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The Legal Implications of the Privatization of Kentucky's Athletics Department



The privatization of Kentucky's athletic department has significant implications on the future of college sports. Stock photo via Kentucky Athletics

by [Jake Bridges 19](#)

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Privatization is beginning in college athletics. This past April, the University of Kentucky [announced the transition](#) of its athletic department to a limited-liability holding company (LLC), forming Champions Blue LLC. Here are some of the legal implications of that move, along with insight into why Kentucky made it.

The move changes the way the university can compensate its athletes. As per the [House Settlement](#), direct school-to-athlete payment is capped: schools have \$20.5 million with which they can compensate their athletes. That remains the same. What changes is that through Champions Blue LLC, Kentucky can essentially offer its own athletes NIL deals.

Clay M. Grayson, founder of Grayson Law Firm, explained the details in an [article](#) published by [sportsbusinessjournal.com](#).

“With the newfound ability of schools to engage student athletes directly post-house, these for-profit LLCs can function like NIL collectives,” Grayson said. This means that UK’s athletic department, Champions Blue LLC, could offer its athletes NIL deals.

Grayson highlights the significance of this, saying that if the university grants the LLC the right to commercialize UK’s athletic multimedia rights and branding, the LLC can then pay Kentucky athletes to promote Kentucky athletics, and pay them fair market value for that service.

According to Grayson, universities typically contract out the management of these rights to third-party companies, which then pay athletes for promotional work. By turning their athletic department into a for-profit LLC, Kentucky can cut out the middleman.

Grayson also highlights that the change to an LLC means that all athletic department personnel go from government employees to employees of a private company. Public universities like Kentucky are governmental institutions and are subject to governmental regulations such as employee compensation caps. Champions Blue LLC is not subject to such regulations.

There are also tax-related reasons for the decision. In a [jmco.com article](#), Certified Public Accountant and financial advisor to multiple universities, **Katie Davis**, explained how.

Legally separating athletics from the university as a whole serves as a strategy to protect the tax-exempt status of the school.

Public universities are typically nonprofits. Davis explains that when a nonprofit earns income from operations that are not significantly related to its stated mission, unrelated business income tax (UBIT) can be applied. While college athletics have not been subjected to UBIT in the past, Davis says the significant commercial growth seen in recent years has led to discourse about whether UBIT should be applied to income derived from college sports.

The creation of Champions Blue LLC shields the University of Kentucky from that potential taxation.

The direct payment of athletes by universities also has the potential to be seen as a private benefit violation, says Davis, if those universities are tax-exempt nonprofits. If a tax-exempt nonprofit is seen by the Internal Revenue Service (IRS) as serving the benefit of private individuals (athletes) rather than its stated purpose (education), it can be subject to financial penalties.

Davis says that “By creating a collegiate athletic LLC to handle these commercial (and potentially taxable) operations, a university might be able to reduce its exposure to both UBIT and private benefit scrutiny.”

Exactly how the LLC and university will be taxed is unclear. It depends on the specific legal structure and tax election of the LLC, says Davis, which is unknown.

A few other schools, such as the University of Florida and Florida State University, have transitioned their athletic departments to LLCs in the past. Kentucky’s transition has gained attention because they were the first university to make the change in the post-house era.

Grayson thinks that the outcome of the house settlement will cause the practice to become more commonplace, even though the vast majority of schools have yet to make the jump. Grayson says “More likely than not, universities already have these structures in place, ready and waiting.”