

## Image rights – it is time for certainty and clarity

The tax treatment of image rights is contentious in many countries, South Africa included. Lionel Messi the hero of Spanish football, recently paid €5m to the tax authorities after he had been charged with tax evasion in respect of the sale of the commercial rights to use his image, autograph and name (“image rights”). The charges arose from the income from the sale of Messi’s image rights to offshore companies. The perceived value of image rights was also rumoured to be an important aspect of the talks surrounding Gareth Bale’s record breaking transfer from Tottenham Hotspur FC to Real Madrid. In the UK it has been reported that several football clubs in the Premier League have settled disputes with HM Revenue and Customs (\*HMRC) regarding the taxation of image rights.

The commercialisation of their image rights by famous sportsmen is common place: in the UK sportspersons often dispose of their image rights either an agent, to an offshore company or to the club which the sportsmen are contracted with.

When footballers are contracted to a club the more famous footballers will typically enter into two types of agreements. The first agreement will be a standard fixed term contract of employment with the club under which a salary is paid to the footballer to play for the club. The second agreement is a image rights transfer agreement whereby the footballer is required to transfer his image rights in exchange for payment. For the duration of the image rights agreement, the footballer will divest himself of the rights to exploit or use his image and autograph for personal gain and the club or agent who has acquired these rights, will exploit them for commercial gain.

In a Draft Guide on the Taxation of Professional Sports Clubs and Players<sup>1</sup>, SARS stated that “image licensing agreements” involving the commercial exploitation of a player's image form part of the player’s gross income and will therefore be included in his or her taxable income. SARS regard payments for image rights as being similar “to endorsement fees and appearance fees as all three form part of a sports player's remuneration, are of a revenue nature and are accordingly taxable”. SARS requires PAYE to be deducted from payments in respect of image rights, irrespective of whether these payments are made to agents, to companies owned by the agents or to the players themselves.

Is there merit to this stance, or are SARS “behind the times” and should legislation be introduced to deal with topic? Certainly, in the UK, as in SA, the protection by players (for convenience we will call them footballers) of their image rights rely on an unsatisfactory combination of privacy law, licensing agreements and passing off protection. There is doubt whether SARS’ stance is correct, and although

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<sup>1</sup> DRAFT GUIDE ON THE TAXATION OF PROFESSIONAL SPORTS CLUBS AND PLAYERS, page 15

the answer depends on the merits of each matter, it is clear that image rights are recognised in many countries as an asset that can be commercially exploited, and as such, as something separate from the services that a player will render to his employer club.

From a tax perspective, the employment agreement with the footballer would attract Pay As You Earn ("PAYE"). However, the second agreement, which involves a once-off payment to the footballer for the disposal of (arguably) a capital asset, is a contentious issue.

There are two schools of thought about the taxation of image rights. Currently SARS take the view that any payment to a player is for services performed. This, in their view, includes public appearances using their image or autograph, for the club or sponsors. As a consequence, any payment for image rights is treated by SARS as revenue. If the payments for image rights are made by the employer, they are obliged to deduct PAYE in respect of such payments. SARS go one step further: even if the employer/club makes the payment for the image rights, to an agent, or to a company which acquires the image rights, SARS regard this as a gross income in terms of paragraph (c)(ii) of the definition of gross income and requires employer's tax to be withheld from these payments as well.

The other view is that image rights are capital in nature and therefore, any receipt in respect of the disposal of these rights, are not revenue and should (depending on the facts of each matter, of course) typically be taxed as a capital gain. The distinction between capital and revenue is central to the treatment of image rights. There is no standard test to determine whether accrual or receipt of image rights payments is of a capital or revenue nature and the answer will depend on the facts of each case.

In the sports industry there is a difference between salaries paid to sportsmen and payments for image rights. The latter are analogous to restraint of trade payments. When a sportsman disposes of his image rights he sterilises an asset that could have been used by him to generate income. When a person undertakes not to exercise a trade, profession or occupation in a specified area for a defined period of time in return for compensation, the payments received in respect of the restraint of trade are capital in nature. When a footballer disposes of his image rights, he relinquishes an essential part of his or her ability to generate additional income.

SARS has promulgated legislation in respect of restraint payments and in our view, it should also publish legislation to deal with image rights. Why not, for example, recognise that certain sportsmen have image rights that are capable of commercial exploitation? If the tax authorities fear abuse or avoidance, they could place a cap on the percentage of the sportsman's income that can be allocated

to image rights, with exceptions being made for players who can prove the commercial value of their image rights.

The contrasting view is to treat all payments to sportsmen as “remuneration” and subject to PAYE. Although this may be attractive to the tax authorities, it ignores the commercial reality that certain players have valuable image rights.

It still remains to be seen how the SARS will choose to treat image rights payments made to sportsmen and their agents. Payments for the use of image rights are common place in all sporting industries. It is necessary to clarify whether payments made for the use of image rights are capital or remuneration in order to prevent industry wide disputes between clubs, players and SARS.