planning services are provided by RMFI or RBC WMFS and each is licensed as a financial services firm in that province. In the rest of Canada, financial planning services are available through RMFI, Royal Trust Corporation of Canada, The Royal Trust Company, or RBC DS. Estate and trust services are provided by Royal Trust Corporation of Canada and The Royal Trust Company. If specific products or services are not offered by one of the Companies or RMFI, clients may request a referral to another RBC partner. Insurance products are offered through RBC WMFS, a subsidiary of RBC DS. When providing life insurance products in all provinces except Quebec, Investment Advisors are acting as Insurance Representatives of RBC WMFS. In Quebec, Investment Advisors are acting as Financial Security Advisors of RBC WMFS. The strategies, advice and technical content in this publication are provided for the general guidance and benefit of our clients, based on information believed to be accurate and complete, but we cannot guarantee its accuracy or completeness. This publication is not intended as nor does it constitute tax or legal advice. Readers should consult a qualified legal, tax or other professional advisor when planning to implement a strategy. This will ensure that their individual circumstances have been considered properly and that action is taken on the latest available information. Interest rates, market conditions, tax rules, and other investment factors are subject to change. This information is not investment advice and should only be used in conjunction with a discussion with your RBC advisor. None of the Companies, RMFI, RBC WMFS, RBC DI, Royal Bank of Canada or any of its affiliates or any other person accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or the information contained herein. © Registered trademarks of Royal Bank of Canada. Used under license. © 2016 Royal Bank of Canada. All rights reserved. NAV0147 (06/2016)