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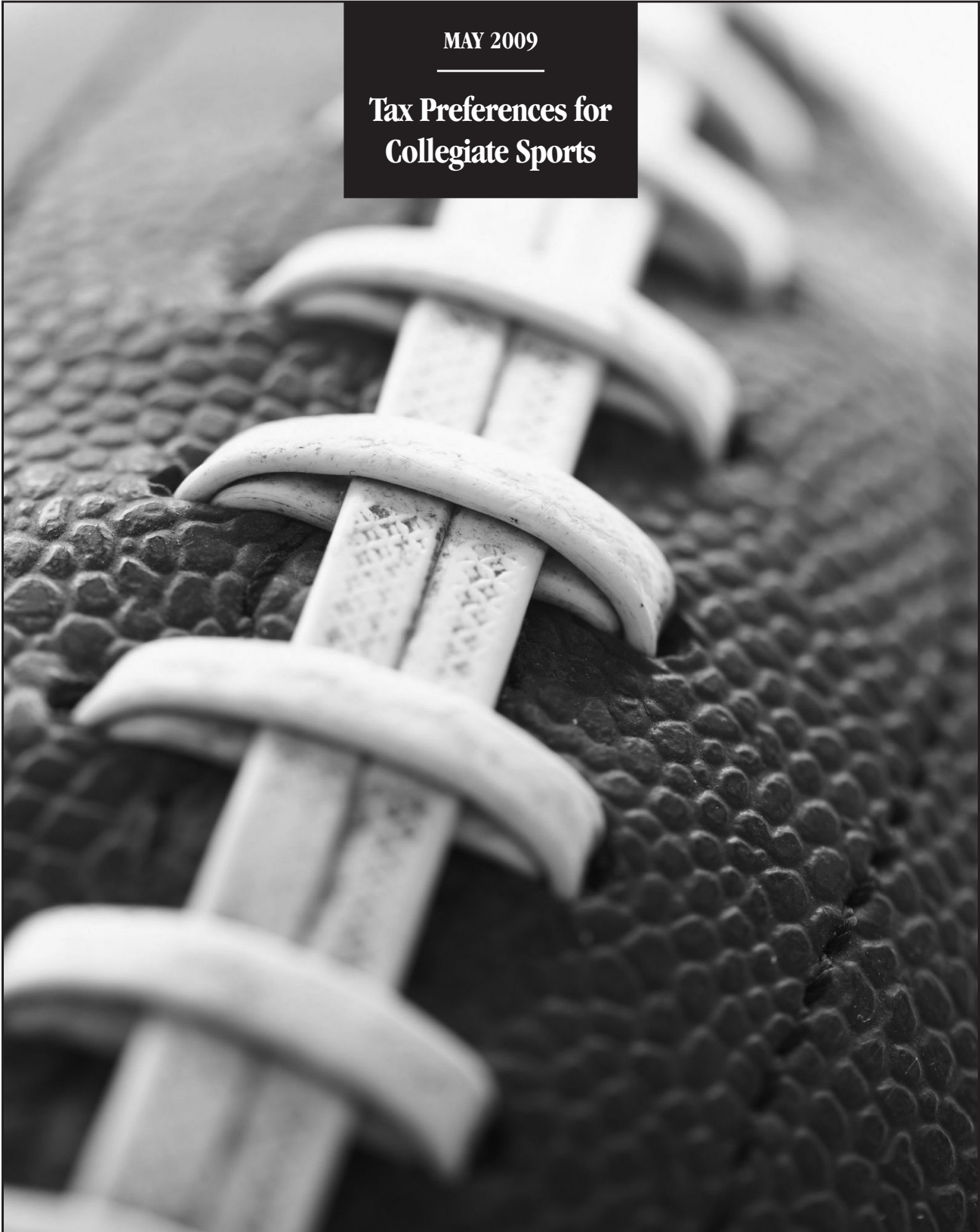
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CBO

PAPER

MAY 2009

**Tax Preferences for  
Collegiate Sports**







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May 2009





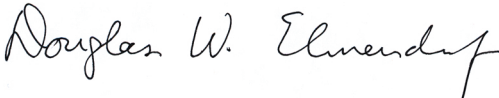
# Preface

**C**olleges and universities generally qualify for preferential treatment under the federal income tax because their educational mission has important benefits for the public. But concerns have arisen that some activities undertaken by colleges and universities are only loosely connected to educating students and might be viewed as unrelated to the schools' tax-favored purpose. Long viewed as an integral component of higher education, sports in many universities have become highly commercialized. The large sums generated through advertising and media rights by schools with highly competitive sports programs raise the questions of whether those sports programs have become side businesses for schools and, if they have, whether the same tax preferences should apply to them as to schools in general.

This Congressional Budget Office (CBO) paper, which was prepared at the request of the Ranking Member of the Senate Finance Committee, compares athletic departments' share of revenue from commercial sources with that of the rest of the schools' activities to assess the degree of their commercialization. It also discusses the benefits of intercollegiate sports programs and some of the issues that might arise if the Congress decided to alter the treatment of those programs in the tax code. In accordance with CBO's mandate to provide objective, impartial analysis, the paper makes no recommendations.

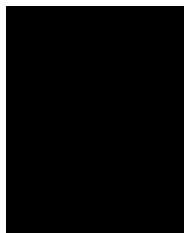
Kristy Piccinini of CBO's Tax Analysis Division and Dennis Zimmerman, formerly of the Tax Analysis Division, wrote the paper, under the supervision of Frank Sammartino and G. Thomas Woodward, formerly of CBO. Paul Cullinan and Joseph Kile of CBO and Brad Humphreys of the University of Alberta commented on early drafts, and Nabeel Alsalam of CBO provided help with the data. (The assistance of an external reviewer implies no responsibility for the final product, however, which rests solely with CBO.)

Sherry Snyder edited the study, and John Skeen proofread it. Maureen Costantino designed the cover and prepared the report for publication. Lenny Skutnik printed the initial copies, Linda Schimmel coordinated the print distribution, and Simone Thomas prepared the electronic version for CBO's Web site ([www.cbo.gov](http://www.cbo.gov)).



Douglas W. Elmendorf  
Director



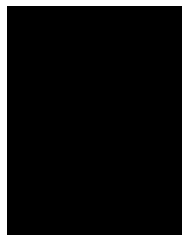


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## Summary

**C**olleges and universities generally qualify for preferential treatment under the federal income tax. The income of nonprofit private and public postsecondary schools is exempt from taxation, and gifts to those schools are generally tax-deductible to the donor. Those tax preferences stem from the schools' educational mission. But concerns have arisen that some activities undertaken by colleges and universities are only loosely connected to educating students and might be viewed as unrelated to the schools' tax-favored purpose.

One such activity is intercollegiate sports. Long viewed as an integral component of higher education, sports in many universities have become highly commercialized. Successful athletic programs are very rewarding financially: The National Collegiate Athletic Association (NCAA) men's basketball tournament alone garnered about \$143 million in revenue for athletic departments in 2008, and college football bowl games generated a similar amount.

Such large sums raise the questions of whether those sports programs have become side businesses for schools and, if they have, whether the same tax preferences should apply to them as to schools in general. This Congressional Budget Office (CBO) paper compares athletic departments' share of revenue from commercial sources with that of the rest of the schools' activities to assess the degree of their commercialization. It also discusses some of the issues that might arise if the Congress decided to alter the treatment of intercollegiate sports programs in the tax code.

This analysis focuses on the athletic programs of colleges and universities in the NCAA's Division I—those that have the largest sports programs and, consequently, are most likely to engage in commercial activities. Broadly defined, commercial activities provide a good or service in exchange for a fee in a market that also includes taxed businesses; in sports, those activities include ticket sales, shared revenue from championship games, sales of media

rights, and advertising. In conducting this study, CBO relied on two sources of data on the revenue generated by the athletic programs of Division I schools: budget reports from the athletic departments of NCAA schools collected in 2006 by the *Indianapolis Star* newspaper under the Freedom of Information Act and data on total revenue for those schools from the Department of Education.

The study also examines the issues that might arise if policymakers decided that some or all of the activities of the schools' athletic programs were primarily commercial rather than educational—a decision that would greatly reduce or eliminate the rationale for giving those activities preferential tax treatment. The Congress could change the tax treatment of revenue from those activities in several ways, for example, by limiting the deduction for contributions, limiting the use of tax-exempt bonds, or limiting the exemption from income taxation.

On the basis of its analysis, CBO concludes the following:

- Athletic departments in NCAA Division I schools derive a considerably larger share of their revenue from commercial activities than do other parts of the universities.
- In the case of Division IA schools (a subset of schools in Division I that meet NCAA requirements for football programs), 60 percent to 80 percent of athletic departments' revenue comes from activities that can be described as commercial. That proportion is seven to eight times that for the rest of the schools' activities and programs, suggesting that their sports programs may have crossed the line from educational to commercial endeavors. Revenue from commercial activities accounts for a much smaller share of athletic department revenue (20 percent to 30 percent) for schools in the rest of Division I.

■ Nonetheless, removing the major tax preferences currently available to university athletic departments would be unlikely to significantly alter the nature of those programs or garner much tax revenue even if the sports programs were classified, for tax purposes, as engaging in unrelated commercial activity. As long as athletic departments remained a part of the larger nonprofit or public university, schools would have considerable opportunity to shift revenue, costs, or

both between their taxed and untaxed sectors, rendering efforts to tax that unrelated income largely ineffective. Changing the tax treatment of income from certain sources, such as corporate sponsorships or royalties from sales of branded merchandise, would be more likely to affect only the most commercial teams; it would also create less opportunity for shifting revenue or costs.



# Tax Preferences for Collegiate Sports

## Current Tax Treatment of the Activities of Colleges and Universities

As nonprofit institutions, colleges and universities are granted a variety of federal tax preferences that are designed to support their educational purpose, which has social as well as private benefits. Those preferences are not unlimited. The law has consistently attempted to balance the advantages of preferential federal tax treatment for nonprofit organizations against the possibility that those preferences could be used to engage in commercial activities that compete with taxable businesses.

Institutions of higher education, both public and private, benefit from several types of preferential tax treatment. Nonprofit private schools, like other nonprofits defined in section 501(c)(3) of the Internal Revenue Code, are exempt from the federal income tax, are eligible to receive charitable contributions that the donor may deduct, and may use tax-exempt debt to finance capital expenditures. Public colleges and universities receive broadly similar tax preferences; as state or local government entities, they are exempt from federal income taxation, are eligible for deductible contributions, and may have access to tax-exempt debt.

Like other nonprofit organizations, colleges and universities receive those preferences because they serve a public purpose. For institutions of higher learning, that public purpose is clearly education, which has traditionally included education through participation in athletics. Education is associated with a wide range of favorable outcomes. Investment in human capital through education confers a considerable private benefit on the individual, in the form of higher income and better health.<sup>1</sup> Education also creates public benefits for the community as a whole, including a more skilled workforce, increased economic growth, and greater social mobility.<sup>2</sup> An individual's decision regarding how much education to invest in will depend on his or her private benefit alone; in the

absence of government intervention, that decision will yield fewer public benefits than is socially desirable. The favorable tax treatment of educational institutions, including those providing postsecondary education, is one way in which policymakers may be able to offset some of the potential underinvestment in human capital and subsidize the social benefits of education.

Because providing such benefits is the primary justification for nonprofit institutions' federal tax preferences, the government has a clear interest in ensuring that those preferences are used to facilitate activities that yield those benefits and not other activities. Thus, the federal income tax exemption for nonprofits is limited to income earned from the pursuit of the purpose that renders them eligible for the exemption, referred to as related income. Income earned from activities that are not substantially related to the performance of the exempt purpose is not tax-exempt

1. Claudia Goldin and Lawrence F. Katz (*Long Run Changes in the U.S. Wage Structure: Narrowing, Widening, Polarizing*, Working Paper No. 13568 [Cambridge, Mass.: National Bureau of Economic Research, November 2007]) document a rise in the return to education in general over the past several decades and, in particular, a rise in the return to postsecondary education. David M. Cutler and Adriana Lleras-Muney ("Education and Health: Evaluating Theories and Evidence," in Robert F. Schoeni and others, eds., *Making Americans Healthier: Social and Economic Policy as Health Policy* [New York: Russell Sage Foundation, 2008]) discuss the evidence for a positive relationship between education and health outcomes, with particular attention to the mechanisms through which education may be the cause of better health.
2. Eric Hanushek and Ludgar Woessmann (*Do Better Schools Lead to More Growth? Cognitive Skills, Economic Outcomes, and Causation*, Working Paper No. 14633 [Cambridge, Mass.: National Bureau of Economic Research, January 2009]) find empirical evidence of a causal relationship between educational attainment and economic growth rates across countries. For a discussion of the relationship between postsecondary education and social mobility, see Robert Haveman and Timothy Smeeding, "The Role of Higher Education in Social Mobility," *Future of Children*, vol. 16, no. 2 (2006), pp. 125–150.

and is subject to the corporate income tax on unrelated business income, commonly referred to as the unrelated business income tax (UBIT). That tax was enacted in 1950, at least partially in response to New York University's acquisition of Mueller's, the noodle and pasta company. The purchase of that previously taxable business contributed to the perception that nonprofit-owned businesses, facing lower costs because of their tax-exempt status and other federal subsidies, would be able to underprice taxable businesses, leading to unfair competition and the erosion of the corporate tax base.<sup>3</sup>

Policymakers at that time were also concerned that allowing charitable institutions to pursue commercial activities on a tax-exempt basis would encourage them to allocate an excessive amount of resources to those activities rather than to their charitable purpose. To that end, the law they enacted subjected income from commercial enterprises to the UBIT even if that income was used to finance the primary mission of an exempt organization. For colleges and universities, for example, the income they earn from tuition, research grants, passive investment income (which includes royalties, interest, and capital gains), contributions, and athletics is considered related to the exempt purpose and is therefore tax-exempt, but income earned from operating a restaurant that serves the general public is not, even if the profits are used to provide educational services for students.

Because public universities operate under the auspices of state governments, laws regarding state commercial enterprises may also be relevant to the commercialization of their activities. In general, the Internal Revenue Service (IRS) has never considered state commercial enterprises of any type taxable, even if they are separately incorporated, because their operation is invariably classified as an essential state function and the income accrues to the state government. The Internal Revenue Code, however, specifically makes state colleges and universities subject to the UBIT. That situation creates an anomaly: Any other state entity running a trade or business would not be subject to the UBIT and taxation, but a state college running the same unrelated business would be subject to the tax under current law.

3. Because the corporate income tax limits the deduction that corporate donors can take for their charitable donations, a commercial entity whose income accrues directly to a nonprofit parent would, in the absence of the UBIT, pay lower taxes than a business that simply donated all of its profits to a nonprofit organization.

Like the exemption from federal income taxation, the deductibility of charitable contributions to a nonprofit entity is subject to some limits when the contribution resembles a commercial transaction. In general, contributions given to a nonprofit in exchange for a good or service are nondeductible for the donor. Some donations to athletic departments are made to obtain the right to buy game tickets or preferential seating, and in 1986 the IRS ruled that such contributions were in return for a "substantial benefit" and were therefore nondeductible. In 1988, however, the Congress enacted legislation that explicitly permitted donors to deduct 80 percent of those contributions under section 170 of the Internal Revenue Code.

## Comparing Commercialization in Athletic Departments and Other University Activities

This paper does not consider the possible commercial nature of a college or university as a whole.<sup>4</sup> Rather, the analysis takes the primarily noncommercial nature of the entire institution as a given and focuses on the activities of athletic programs. Specifically, this analysis addresses the concern that athletic programs have become primarily commercial—that is, they regularly provide a good or service in exchange for a fee in a market that also includes businesses subject to taxation—rather than educational. To assess the commercial nature of sports programs, the Congressional Budget Office (CBO) first examined the sources of athletic departments' revenue for a subset of colleges and universities and then compared them with the sources of revenue for the schools as a whole. The data indicate that athletic departments at some schools are significantly more commercial than the schools' other activities.

### Commercial Activity in Athletic Programs

The analysis focused on athletic departments at schools in Division I of the National Collegiate Athletic Association (NCAA)—a voluntary organization through which colleges and universities govern their sports programs. Division I comprises the schools that have the largest sports programs—they must meet NCAA minimum

4. A previous Congressional Budget Office report, *Taxing the Untaxed Business Sector*, Background Paper (July 2005), discussed how those institutions are similar to for-profit businesses in important ways.

standards for the number of sports played and for the amount of financial aid awarded to athletes—and are therefore most likely to engage in commercial activities. The division is further divided into three subdivisions—Divisions IA, IAA, and IAAA—that are relevant only for football.<sup>5</sup> To participate in Division IA, schools must meet certain minimum standards for football programs, including home game attendance and scheduled games against other members of the subdivision.

Information on athletic departments' budgets is available for 164 of the 327 schools that were members of Division I in academic year 2004-2005. The data were collected by the *Indianapolis Star* newspaper in 2006. The *Star* requested, under the Freedom of Information Act (FOIA), the budget reports that the NCAA requires from the athletic departments in all schools in Division I. The 112 private schools in the division were exempt from the requests, as were public schools in Pennsylvania and Delaware, by state law.<sup>6</sup>

The *Star* data show that the largest source of athletic departments' revenue is ticket sales, followed by contributions, distributions by athletic conferences of revenue from championship games (including the sale of television rights for those games), and student fees. Large differences exist within the group, however. Division IA schools receive a considerably higher share of revenue from ticket sales (25.4 percent), contributions (20.8 percent), and conference distributions (15.6 percent) than the two other subgroups. That result is not surprising,

considering the much higher profile of the football teams in Division IA (see Table 1).

For its analysis of commercialization, CBO divided athletic departments' revenue into two main categories: commercial and noncommercial, described in more detail in Box 1. Revenue received in exchange for goods or services was classified as "commercial" revenue. Commercial sources include income from ticket sales, conference distributions (most of which derive from the sale of the rights to broadcast championship games), sales of team merchandise, and sales from advertisements. Support from the government and the school, the use of the school's facilities, and student fees were classified as "noncommercial."

Contributions to the athletic programs are more difficult to classify than the other sources. Although some contributions are given purely in support of the program, others guarantee the donor a tangible benefit in the form of a good or service. The data specifically count as contributions any amount paid in excess of the face value of a ticket; those excess values are typically paid in return for preferential seating at games. Payments may also be required before a fan can even become eligible to purchase premium tickets to games; such payments are legally considered partially deductible (80 percent) charitable contributions, despite the clear parallel to fee-for-service commercial transactions. The value of some donations of in-kind merchandise, such as apparel and soft drinks, are counted as contributions in the *Star* data, and those gifts represent an exchange in which the donor is paid with advertising and exposure when teams use their products. Contributions to the programs of the schools in Divisions IAA and IAAA, which have a lower profile, are unlikely to be related to premium ticketing or advertising, but over 90 percent of the total contributions to athletic departments go to Division IA schools, at which those factors are likely to be important. Most contributions thus seem to be related to the exchange of goods or services and therefore are primarily commercial. However, because the data do not specify which contributions are associated with a benefit to the donor and which are not, the tables in this report present the commercial share of revenue both with and without contributions.

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5. The NCAA has recently replaced the names IA, IAA, and IAAA with Football Bowl Subdivision, Football Championship Subdivision, and Division I Non-football, respectively. This paper uses the older terminology for brevity.
  6. Very little information is available regarding the budgets of athletic departments at nonprofit private schools. Those schools and their athletic departments receive the same preferential tax treatment as public schools. The current lack of publicly available information about their programs makes a similar evaluation of their commercialization impossible and could be one justification for mandating additional disclosure of budget information from institutions registered as nonprofits.

**Table 1.**

### Sources of Revenue for NCAA Division I Athletic Programs, Academic Fiscal Year 2004-2005

Source	Average Revenue (Millions of dollars)				Share of Revenue (Percent)			
	All	IA	IAA	IAAA	All	IA	IAA	IAAA
Commercial <sup>a</sup>								
Ticket sales	5.1	8.9	0.5	0.3	21.9	25.4	5.4	4.1
Conference distributions	3.2	5.5	0.5	0.3	13.7	15.6	4.8	3.8
Advertisements	1.3	2.1	0.3	0.2	5.4	5.8	3.1	3.1
Media rights	0.6	1.1	0	0	2.5	3.0	0.1	0.3
Guarantees	0.6	0.9	0.3	0.1	2.4	2.5	2.8	1.4
Items sold on game day	0.6	1.0	0.1	0	2.4	2.7	0.7	0.6
Investments	0.5	0.8	0.1	0.1	2.0	2.2	1.0	0.6
Sports camp	0.3	0.5	0.2	0.2	1.4	1.3	1.6	1.9
Third-party support	0.1	0.2	0	0	0.5	0.5	0.2	0.3
Other	0.5	0.8	0.2	0.2	2.3	2.4	2.0	2.0
Subtotal	12.7	21.6	2.1	1.4	54.4	61.5	21.7	18.1
Noncommercial								
Student fees	3.1	2.9	3.2	3.6	13.2	8.1	32.6	45.8
Institutional support	2.4	2.5	3.0	1.5	10.4	7.0	31.1	19.2
Facilities and administrative support	0.5	0.6	0.5	0.4	2.2	1.6	5.7	5.2
Government support	0.3	0.4	0.2	0.2	1.2	1.0	1.8	1.9
Subtotal	6.3	6.2	6.9	5.7	27.0	17.7	71.2	72.1
Contributions <sup>b</sup>	4.3	7.3	0.7	0.8	18.6	20.8	7.1	9.8
<b>Average Total Revenue</b>	<b>23.3</b>	<b>35.2</b>	<b>9.7</b>	<b>7.9</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
Share of Revenue from Commercial Activities								
Contributions counted as noncommercial	n.a.	n.a.	n.a.	n.a.	54.4	61.5	21.7	18.1
Contributions counted as commercial	n.a.	n.a.	n.a.	n.a.	73.0	82.3	28.8	27.9
<b>Memorandum:</b>								
Number of Schools	164	90	41	33				
Total Revenue, All Schools	3,824	3,166	397	261				

Source: Congressional Budget Office based on data included in the budget reports that all Division I schools submit to the National Collegiate Athletic Association for their athletic programs. The data presented here, which include 164 of the 327 schools in Division I in academic fiscal year 2004-2005, were made available in response to a request by the *Indianapolis Star* newspaper under the Freedom of Information Act.

Notes: The academic fiscal year typically runs from July 1 to June 30.

NCAA = National Collegiate Athletic Association; n.a. = not applicable.

a. Defined as revenue received in exchange for goods or services in a market that also includes taxed businesses.

b. Contributions can be commercial or noncommercial.

When contributions are counted as commercial revenue, 73 percent of the revenue of athletic departments for Division I schools comes from commercial sources; when contributions are considered noncommercial, the share is about 54 percent. Within Division I, however, there are dramatic differences. Depending on whether contributions are considered commercial, athletic departments at Division IA schools receive about 60 percent to 80 percent of revenue from commercial sources, compared with 20 percent to 30 percent for schools in Divisions IAA and IAAA.

### Commercial Activity in Other University Programs

The share of revenue from commercial activity in the rest of the university serves as a useful benchmark in determining whether athletic departments generate a disproportionately high share of revenue from commercial activity.

The Department of Education maintains the Integrated Postsecondary Education Data System (IPEDS), which contains data on revenue from most postsecondary institutions. CBO used those data to estimate the commercial share of total revenue for the entire school. IPEDS includes a category for revenue earned from auxiliary enterprises, defined as “revenues generated by or collected from the auxiliary enterprise operations of the institution that exist to furnish a service to students, faculty, or staff, and that charge a fee that is directly related to, although not necessarily equal to, the cost of the service.”<sup>7</sup> Examples of auxiliary enterprises include residence halls, food services, and athletic departments; all revenue from those sources is classified as commercial.

Many university systems also have hospitals, which serve populations and missions that are somewhat different—though overlapping—from those served by the rest of the university. Although most hospital revenue is received in exchange for services, universities’ hospital services are not typically viewed as a commercial enterprise. Whether hospitals should be considered a fundamental part of the universities’ educational mission is unclear; the share of revenue from the universities’ commercial enterprises shown in Table 2 is therefore presented both with and

without hospitals included in the schools’ overall revenue. Hospital revenue is classified as noncommercial when included in the universities’ total revenue.

With associated university hospitals excluded, the universities as a whole derive almost 11 percent of their revenue from commercial activities when contributions to the university are considered a noncommercial source of revenue. That share rises to about 14 percent when contributions are classified as commercial (see Table 2).<sup>8</sup>

A final consideration is the treatment of athletic programs’ revenue within the overall university. For schools in Division IA, that revenue comes primarily from commercial sources, so including it boosts the share of revenue from commercial sources for the university as a whole. Because the IPEDS data do not have a separate category for the revenue of athletic programs, CBO used the *Indianapolis Star* data to estimate each category of revenue net of the effect of athletic programs.<sup>9</sup>

When athletic departments are removed from the calculation of commercial revenue for the university, the commercial share falls (see Table 2). Excluding hospitals, the share of university revenue from commercial sources is about 8 percent when contributions are considered noncommercial. That treatment of contributions may be more appropriate for the rest of the university than for the athletic department, although individuals or organizations making the largest donations to universities also tend to receive something, such as naming rights, in return. When contributions are considered commercial,

7. Susan G. Broyles, *IPEDS Glossary* (Department of Education, National Center for Education Statistics, rev. August 1995), <http://nces.ed.gov/pubs95/95822.pdf>, p. 28.

8. When hospitals are included in the calculation, the commercial share of revenue is 9.5 percent with contributions considered noncommercial and 12.6 percent with contributions considered commercial.

9. In adjusting the universities’ revenue to exclude revenue from athletic departments, CBO assumed that the schools that did not respond to the FOIA request were similar to those that did. CBO made the adjustment using averages from the *Indianapolis Star* data. For example, the calculation for all university revenue excluding athletics was made by subtracting the average revenue of athletic departments in the *Star* data, multiplied by the number of schools (101), from the total university revenue given in IPEDS. CBO used a similar process to calculate university revenue excluding athletics for contributions and auxiliary enterprises, using the *Star* data averages for contributions to athletic departments and commercial revenue from athletic departments, respectively.

**Box 1.****Sources of Revenue of Athletic Departments**

The data the Congressional Budget Office (CBO) used to determine the sources of revenue of athletic departments in Division I of the National Collegiate Athletic Association (NCAA) are from the request made by the *Indianapolis Star* newspaper under the Freedom of Information Act in 2006. That request was for the budget reports that athletic departments are required to submit to the NCAA. The data include 164 of the 327 schools in Division I in academic year 2004-2005. CBO classified the sources as commercial or noncommercial, as described below; contributions, which can be commercial or noncommercial, were put in a separate category.

**Commercial Sources of Revenue**

Broadly defined, commercial activities provide a good or service in exchange for a fee in a market that also includes taxed businesses. For this paper, CBO classified the following activities as commercial:

**Ticket sales.** Ticket sales to the public, faculty, and students and money received for shipping and handling of tickets. Excludes ticket sales for conference and national tournaments.

**Conference distributions.** Revenue received from participation in bowl games, tournaments, and all NCAA distributions (for example, amounts received for direct participation or through a sharing arrangement with an athletic conference, including shares of conferences' television agreements).

**Advertisements.** Revenue from corporate sponsorships, sales of advertisements, trademarks, and royalties. Includes the value of in-kind products and services provided as part of a sponsorship (for example, equipment, apparel, soft drinks, water, and isotonic products).

**Media rights.** Institutional revenue received directly for radio and television broadcasts; Internet and

e-commerce rights received through contracts negotiated by the institution.

**Guarantees.** Revenue received from home teams for participating in away games.

**Items sold on game day.** Revenue from the sale of programs, novelties, and food or other concessions and from parking fees.

**Investments.** Distributions from an endowment and other investment income in support of the athletic department.

**Sports camp.** Amounts received by the athletic department for sports camps and clinics.

**Third-party support.** All amounts provided by a third party and contractually guaranteed by the institution but not included on the institution's W-2 (for example, a stipend for the use of a car; membership in a country club; allowances for entertainment, clothing, and housing; speaking fees; compensation from camps; and income from radio, television, shoes, and apparel).

**Other.** Accounts for less than 5 percent of total revenue.

**Noncommercial Sources of Revenue**

All sources of revenue not meeting the definition of "commercial" were classified as noncommercial:

**Student fees.** Fees assessed for support of (or the portion of overall fees allocated to) intercollegiate athletics.

**Institutional support.** Includes the value of institutional resources for the current operations of intercollegiate athletics; all unrestricted funds allocated to the athletic department by the university. That support may include state funds, tuition, tuition waivers, and transfers.

Continued



**Box 1.**

Continued

**Sources of Revenue of Athletic Departments**

**Facilities and administrative support.** Includes the value of facilities and services provided by the institution and not charged to the athletic department (for example, an allocation for institutional administrative costs, facilities and maintenance, grounds and field maintenance, security, risk management, utilities, and debt service).

**Government support.** Includes state, municipal, federal, and other government appropriations made in support of the operations of intercollegiate athletics (including funding specifically earmarked for the athletic department by government agencies for which the institution has no discretion to reallocate).

**Contributions**

Contributions were defined as amounts received directly from individuals, corporations, associations, foundations, clubs, or other organizations that are designated, restricted, or unrestricted by the donor for the operation of the athletic program. Examples of contributions are amounts paid in excess of a ticket's value (for example, to obtain premium seating), cash, marketable securities, and in-kind contributions. In-kind contributions may include automobiles provided by dealers (measured as the market value of the use of a car), apparel, and soft drinks for use by staff and teams.

the share of university revenue from those sources is about 11 percent.<sup>10</sup> Clearly, athletic departments derive a considerably higher share of their revenue from commercial activities than do other parts of universities. Depending on how it is calculated, the share of revenue from commercial sources is seven to eight times higher for Division IA athletic programs than for all other functions at those universities. For Divisions IAA and IAAA, the share of commercial revenue for athletic programs is only two to three times as large as for the universities' other activities (assuming that the extent of commercial activity in those schools, apart from the athletic department, is comparable with that in Division IA schools).

Looking at the net income of athletic programs highlights the differences in the commercial nature of programs between the three Division I subgroups (see Table 3). Nearly 99 percent of total net income accrues to Division IA programs, according to the data reported by universities to the NCAA.<sup>11</sup> Average income for programs in Divisions IAA and IAAA is less than a tenth of that in the more commercial Division IA. Those differences in

reported income are discussed later in the context of possible policy changes.

Even in that group of elite Division IA programs, however, more than a quarter of the athletic programs report a deficit each year. That result is more likely to reflect the conceptual difficulties in measuring income rather than a statement about the true underlying profitability of those programs. The correct allocation of revenue and expenses to athletic departments, and thus their net profit, is complicated. There are no rules or even standard practices delineating how schools divide revenue from parking, concessions, or licensing, for example, between the athletic department and the university.<sup>12</sup> On the cost side,

10. Including hospitals, universities derive about 7 percent of revenue from commercial sources when contributions are considered non-commercial and 10 percent of revenue from commercial sources when contributions are considered commercial.

11. The majority of income is, of course, reinvested directly into the athletic programs—for example, into compensation for coaches and administrators. Because the athletes retain amateur status, there are strict limits on their compensation, and they are barred from receiving benefits that are proportional to the income that they earn for the university. Robert W. Brown and R. Todd Jewell (“Measuring Marginal Revenue Product in College Athletics: Updated Estimates,” in John Fizel and Rodney Fort, eds., *Economics of College Sports* [Westport, Conn.: Praeger, 2004], pp. 153–162) estimate that universities earn \$400,000 from each high-performing football player and over \$1 million from each high-performing basketball player.

12. Robert Sandy and Peter Sloane, “Why Do U.S. Colleges Have Sports Programs?” in Fizel and Fort, eds., *Economics of College Sports*, pp. 87–110.

**Table 2.**

## Sources of Revenue for Schools in NCAA Division IA, Academic Fiscal Year 2004-2005

Source	Including Athletic Department	Excluding Athletic Department
<b>Total Revenue, by Source (Millions of dollars)</b>		
Commercial		
Auxiliary Enterprises	8,429	6,245
Noncommercial		
Hospitals	9,833	9,833
All other sources	67,389	66,758
Contributions <sup>a</sup>	2,670	1,931
<b>All Sources</b>	<b>88,321</b>	<b>84,768</b>
<b>Revenue from Universities' Commercial Activities as a Percentage of Total Revenue</b>		
Excluding Hospitals		
Contributions counted as noncommercial	10.7	8.3
Contributions counted as commercial	14.1	10.9
Including Hospitals		
Contributions counted as noncommercial	9.5	7.4
Contributions counted as commercial	12.6	9.6

Source: Congressional Budget Office based on data from the Department of Education's Integrated Postsecondary Education Data System.

Notes: The academic fiscal year typically runs from July 1 to June 30.

The sample includes the 101 public schools in NCAA Division IA.

NCAA = National Collegiate Athletic Association.

a. Contributions can be commercial or noncommercial.

schools generally list the full standard tuition as the cost of an athletic scholarship, even though that measure overstates the true cost of awarding the scholarship.<sup>13</sup> Because accounting practices vary, the reported profit or loss reported here (in Table 3) may be a poor guide to the true financial status of athletic departments.<sup>14</sup>

13. If class sizes are fixed, the cost of granting a scholarship to an athlete is the tuition that would have been paid by another student who cannot now be admitted, and the majority of students do not pay the listed tuition because they receive financial aid in the form of tuition discounting or grants. See Burton A. Weisbrod, Jeffrey P. Ballou, and Evelyn D. Asch, *Mission and Money: Understanding the University* (Cambridge, U.K.: Cambridge University Press, 2008), Chapter 5. If class sizes are not fixed, the cost of granting a scholarship to an athlete could be even less than the net tuition that would be paid by another student, because the athlete's admission does not prevent any other applicant from being admitted.

### Competition with For-Profit Entities

Public and private colleges face relatively little competition from taxable competitors; for-profit postsecondary schools accounted for just 5 percent of total enrollment

14. The profitability of collegiate sports is a matter of continuing debate. On the one hand, Andrew Zimbalist (*Unpaid Professionals: Commercialism and Conflict in Big-Time College Sports* [Princeton, N.J.: Princeton University Press, 1999], Chapter 7) estimates that although the top dozen programs run persistent surpluses and some others may turn a profit during a particularly successful year, the average program runs a deficit of \$710,000 per year once adjustments for some of the reporting problems discussed in the text are made. On the other hand, Brian Goff ("Effects of University Athletics on the University: A Review and Extension of Empirical Assessment," *Journal of Sport Management*, vol. 14, no. 2 [2000]) estimates that only 10 percent of the top 109 programs lose money in a year. He concludes that public universities may underestimate profits by \$800,000 per program and that private schools underestimate profits by even more.

**Table 3.**

### Net Profit or Loss of NCAA Division I Athletic Programs, Academic Fiscal Year 2004-2005

	Number of Programs	Total Net Income or Loss (Millions of dollars)	Subdivision's Share of Total Net Income or Loss (Percent)	Average Income (Millions of dollars)
Division IA Programs				
With net profit	60	141.4	89.9	2.4
With net loss	24	-34.7	70.4	-1.4
That break even	6	0	0	0
Subtotal	90	106.8	98.8	1.2
Division IAA Programs				
With net profit	22	6.7	4.2	0.3
With net loss	13	-2.6	5.2	-0.2
That break even	6	0	0	0
Subtotal	41	4.1	3.8	0.1
Division IAAA Programs				
With net profit	19	9.2	5.9	0.5
With net loss	12	-12.0	24.4	-1.0
That break even	2	0	0	0
Subtotal	33	-2.8	-2.6	-0.1
All Division I Programs				
With net profit	101	157.3	n.a.	1.6
With net loss	49	-49.2	n.a.	-1.0
That break even	14	0	n.a.	0
<b>Total</b>	<b>164</b>	<b>108.1</b>	<b>n.a.</b>	<b>0.7</b>

Source: Congressional Budget Office based on data included in the budget reports that all Division I schools submit to the National Collegiate Athletic Association for their athletic departments. The data presented here, which include 164 of the 327 schools in Division I in academic fiscal year 2004-2005, were made available in response to a request by the newspaper the *Indianapolis Star* under the Freedom of Information Act.

Notes: The academic fiscal year typically runs from July 1 to June 30.

There are no rules or even standard practices delineating how schools divide revenue and costs between the athletic department and the university. The profits and losses reported in this table may therefore be a poor guide to the true financial status of athletic departments.

NCAA = National Collegiate Athletic Association; n.a. = not applicable.

in degree-granting institutions in 2004.<sup>15</sup> When athletic departments function primarily as a part of the educational experience for students, they participate in that nonprofit market. However, highly competitive college sports teams with large-capacity stadiums and prime-time television events with advertising are more reasonably

considered participants in the market for entertainment. They compete for entertainment spending with many other recreational options, but their most direct competitors are professional sports leagues.

Even though competitive university sports programs enter the same market with tax advantages unavailable to the taxable professional leagues, those leagues have never advocated removing tax preferences for the college

15. U.S. Department of Education, *Digest of Education Statistics*, [http://nces.ed.gov/programs/digest/d07/tables/dt07\\_185.asp](http://nces.ed.gov/programs/digest/d07/tables/dt07_185.asp).

programs. One reason may be that college sports tend to reduce costs for professional sports.<sup>16</sup> The two sports with the most active and commercial college programs—football and basketball—are each controlled by a single professional association that spends very little on training players. In many cases, all but the final polishing is done by the colleges while the players maintain amateur, non-paid status.<sup>17</sup> If players were not trained by colleges, the professional leagues would probably have to pay those players a salary and complete the training themselves. Particularly in football, the same lack of other leagues in the market—due at least in part to the partial antitrust exemptions granted to the National Football League (NFL)—has also facilitated explicit arrangements between the NCAA and the NFL that avoid direct competition so that they can jointly maximize revenue. For example, college and professional football teams play on different days of the week during the college season. Once the college football season is completed, professional teams play some games on Saturday, the day usually reserved for colleges.

## The Benefits of Collegiate Athletics

Although this analysis focuses on the commercialization of university athletics, the favorable tax treatment of athletic departments within a university might also be evaluated in terms of the social benefit those programs provide to federal taxpayers, who finance the subsidies the universities receive. Research indicates that student athletes tend to underperform academically relative to their credentials, although there is no clear evidence about whether their participation in competitive athletics creates other types of human capital with social benefits.<sup>18</sup> If student athletes reap less academic benefit from higher education than other, similarly qualified students, the admission preferences they currently have represent a misallocation of education resources.

16. College baseball is an exception in that it competes for players with the minor leagues; even so, the collegiate and professional baseball seasons do not overlap the majority of the time.

17. The lack of compensation for college athletes (despite the substantial revenue that they earn for the university) is one factor encouraging basketball players to forgo college and instead improve their skills in professional leagues in other countries before returning to play for a professional team in the United States. If more athletes decided to play for foreign professional leagues rather than for colleges, the result could be both a decline in the commercialization of college basketball and a decline in its value to the domestic professional league.

Collegiate athletics, like other extracurricular activities, may also enhance the quality of student life in various nonacademic ways that could also have social benefits. Supporters of university athletic programs cite the leadership skills, teamwork, and dedication that student athletes may learn through their participation.<sup>19</sup> Participating in and watching sporting events can also contribute to an institution's sense of community.

Athletics are unique among extracurricular activities, however, because of the expensive infrastructure support associated with providing such benefits to participants. Although some other activities also require facilities that are expensive to construct and maintain, salaries for coaches are higher than those for almost any other university employee, including college presidents, and no other extracurricular activities are provided with academic tutoring programs like those that focus on maintaining athletic eligibility.<sup>20</sup>

Athletic programs might also provide ancillary benefits (in addition to any direct profit from the programs themselves) to the schools, allowing them to further their mission of higher education. Athletic programs could benefit schools indirectly by improving their name recognition or reputation.<sup>21</sup> Successful athletic programs could also encourage increased giving by alumni to a school or improve the quality of the entering class by increasing the

18. See, for example, William G. Bowen and Sarah A. Levin, *Reclaiming the Game: College Sports and Educational Values* (Princeton, N.J.: Princeton University Press, 2003), Chapter 6. The authors concluded that after accounting for the influence of race, field of study, individual scores on the Scholastic Aptitude Test (SAT), and the average SAT score at the institution, athletes who are recruited achieve lower class rank relative to their academic credentials than do walk-on athletes or the general student body. The effect is most pronounced among football players and rowers. Others have noted that graduation rates for football and basketball team members in Division I are considerably lower than those for nonathletes or for athletes in other sports. See Weisbrod, Ballou, and Asch, *Mission and Money*, p. 231.

19. Letter from Myles Brand, President of the National Collegiate Athletic Association, to the Honorable William Thomas (November 13, 2006), [www.ncaa.org/wps/ncaa?ContentID=44636](http://www.ncaa.org/wps/ncaa?ContentID=44636), p. 4.

20. For a comparison of coaches' and university presidents' salaries, see Weisbrod, Ballou, and Asch, *Mission and Money*, pp. 221 and 251–277. For a discussion of spending on tutoring programs for athletes, which the NCAA requires of all Division I schools, see Zimbalist, *Unpaid Professionals*, pp. 43–44.

21. Goff, "Effects of University Athletics on the University," p. 91.

number of students who apply for admission. Although various empirical studies on both of those points have come to conflicting conclusions, overall the evidence indicates that the effect of successful programs on either of those measures at a specific school is likely to be positive but small (see the appendix).

Applying those conclusions to all university athletic programs in the nation—the appropriate level at which to evaluate a federal subsidy—is difficult. Most studies look at the relationship between success, defined by win-loss records or championship wins, and alumni giving or the number of applications at a specific school. Because athletic success is in general a zero-sum endeavor (championship games always have a winner), the relationships that hold for a single or small group of athletic programs may not hold for all athletic programs in the nation. There is no evidence suggesting that athletic programs increase the overall amount of charitable contributions (as opposed to shifting them between different schools or other non-profit organizations) or the average quality of students attending all colleges.<sup>22</sup> Furthermore, the effect of athletic programs on either of those measures seems likely to be dwarfed by that of the many other federal subsidies for charitable giving and higher education. In fact, the current subsidy to athletic departments may simply encourage an “arms race” between schools, in which universities spend increasing resources on measures of athletic success that, at most, benefit their own institutions at the expense of others. Encouraging such competition within the higher education sector seems unlikely to benefit the federal taxpayers that ultimately pay for the subsidy.

## Policy Options

If the Congress decided that some or all of the activities undertaken by college athletic programs are primarily commercial, the rationale for providing preferential tax treatment to those activities would be eliminated or greatly reduced. Changes to the tax preferences could be achieved in one or more of the following ways:

- Limiting the deduction of charitable contributions,
- Limiting the use of tax-exempt bonds, or
- Limiting the exemption from income taxation, either for all or for certain types of income.

Several issues might arise if the Congress decided to eliminate or reduce those tax preferences. Most important, the position of athletic departments within larger non-profit institutions affords many opportunities for shifting contributions, other revenue, or expenditures from one part of the university to another. The budgetary relationship between universities and their constituent parts would significantly reduce the effectiveness of most attempts to limit the general tax preferences for athletics while leaving those for the entire university intact. More targeted changes, such as limiting the types of income statutorily exempt from the unrelated business income tax, are more likely to have an impact but would still require assessing the commercialization of all of the university’s activities rather than just those of the athletic department.

### Limiting the Deduction of Charitable Contributions

Under the Internal Revenue Code, donors to college sports programs may deduct their contributions from their federal adjusted gross income. Many of those contributions, however, are made in order to become eligible to purchase game tickets or to ensure access to premium seating. In effect, the transaction is an exchange of money for valuable rights, and the benefits of the contribution accrue to the donor. Under current law, the donor may nonetheless deduct 80 percent of the value of such contributions.

If the Congress decided that contributions to athletic departments are primarily commercial, it could specify that contributions to universities’ sports programs or to foundations that support them—either contributions given in exchange for certain benefits or all contributions—may not be deducted on the donor’s federal tax return. Money can easily be moved between departments within the university, however, and a university administration can allocate a greater share of its own budget to its sports program. If that fact is well understood by donors and administrators, donations to sports programs might be unaffected by such a policy change; lower explicit donations to the athletic programs could simply be offset by indirect donations through the university.

22. Total charitable donations to all sectors have remained roughly 2 percent of disposable income over time, suggesting that increased donations to higher education are offset by decreased giving to other nonprofits (Weisbrod, Ballou, and Asch, *Mission and Money*, p. 36).

Although such a response might completely offset the effects of a change in the deductibility of contributions, it would probably not do so. Total donations would be likely to decline to some extent, and a school's response would determine how the effects of that decline were shared between the athletic program and other parts of the budget.

### Limiting the Use of Tax-Exempt Bonds

Although contributions can be given to or earmarked for sports programs directly, athletic departments generally do not have borrowing authority that is separate from that of the college or university as a whole. The borrowing is undertaken on behalf of the school and is earmarked for the sports program in the tax-exempt bond offering.

It would thus be more difficult for schools to move borrowing that is earmarked for another part of the university to the athletic department if the Congress prohibited the use of tax-exempt bonds to finance the capital facilities of sports programs. Even so, it might be possible for the university to borrow indirectly for the sports program. If the university could not use the proceeds from bonds directly for the sports program, it could still borrow for capital spending in other areas that would have been financed with operating revenue and use that operating revenue to finance the sports facilities. The major problem would be the large amount of revenue needed—the university might not have adequate capital facilities being financed with operating revenue to make the substitution. Thus, eliminating the direct use of tax-exempt bonds for sports facilities would be unlikely to eliminate their use but would probably have a bigger effect on the total amount of bonds a university issues than the elimination of charitable contributions would have on total charitable contributions.

### Limiting the Exemption from Income Taxation

Attempts to end the exemption from income taxation for athletic departments would probably encourage universities to undertake significant efforts to avoid taxes. A sports program's position within a much larger institution makes successful taxation of its true net income a difficult undertaking. Changing the treatment of income from specific sources, such as royalty income or income from corporate sponsorships, might be effective, especially if the changes applied to the entire university rather than just the athletic program.

**Subject the Income of Athletic Programs to the UBIT.** The Congress could, by statute, reclassify collegiate athletic programs as unrelated commercial entities operated by a nonprofit organization, thereby subjecting them to the unrelated business income tax.<sup>23</sup> Because an athletic program in a nonprofit private or public postsecondary institution is part of a much larger economic entity that would remain classified as a nonprofit, the institution would have a substantial incentive to shift costs from the untaxed portion of the university to the taxable portion and to shift income in the other direction. Increased net income would have no tax consequences for the untaxed sector, and increased costs would reduce or eliminate taxable net income for the athletic program.<sup>24</sup>

Universities have other means of eliminating taxable income if cost shifting failed to do so completely. Unlike a for-profit enterprise, which has shareholders who expect managers to distribute a surplus as dividends or retain the surplus and distribute it in the future as capital gains, the nonprofit or public enterprise has no shareholders. If athletic programs still showed a profit even after income or cost shifting, that profit could be reduced or eliminated in two ways. First, the program could increase costs by paying higher wages to coaches or administrators or by spending more for other items, such as athletic facilities.<sup>25</sup> Second, the program could reduce revenues—for example, by lowering the price of game tickets. Directors of athletic programs might prefer to use one of those alternatives rather than pay taxes; all of the alternatives would reduce the income subject to tax.

23. For an in-depth discussion of the legal argument for applying the UBIT to college athletics under current law, see John D. Colombo, "The NCAA, Tax Exemption, and College Athletics" (*University of Illinois Law Review*, forthcoming; also available at <http://papers.ssrn.com/abstract=1336727>).

24. Joseph J. Cordes and Burton A. Weisbrod ("Differential Taxation of Nonprofits and the Commercialization of Nonprofit Revenues," in Burton A. Weisbrod, ed., *To Profit or Not To Profit* [Cambridge, U.K.: Cambridge University Press, 1998]) conclude that nonprofits subject to the UBIT may shift expenses that are up to one-third of their gross profit to the taxable portion of the entity.

25. The large number of programs that currently post a loss (see Table 3) may suggest that those behaviors already occur; administrators and coaches may be able to extract higher salaries from those nonprofit programs because such programs have no incentive to show a profit.

**Restructure the Relationship Between Athletic Departments and the University.** The schools' ability to shift income from one part of their budget to another is likely to prevent the net income of collegiate athletic programs from being taxed. To prevent such shifting, the Congress could require that the financial relationship between athletic programs judged to be commercial and their universities be severed completely. Like any commercial entity, the athletic programs could still lower their tax liability by reducing revenue or increasing costs, but they would be limited in doing so by their need to raise capital.

Such a major restructuring of the relationship between athletic departments and universities would present a variety of practical and political issues. Perhaps most important, it would be extremely difficult to implement effectively at the public universities that host most of the major sports teams. The Congress has made many changes to the exemption for nonprofit institutions, including imposing the unrelated business income tax. But the IRS has considered every commercial activity undertaken by a state or local government to be an essential public service and therefore not subject to taxation. Taxing a public entity would raise legal issues with regard to intergovernmental tax immunity. At the moment, the tax law treats nonprofit and public enterprises very differently. Therefore, a state institution of higher education operating a sports program classified as a commercial enterprise would be subject to the UBIT under that approach, but a state operating the identical sports program as a state entity not affiliated with its public university would not.

**Reclassify Certain Types of Income.** Instead of attempting to classify all net income from athletic programs as commercial and subject to the UBIT, the Congress could consider reclassifying certain types of income typically earned by those programs as unrelated income. For example, an athletic program earns royalty income when it receives a payment in exchange for allowing a for-profit enterprise to use its name. Current law excludes all royalty income from the UBIT because such income is considered passive. In general, passive income, which also includes income from investments, is not considered commercial because it is not derived from direct competition with commercial enterprises.

Some types of royalty income may reasonably be considered more commercial than others. The royalty income

derived from the ownership of mineral and oil rights is usually a clear example of passive income; universities own the land to which such rights are attached but have little or no involvement in the ongoing commercial activity that occurs. In contrast, when colleges and universities license team names, mottoes, and other trademarks to for-profit businesses that supply apparel, accessories, and credit cards to the general public, they approve each product and use of their symbols and, in some cases, exchange information, such as donor lists, with the licensees to aid in their marketing. In 2005, the collegiate sector earned \$203 million in that type of licensing revenue.<sup>26</sup> The manufacture or sale of such items would clearly be commercial—and subject to the UBIT—if undertaken directly by the schools. Schools' active involvement in generating licensing income could be the basis for considering such income as commercial and therefore subject to the UBIT. Even the income from mineral rights has been determined taxable if the university is substantially involved in the daily operation of such properties.

Bringing royalty income that accrues only to athletic departments under the UBIT would be problematic, however, for several reasons. First, schools could simply limit their licensing of the names and trademarks of their athletic teams and increase their licensing of the school's name and trademarks to minimize the amount of taxable activity, although doing so would be likely to decrease sales. More important, if royalty income from licensing team names to for-profit businesses was truly considered commercial and subject to the UBIT, the same arguments would apply in full force to licensing all other university names and trademarks. A consistent policy would subject all such income to the UBIT because of its commercial nature. Such a change in policy could affect many other nonprofits in addition to colleges and universities, although the amount of all commercial activity in athletic departments relative to that undertaken by universities and other nonprofits does provide a rationale for different treatment.

Income from corporate sponsorship is also explicitly excluded from the UBIT. Generally, sponsorship income arises from corporate payments made in exchange for associating the corporate name with the nonprofit or public institution. In the context of college athletics,

26. Weisbrod, Ballou, and Asch, *Mission and Money*, p. 245.

most major college championship games, stadiums, and arenas have a corporate sponsor whose name is included in the name of the event or facility. The IRS considered subjecting such income to the UBIT in 1991. In the Taxpayer Relief Act of 1997, however, the Congress responded by excluding “qualified sponsorship payments” from the UBIT, defining such payments as those in return for no other benefit than the acknowledgment of the sponsor. The law makes a distinction between payments in return for advertising (which includes descriptions of the sponsor’s products, locations, or other features) and payments in return for adding the sponsor’s name to an event or facility (which is not considered a substantial benefit). The NCAA estimated that corporate sponsorship payments to all athletic programs totaled \$275 million in academic year 2004-2005.<sup>27</sup>

The fact that sponsors of athletic facilities and bowl games are willing to pay large sums in qualified sponsorship payments suggests that they derive some benefit from the prominent location and display of their corporate trademarks during athletic contests and national broadcasts. If the Congress decided that those benefits were essentially similar to those conferred by advertising as defined in the law, it could reclassify such payments as taxable income from an unrelated business. Such a determination would be supported not only by the commercial nature of those specific transactions but also by the commercial nature of athletic departments themselves, in

contrast to other nonprofits that earn some revenue from similar sources while remaining financed primarily by noncommercial activities.

However, not all payments for naming rights at athletic facilities really are in return for a substantial benefit; the benefit to the sponsor varies considerably among schools and is of course largest for the few schools whose athletic arenas attract extremely large crowds and host widely televised events. The range of success among programs—and thus the benefit in being a sponsor—implies that a blanket determination of “substantial benefit” from all sponsorships could be unreasonable. The situation is clearer in the case of sponsors of championship games. Title sponsors of widely televised events such as bowl games clearly receive a substantial benefit from their sponsorship. If the Congress determined that such transactions are commercial, it could specifically classify sponsorship payments for those particular athletic contests as taxable income.

Even reclassifying certain types of income might fail to be effective if the policy was intended to apply only to athletic departments. Unless the treatment of such income was consistent across the entire university, strong incentives would remain to shift income taxable to the athletic department to the nontaxed portion of the university. However, reclassifying certain types of income as unrelated, and therefore taxable, would have the advantage of focusing directly on the types of revenue that are associated with the relatively few highly commercial athletic departments rather than on the majority of athletic departments that engage in little commercial activity.

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27. Letter from Myles Brand to the Honorable William Thomas (November 13, 2006).





## Appendix: Research on Certain Benefits of Intercollegiate Sports

**A**lthough the extent of commercialization in college sports provides one basis for evaluating athletic programs' access to federal subsidies intended for nonprofit organizations, other factors may also play a role. For example, many supporters of university athletics argue that a successful athletic department creates benefits for colleges and universities that are then passed on to the students. Numerous studies have attempted to prove or disprove that notion.

Athletic success is generally thought to benefit schools in one of two ways: by increasing donations to the school or by increasing the pool of applicants for admission. Research on the relationship between athletics and donations has used a variety of measures of athletic success and has come to conflicting conclusions. One study, for example, found that winning percentages in the major sports did not have a significant effect on donations.<sup>1</sup> A larger study reached a similar conclusion regarding winning records, but the authors documented a positive relationship between giving and appearances in championship games.<sup>2</sup> Using a panel data set of 320 institutions, a third study concluded that postseason success in football and basketball leads to increased gifts restricted for the use of the athletic department for some schools but no increase in unrestricted giving to the university.<sup>3</sup> Another study, using detailed data from a single large university,

found little relationship between teams' general success and donations but found a significant increase in donations for some alumni when a sport in which they had participated was successful.<sup>4</sup> Overall, those studies seem to indicate that postseason success may increase restricted donations to the athletic department by particular alumni but that the effect on total giving to the university is likely to be small.

The results of research on the relationship between athletic success and the quality of entering classes are equally inconsistent. One study documented a positive relationship between advancing in the National Collegiate Athletic Association (NCAA) basketball tournament and Scholastic Aptitude Test (SAT) scores for the entering class.<sup>5</sup> In contrast, another study found that championships increased the number of applications but had no effect on the SAT scores or grades of entering students.<sup>6</sup> A comprehensive study of the effects of athletic success

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1. Paul W. Grimes and George A. Chressanthis, "Alumni Contributions to Academics: The Role of Intercollegiate Sports and NCAA Sanctions," *American Journal of Economics and Sociology*, vol. 53, no. 1 (1994), pp. 27–40.
  2. Robert Baade and Jeffery Sundberg, "Fourth Down and Gold to Go? Assessing the Link Between Athletics and Alumni Giving," *Social Science Quarterly*, vol. 77, no. 4 (1996), pp. 789–803.

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3. Brad R. Humphreys and Michael Mondello, "Intercollegiate Athletic Success and Donations at NCAA Division I Institutions," *Journal of Sport Management*, vol. 21, no. 2 (April 2007).
  4. Jonathan Meer and Harvey S. Rosen, *The Impact of Athletic Performance on Alumni Giving: An Analysis of Micro Data*, Working Paper No. 13937 (Cambridge, Mass.: National Bureau of Economic Research, April 2008).
  5. Franklin G. Mixon Jr., "Athletics versus Academics? Rejoining the Evidence from SAT Scores," *Education Economics*, vol. 3, no. 3 (December 1995), pp. 277–283.
  6. J. Douglas Toma and Michael Cross, "Intercollegiate Athletics and Student College Choice: Understanding the Impact of Championship Seasons on the Quantity and Quality of Undergraduate Applicants" (paper presented at the 21st Annual Meeting of the Association for the Study of Higher Education, Memphis, Tenn., October 30–November 2, 1996).

on the quality of incoming students concluded that the percentage of games won was positively correlated with the quality of the students but that the effect was generally small and statistically insignificant; the authors also reached similar conclusions about the relationship between winning and alumni donations.<sup>7</sup> Another paper examined a separate mechanism through which athletic success could provide benefits to public schools—increased state funding. The author found that schools with a Division IA football program receive significantly more in state funding than those without one but that an

increase in the success of the program does not raise the amount of appropriations it receives.<sup>8</sup>

Although the studies reach conflicting conclusions, even in the studies that find that successful athletic programs have a positive impact on the school overall, the measured impacts are generally quite small. In addition, studies that demonstrate a positive impact for a single school or a subset of schools do not address whether success in intercollegiate athletics increases donations or student quality at all schools—or simply shifts them between schools.

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7. Robert E. Litan, Jonathan M. Orszag, and Peter R. Orszag, *The Empirical Effects of Collegiate Athletics: An Interim Report* (prepared by Sebago Associates for the National Collegiate Athletic Association, August 2003), [www.ncaa.org/databases/baselineStudy/baseline.pdf](http://www.ncaa.org/databases/baselineStudy/baseline.pdf).

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8. Brad R. Humphreys, “The Relationship Between Big-Time College Football and State Appropriations for Higher Education,” *International Journal of Sport Finance*, vol. 1, no. 2 (May 2006).