

## ARTICLES

# THE ECONOMICS OF SPORTS LEAGUES — THE CHICAGO BULLS CASE

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### I. INTRODUCTION

Over the last two decades or so, there have been a number of anti-trust cases brought against sports leagues. Some have involved restrictions on competition for players; many have involved relocations or planned relocations by individual teams. In these cases, the plaintiff has typically claimed that the teams that comprise a given league have conspired to restrain competition among them. The defendant leagues have denied that such a thing is possible — arguing that they are either, de facto, a single entity incapable of conspiring with itself or, at a minimum, a joint venture acting pro-competitively.

This paper lays out the economic analysis involved in understanding such issues, using as a leading example the case of the Chicago Bulls and WGN (the independent television superstation in Chicago) versus the National Basketball Association.<sup>1</sup> Professor Fisher, one of the co-authors, was the economic expert testifying on behalf of the NBA in the second of two lawsuits relating to this matter.<sup>2</sup>

The matter began in 1990 when the NBA, and its member teams, voted to reduce the number of games that could be telecast by a superstation. WGN and the Bulls filed suit, challenging the rule under the antitrust laws. The trial court ruled in favor of the plaintiffs, a decision that the Appellate Court upheld.<sup>3</sup> In the Appellate Court's decision,

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1. See *Chicago Prof'l Sports Ltd. Partnership v. National Basketball Ass'n*, 961 F.2d 667 (7th Cir. 1992).

2. Professor Fisher was supported in his analysis by Charles River Associates.

3. See *Chicago Prof'l Sports Ltd. Partnership*, 961 F.2d at 667.

however, Judge Frank Easterbrook appeared to suggest that had the NBA "transferred to the networks either the right to show or the right to blackout any additional games," the Sports Broadcasting Act might have protected the NBA's twenty-game rule.<sup>4</sup> The Supreme Court declined to review the case.<sup>5</sup>

On April 27, 1993, in response to Judge Easterbrook's opinion, the NBA's Board of Governors adopted four resolutions. They first amended the NBA's bylaws so that the NBA held the copyrights for all NBA games and their telecasts. The second resolution authorized each member team to license local market telecasts. A third resolution approved the agreement that had been negotiated, but not yet executed, between the NBA and NBC, granting NBC the exclusive over-the-air national network NBA telecast rights and providing a degree of exclusivity for cable telecasts. The fourth resolution repealed the NBA's prior rules regarding superstition telecasts.

The NBA petitioned the court, asking that it rule on the legality of the resolutions. A new trial was scheduled.<sup>6</sup> The NBA believed that the question in the new case before the late Judge Hubert Will did not concern the legitimacy of superstition restrictions. It contended that the question before the court was rather whether the NBA has the right to "exploit [the] national market on behalf of all the teams."<sup>7</sup> The NBA believed that its revised television policies, whether judged under the Sherman Act<sup>8</sup> or the Sports Broadcasting Act,<sup>9</sup> were legal.

In 1995, Judge Will again found in favor of the Bulls and WGN, and the NBA was required to permit the superstition WGN to televise Bulls

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4. *Id.* at 671. At the time of the first trial, it was the NBA's position that since its rules gave it control over the copyrights of NBA games, such control was as good as ownership. See *Chicago Prof'l Sports Ltd. Partnership v. National Basketball Ass'n*, No. 90-C 6247 (N.D. Ill. 1993) (Defendant's Opening Argument, Vol. 1 at 72). The courts apparently did not reach the same conclusion.

5. See *National Basketball Ass'n v. Chicago Prof'l Sports Ltd. Partnership*, 506 U.S. 954 (1992).

6. See *Chicago Prof'l Sports Ltd. Partnership v. National Basketball Ass'n*, 874 F. Supp. 844 (N.D. Ill. 1995).

7. *Chicago Professional Sports Ltd. Partnership v. National Basketball Ass'n*, No. 90-C 6247 (N.D. Ill. 1993) (Defendant's Opening Argument, Vol. I at 76). The NBA argued that if it is lawful for the teams, collectively, to grant an exclusive license to one over-the-air network instead of another (e.g., NBC instead of CBS), it must also be lawful for the teams, collectively, to grant an exclusive license to one national over-the-air or cable television network instead of another. From an antitrust standpoint, the vertical restriction was the same. See *id.* at 109.

8. See 15 U.S.C.A. § 1 (1999).

9. See 15 U.S.C.A. § 1291 (1999).

games. Using a “quick look” standard, Judge Will concluded that the NBA’s superstation policies were illegal and that any attempt by the NBA “to prevent WGN and the Bulls from televising any games is a naked restraint on output which will reduce the product available to consumers. . . .”<sup>10</sup> At the same time, in keeping with the 1992 Appellate Court decision, Judge Will ruled that the Bulls and WGN could be required to pay the NBA a fee for telecasting Bulls games on a superstation.<sup>11</sup> He urged plaintiffs and defendants to attempt to negotiate the license fee. When the two sides were unable to agree on a price, Judge Will set the fee at roughly \$40,000.00 per game, less than one third the approximately \$138,000.00 per game that the NBA had sought.

Judge Will’s opinion was appealed by the NBA and in September 1996, the Appeals Court vacated the district court decision and remanded the case for a new trial.<sup>12</sup> Writing on behalf of the Appellate Court, Judge Easterbrook stated that the “NBA is sufficiently integrated that its superstation rules may not be condemned without analysis under the full Rule of Reason.”<sup>13</sup> Judge Easterbrook further noted that for plaintiffs to prevail, they must establish “that the NBA possesses power in a relevant market, and that its exercise of this power has injured consumers.”<sup>14</sup> Shortly after the Appellate Court decision, the two sides reached a settlement, permitting WGN to telecast an unlimited number of Bulls games to the Chicago audience while restricting the superstation telecasts outside Chicago.<sup>15</sup> Outside of Chicago, WGN was permitted to telecast twelve games for the remainder of the 1996-97 season and fifteen games for each of the following four seasons. In speaking with the press, NBA Commissioner David Stern said that he was pleased that the agreement recognized “the NBA’s exclusive right to license game telecasts in the national market.”<sup>16</sup>

As we noted above, the decisions in the case partly turned on interpretations of the Sports Broadcasting Act, about which we have little to say. The issues arising in the Bulls case well illustrate the economic issues generally involved in analyzing antitrust issues arising in the context

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10. *Chicago Prof'l Sports Ltd. Partnership*, 874 F. Supp. at 862.

11. *See Chicago Prof'l Sports Ltd. Partnership v. National Basketball Ass'n*, 874 F. Supp. 844, 865 (N.D. Ill. 1995).

12. *See Chicago Prof'l Sports Ltd. Partnership v. National Basketball Ass'n*, 95 F.3d 593 (7th Cir. 1996).

13. *Id.* at 600.

14. *Id.*

15. *See Elliott Harris, Bulls, NBA, WGN End Long Battle*, CHI. SUN-TIMES, Dec. 13, 1996, at 129.

16. *Id.*

of sports leagues — issues that, we believe, are not sufficiently well understood by either lawyers or economists.

## II. EXTERNALITIES AND MARKET FAILURE

To begin, it is first useful to consider a general concept that is central to the understanding of the economics of sports leagues. That is the subject of what economists call “externalities.”

The central propositions of microeconomics explain how markets operate to turn the unfettered individualistic pursuit of private ends to the benefit of the public as a whole. Put a bit less loftily, a competitive system leads to the efficient allocation of resources and the enhancement of consumer welfare because consumer tastes and resource costs are reflected in the private profit and loss calculus performed by the competing agents in the economy. If there is one proposition that economists have to communicate to the outside world, it is this.

But if there is a second proposition that economists have to communicate to the outside world (and perhaps to other economists who have only mastered the first one), it is one that concerns the circumstances under which the first proposition is false. In particular, markets fail to lead to socially desirable results if there are public costs and benefits that are *not* reflected in the private profit-and-loss calculus of competing agents. When that happens, the actions of one agent impose a cost or confer a benefit on others that the given agent fails to take into account. This phenomenon is called an “externality.” Externalities can be positive or negative, depending on whether it is the benefits or the costs that are not taken into account, but this paper concentrates on the case of negative externalities. Examples are easy to come by: a factory that emits air pollutants imposes an externality on the downwind population, or more apt for our purposes is the case of an oil field in which the unfettered attempt by landowners to lift oil before their neighbors (under the “Rule of Capture”) leads to major cost increases for everyone and to a serious reduction in the amount of oil that can be economically recovered.<sup>17</sup>

Externalities can be handled by regulation or in other ways. In the case of oil fields, one such way is through unitization — a system in which the entire field is run as a unit. In that case, the externality ceases to exist as such; it becomes internalized, and the private profit and loss calculus of the single field operator appropriately accounts for the public cuts and benefits of his or her actions.

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17. See EUGENE ROSTOW, A NATIONAL POLICY FOR THE OIL INDUSTRY 17-18 (1948).

All of this is as relevant to understanding sports leagues as are the performance statistics of players.

### III. THE PRODUCT AND EFFICIENT ORGANIZATION OF A SPORTS LEAGUE

It appears elementary that whatever product a sports league produces, that product cannot be produced by a single team. Why not? One might say that the reason is that a single team cannot play itself, but that is not true. One can certainly imagine different squads of the same team playing each other. In fact, however, such intramural scrimmaging would lack the interest of a true sports event. Fans would consider it — correctly — an exhibition rather than a true contest. The real reason that a single team cannot produce the product of a sports league is that an essential part of that product involves genuine competition on the playing field. One team alone cannot produce that.

Indeed, one can go farther than this. Even two teams, or a small number of teams, cannot create the product that is produced by a sports league. That product is a series of games in the context of a league season. The elements of standings, playoffs, and championships, are a very large part of what creates fan interest. Those elements require a league with a non-negligible number of teams.

How then should a league be organized so as to produce that product efficiently, that is, to produce it in a way that makes it best able to compete with other entertainment products? For that is what the league's product does; even television viewers on Monday nights in autumn choose between football and other programs, and, as we shall see, competition is wider than that. One possibility would be for a league literally to be a single entity — a single, centrally controlled corporation, with branches in different cities. Some leagues have chosen to do this: the unsuccessful World Tennis League of some years ago and Major League Soccer are examples.

Most leagues, however, have chosen a different model, and it is easy to see why. To create and maintain interest in a league's product requires that fans perceive that the seasonal contest is a real one — a contest, so far as possible among entities that truly compete on the sports field and are, at least so far as that competition is concerned, as independent as possible. This requirement stems from the same source as the fact that a league's product cannot be produced by a single team. A league that is literally organized as a single, centrally controlled entity is a league that can only put on exhibition games. No matter how good those games are and how fair the league's management is in assigning players and

coaches to different cities, the excitement of a true league season and championship competition will be missing if fans perceive that the entire affair is controlled at the center with no real local autonomy. An example of such a product is wrestling, where it is popularly believed that televised wrestling matches are essentially rigged and not genuine contests. Regardless of the validity of this belief, the public's perception derives, in part, from the lack of both a championship season and local autonomy.

League sports demand a form of organization in which local autonomy is both present and seen to be so. Moreover, there are other, subsidiary benefits from such a form. For example, local knowledge and local contacts are likely to prove very desirable in dealing with local authorities and local media. If such subsidiary reasons are all that is involved, a league might organize as a single entity with local profit centers. But the requirement that local autonomy be seen to be present rules that out. To preserve interest in the league's product, the teams must be seen to act independently in competing for players and for coaches, and in competing on the field of play. The interests of the team owners in winning must be both genuine and made manifest in what they do.

As a result, successful leagues are typically organized with separate owners of separate teams and with decisions made at the local level, so far as possible. "So far as possible," but not farther, and here is where the problem of externalities comes in.

#### IV. DEALING WITH EXTERNALITIES: COMPETITION FOR PLAYERS

When, in order to produce its product, a league organizes as a set of formally independent teams, it necessarily faces a problem of incentives. The requirement that teams be seen to operate independently must be balanced against the possibility that the incentives to such independent action will lead to results profitable for one or more teams but detrimental to the league and its customers as a whole.

This is an externality problem. It arises when the profit and loss calculus of particular teams do not fully take into account the costs and benefits to the league as a whole. Were leagues organized as centrally controlled operations, such problems would not exist; in effect, the externalities would be internalized as in the earlier oilfield example.

Many, if not all, of the regulations that leagues impose on their members address externalities.

For example, consider the case of competition for players. If a league's product is to be attractive, then the on-field competition must be exciting. Interest may not be consistently maintained if, over a long

period and across the entire country, one or two greatly superior teams consistently and completely dominate the competition.<sup>18</sup> But if individual teams have complete autonomy in the hiring of players, richer owners or owners in large cities will have an incentive to buy up the best players. This will be in their own interest, but it will not be in the interest of the league as a whole, whose interests we shall see are aligned with those of consumers.

To deal with this externality and to secure a "level playing field," leagues place restrictions on the way in which teams can compete for players. The best-known and most obvious restriction is the draft. Instead of being permitted to compete freely to hire the best college players, teams must choose players in a certain order, typically with those teams that have the worst records going first. Note that this not only prevents rich teams from acquiring the best new players, and not only favors the poorer-performing teams, it also allows teams to exercise (and fans to witness) their independent judgment, so far as possible. This helps to maintain interest in the game.

Dealing with externalities involving players does not end with the draft, however. In order to prevent rich teams or teams in large cities from acquiring all the best players, it is also necessary to restrict the extent to which players can change teams. (This also helps to maintain interest in the league's product by promoting local fan loyalty.) Accordingly, leagues have a long history of such restrictions, which have become lighter over the years.

The lightness of such restrictions has, of course, largely been due to actions by players and decisions by courts. While restrictions on player mobility are necessary for the production of a league's product and enable that product to compete more effectively with other entertainment offerings, such restrictions in the past clearly hampered competition in the market for players and served greatly to reduce the size of player salaries. While that outcome probably pleased team owners, the arrangements involved could hardly be called no more restrictive than necessary.

Today, the situation has been ameliorated. Free agent rules permit players to move among teams after a certain amount of time has lapsed and under certain conditions. But restrictions on player mobility remain necessary to permit the production of high-quality product by leagues.

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18. Although, of course, the appearance of particular great stars, such as Michael Jordan, can itself stimulate interest in the game.

Accordingly, certain arrangements have been worked out to accomplish this while permitting the players to share more equitably in the league-generated rents than was formerly the case. In the National Basketball Association, for example, there is both a salary cap and a salary minimum. By placing an upper bound on the total amount that a team can spend on players, the salary cap attempts to deal with the externality that would otherwise be created when rich teams bid for players without taking into account league-wide interests.<sup>19</sup> By placing a floor on what teams must spend, the league prevents teams from selling off their players and taking the cash.<sup>20</sup> Naturally, the salary minimum is also useful in persuading the players to agree to the salary cap and to other restrictions on movements; it guarantees them a certain share of revenues.

#### V. DEALING WITH EXTERNALITIES: TELEVISION AND SUPERSTATIONS

Competition for players is not the only area in which the necessary form of league organization leads to externalities. The area that was at issue in the Bulls case was that of television rights. At the time that the Bulls filed suit, most NBA basketball games were telecast on television either over the air or on cable (this continues to be the case). Some games were telecast locally; some were shown nationally, either on NBC or TNT. The league permits each team control over arrangements for local telecasts in its home city, and the revenues from such telecasts stay mainly with the local teams. The league itself deals with national television exposure, however, and the revenues therefrom are shared among all the teams (not just those playing in the games that are shown).

One can see why this makes sense. Local teams have the best information about local opportunities. They can make local television arrangements so as to promote their own interests. More important, in such local arrangements, those interests coincide with those of the league as a whole. No externality is involved. Hence, in keeping with the principle of organizing the league to give as much independence as possible to local teams, each team is allowed to make the decisions that only, or at least primarily, affect it.

The case is different as regards national telecasts. Here the league has several interests that are not those of any one team. First, the league needs to protect the television audience of its members. Were each team

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19. As with all restrictions that affect individual profitability, those restricted have found ways around the salary cap.

20. As did the Florida Marlins in baseball after winning the 1997 World Series.

able to arrange for its own national television exposure, there could be occasions in which national telecasts arranged by one team coincided with games or telecasts of others, splitting audiences in ways that the individual team arranging for national exposure would not take into account. Exclusive television licenses have been broadly recognized as pro-competitive by, among others, the Federal Communications Commission, the Department of Commerce, and certain federal courts, as such exclusivity encourages the efficient production and development of television programming.<sup>21</sup>

Second, were each team able to arrange national television coverage, the teams that were temporarily strong would draw fan support, television audience, and sponsorship money away from the weaker teams. That effect on weaker teams would not be considered by the stronger teams when they arranged television contracts.

Third, by sharing national television revenues among the teams, the league helps to ensure that teams that are temporarily strong — in part, perhaps because of the acquisition of players through the league's draft system — do not cut off revenues from weaker teams, revenues that may assist those teams in competing in the market for players to the extent that relative wealth is still reflected in that competition.

Finally, the league regards national television as an important way in which support for and interest in the league's product — NBA basketball as a season contest — is maintained. The way in which such telecasts

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21. See, e.g., *The Federal Communications Syndicated Exclusivity Rules, Hearings before the Fed. Communications Comm'n, Subcomm. on Communications of the Comm. on Commerce, Science and Transp.*, 101 Cong. 9-11 (1990) (statement of Roy J. Stewart, Chief, Mass Media Bureau Federal Communication); *Video Program Distribution and Cable Television: Current Policy Issues and Recommendations*, DEP'T OF COMMERCE NTIA REP. 88-233, at 104-07 (June 1988); and *Ralph C. Wilson Indus. v. American Broad. Co.*, 598 F. Supp. 694 (N.D. Cal. 1984), *aff'd sub nom. Ralph C. Wilson Indus. v. Chronicle Broad. Co.*, 794 F.2d 1359 (9th Cir. 1986).

To see why exclusivity can be pro-competitive, consider an example drawn from the publishing industry. Publishing new novels is a risky business. While some novels do well, many fail. It is almost impossible at the outset to predict which novels will be successful. It is costly to promote and produce new novels; many of these costs are borne in vain. The few successes compensate publishers for the many failures. In a world without copyright protection, publishers would have little incentive to finance the acquisition, production, and promotion of new novels, knowing that successful novels would be quickly (and cheaply) reproduced by numerous competitors. For instance, suppose that whenever Simon & Schuster developed a best-selling novel, Random House responded quickly with hardback and paperback copies of that novel. Simon & Schuster's profits would be greatly diminished and, facing losses or below-competitive returns, Simon & Schuster would have no incentive to assume the risks and large costs of developing new novels. Ultimately, consumers would be harmed by a reduction in output of new novels.

are handled is an important part of the promotion and sale of that product. (It is not without interest here that the NBA has very detailed rules on how telecasts of league games are to be conducted.)<sup>22</sup>

This system worked quite well for some time. In particular, local team arrangements for local telecasts did not impinge on the league's ability to arrange its national telecasts optimally. Local teams followed local incentives and their profit and loss calculus led them to make decisions that were in the interests of the league as a whole as well as their own.

This changed because of superstations. Superstations are local television stations that are carried on a large number of cable systems outside their local area. These include WTBS in Atlanta, WOR and WPIX in New York, and WGN in Chicago. In particular, WGN, the strongest independent station in Chicago, is carried on a large number of cable systems around the country. Indeed, in 1993, when the NBA passed its four resolutions regarding its television policies, WGN's signal reached a majority of cable television households nationwide.<sup>23</sup>

The Chicago Bulls, like all the other NBA teams, had for many years made their own arrangements for television telecast of their games in their home area. Some of those telecasts were on cable and some were over the air. In 1989, however, the Bulls switched their over-the-air telecasts to WGN, a move that they found locally advantageous.<sup>24</sup>

That move involved a negative externality. Because WGN is a superstation, Bulls telecasts on WGN were carried in many cities around the country. This impinged on the NBA's ability to make its own arrangements for national telecasts and also may have affected the audience for home-area telecasts of other teams. Such effects did not form part of the profit-and-loss calculus of the Bulls.

The NBA (which had reached an agreement with WTBS, the Atlanta superstation) moved to restrict the number of superstation telecasts, and, as noted above, the Bulls and WGN brought suit under the Sherman Act.

Several remarks are worth making at this point. First, the problem actually involved a second externality of sorts. The effect of the Bulls'

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22. According to Dick Ebersol, Chairman of NBC Sports, he and NBA Commissioner David Stern speak approximately 300 days per year. See Bruce Schoenfeld, *David Stern's Full-Court Press*, N.Y. TIMES, Oct. 18, 1998, at 97.

23. In 1992, WGN was available in approximately 28 million cable households outside of the Chicago market. See *Chicago Prof'l Sports Ltd. Partnership v. National Basketball Ass'n*, 754 F. Supp. 1336, 1348 (N.D. Ill. 1991).

24. See *id.* at 1347.

telecasts outside Chicago could be expected to be material for exactly the same reason that made the Bulls very attractive to WGN, namely, the fact that the Bulls were the hottest team in the NBA. That is an externality because the attractiveness of the Bulls is not merely a consequence of the Bulls' own efforts. It also stems from the NBA's player arrangements, such as the draft, and from the efforts of the league as a whole in promoting NBA basketball. To permit the Bulls to reap the entire reward for such efforts would be to give them a free ride. Free riding is a type of externality in which the selfish benefits gained by the free rider are not part of the profit-and-loss calculus of the entity on whose efforts the free ride is taken. (This is in addition to the fact that the costs imposed by the free rider on that entity are not taken into account by the free rider.) As a result, permitting free riding discourages efforts that would otherwise be productive.

Second, it does not matter for analytical purposes whether the negative effects of the WGN telecasts were large or small. The position taken by the Plaintiffs was that the NBA could not legally restrict the Bulls from making their own television arrangements and that the attempt to do so was an attempt to restrict output, which they measured roughly as the number of basketball games on television. But there is no principled way in which that claim can be distinguished from the claim that the NBA cannot legally restrict its teams from making their own television arrangements in any way that the teams choose. This would mean, for example, that teams would be free to negotiate with television networks, and that the NBA could not offer its chosen carriers a guarantee of exclusivity in national telecasts. The late Judge Will, who presided over the trial, refused to listen to such arguments saying that such matters were not before him, but that does not make them go away.

Finally, suppose it to have been true that the Bulls telecasts had no effect on television audiences outside Chicago for other NBA games. What anti-competitive motive could the NBA have had for restricting them? We shall later discuss the question of the market in which such telecasts and all sports leagues compete, but if WGN and other national NBA telecasts do not compete, there could not be any national anti-competitive effect stemming from the restriction of WGN telecasts. If the NBA's restrictions did not limit output, such restrictions could not be illegal under the Sherman Act.

One might still argue (as did the Plaintiffs) that there could still be a restriction of output inside Chicago stemming from a misapprehension on the part of the NBA as to the national effect of WGN telecasts, but this is unconvincing. The NBA could have no anti-competitive motive to

restrict the output of local Chicago telecasts. Even though having to change their arrangements within Chicago might have hampered the Bulls, any such problem ought to be secondary to a larger principle. It is not the business of the antitrust laws to tell an entity — in this case the NBA — how it should manage its business so as to compete effectively.

## VI. DO SPORTS LEAGUES HAVE MONOPOLY POWER?

Like a good deal of the above analysis, that last statement appears to suppose that sports leagues, the NBA among them, do in fact compete with somebody. Do they, and, if so, with whom? Put differently, do sports leagues have monopoly power?

There are three commonly made mistakes about the economics of sports leagues. The first is to suppose that they can be analyzed as a collection of teams that compete with each other in economic terms as they do on the playing field. That topic was discussed above. The second mistake is to suppose that the fact that sports leagues are paid high prices either by fans or by television carriers implies that they have monopoly power. This is associated with the third mistake, which is also to infer monopoly power from the existence of fans who really like to watch a particular sport in preference to other forms of entertainment. We discuss these two fallacies together.

It is important to understand that high prices do not themselves signal monopoly power at least until one has understood the nature of the product involved. Lexus automobiles sell for higher prices than does the Honda Civic, but that, by itself, tells one nothing about monopoly power for Lexus. The ability to charge a high price can be the reward for producing a high-quality product that is attractive to consumers. Indeed, once we leave the textbook world of homogeneous products, it can very well be that an apparently high-priced product is, in quality-corrected terms, no more expensive than a competing, apparently low-priced one. The ability to charge high prices by offering superior products is not monopoly power. Monopoly power involves the ability to charge high prices without offering superior products. Monopoly power involves the power to charge high prices by restricting output, not by offering what, in quality-corrected terms, is an expanded output.

To put the matter slightly differently: the offering of an attractive product, even the offering of what may be in some respects a uniquely

attractive product is not monopoly power. Rather, it is the kind of result that competition is supposed to bring about.<sup>25</sup>

With whom, then, do sports leagues compete? In terms that might be considered dangerously imprecise but are familiar in antitrust cases, in what market do they operate? We have already indicated that the answer is that sports leagues compete with other entertainment products. We now address this more thoroughly.

A sports league sells its principal product in two major ways: It sells to fans who attend the contests and purchase tickets, and it sells to television (and radio) carriers who in turn resell to advertisers. In both cases, the attractiveness of the league's product to fans is what makes it sell, but the two cases involve different phenomena in analyzing the question of competition.

In the case of fan attendance at games, the league competes with other leisure-time activities. We need not concern ourselves with the question of how close that competition is, however, for it seems clear that leagues do not exercise monopoly power in this area. Leagues schedule games quite frequently, so that there is no direct evidence of output restriction. Games of good teams often sell out, suggesting that the only limitation is one of stadium or arena size. Where games do not sell out, the obvious explanation is team quality rather than an attempt to earn supranormal profits through high ticket prices.

The situation as regards television revenues is more complicated (and this, of course, was the area in which the plaintiffs in the Bulls case alleged that competition was being restrained). Leagues license television rights to networks and other carriers, which in turn sell advertising time to sponsors. One can say that the telecasts of league games compete for viewer attention with other entertainment programs. That is certainly true, but it is not dispositive.

The plaintiffs in the Bulls case claimed that NBA telecasts attracted a group of viewers (young males) who watched basketball disproportionately. That is, the viewers of basketball were unlikely to watch other programs nearly as much. Putting aside the question of whether this is factually correct (which seems very doubtful), let us move to the extreme and suppose that it is true that there is a group of viewers who watch

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25. Part of what is involved here can be seen by considering a question that arose in the deposition of Jerry Hausman, who was the economic expert for the plaintiffs in the Bulls case. When Michael Jordan left professional basketball did the supposed monopoly power of the NBA — or, for that matter, of the Chicago Bulls — decrease? Obviously, it did not. Rather, the quality of the product went down.

basketball and nothing else. Would not that mean that the NBA has monopoly power over that group? Would not that mean that sponsors wishing to reach that group would have no choice and that this would give television carriers of NBA games and, in turn, the NBA monopoly power?

To see that the answers to these questions are in the negative requires thinking about the way in which television is financed and the question of who, in fact, are the ultimate buyers of league telecasts. Commercial television in the United States is not financed by viewers but by business sponsors. Treating the television carriers simply as intermediaries, the NBA and other program producers sell not to viewers but to sponsors. Viewers are important, but that is only because program producers sell viewer attention, as it were.

In this situation, the only competition that can possibly come within the purview of the antitrust laws is competition for sales to sponsors. If that competition is strong, then, so far as competition policy is concerned, there is an end to the matter. It may very well be that sponsors do not adequately reflect the interests of viewers and that, were viewers to pay directly for the programs they choose, a different set of programs would be telecast. But that phenomenon, if it exists, is a consequence of the way we have chosen to organize television; it is not a consequence of a lack of competition among program producers.

To put this another way, it is a mistake (sometimes made by courts) to suppose that television viewers are the customers for television programs. The customers are the sponsors and it is sponsor welfare that is served by competition in television programming. This may or may not be a desirable state of affairs, but it is not to be cured by antitrust policy.

Thus, consider the example of basketball fans. Assume, for the moment, that the market for sales of television programs to advertisers is competitive. Suppose that it is the case that, from the point of view of die-hard basketball fans, there are an insufficient number of NBA games on television. Then it must be the case that sponsors regard the group of die-hard basketball fans either as insufficiently numerous or insufficiently responsive to ads compared to other groups to make it profitable to put on more basketball games and fewer other programs — programs that other viewers wish to watch in preference to basketball. If one believes that sponsors are wrong about this, or that the interests of the die-hard basketball fans should nevertheless be served in preference to the interests of other viewers, the remedy, if any, surely lies with the Federal Communications Commission and not in an antitrust case against the NBA. Markets are driven by money, and if the NBA and other program

producers respond competitively to the signals given by buyers, then they are doing all that competition policy can expect of them.

The only issue that remains, therefore, is whether the NBA (or any other sports league) has monopoly power over sponsors. Is it not the case that sponsors who wish to reach die-hard basketball fans have no choice but to buy spots on NBA programs? By restricting the number of such programs cannot the NBA earn monopoly profits?

The problem here is that these questions are loaded, and loaded incorrectly. Sponsors have no direct interest in reaching a particular group of consumers; they are interested in selling their products. In pursuing that interest, they will arrange advertising campaigns in the way that seems to them to be most profitable.

Consider McDonald's, for example.<sup>26</sup> McDonald's advertises on NBA telecasts not to reach die-hard NBA fans, but to sell hamburgers (and associated products). McDonald's also advertises on many other telecasts that reach other classes of viewers (as well as advertising in other media). Obviously, McDonald's does not care how many hamburgers it sells to die-hard basketball fans; it cares about the total number of hamburgers that it sells and the profits that it will obtain in selling them. In arranging its advertising campaign, McDonald's must compare the cost and effectiveness of an advertising spot in an NBA telecast with the cost and effectiveness of a spot elsewhere. If McDonald's (or its agent) acts efficiently, then the marginal profit to be made from an additional spot directed at any group of viewers will be the same for all such groups. In this circumstance, an attempt by the NBA (or its television carriers) to raise the price of a spot will result in McDonald's shifting its advertising away from basketball fans and toward other groups.

It is interesting to note in this regard, that a study done for the Bulls case shows that advertisers on NBA telecasts, including the heaviest advertisers, also advertise elsewhere on television.<sup>27</sup> The McDonald's example is not special. For example, as Figure 1 indicates, between January and April of 1993, among the ten advertisers spending the most on over-the-air regular season NBA spots, none allotted more than a small percentage of their over-the-air advertising expenditures to over-the-air reg-

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26. From January through April of 1993, McDonalds spent more on over-the-air regular season NBA advertising than any other regular season NBA advertiser.

27. The study was based on Arbitron data. The Arbitron Company may be contacted at 142 West 57th Street, New York, NY, 10019.

ular season NBA.<sup>28</sup> Collectively, between January and April of 1993, over-the-air regular season NBA advertisers allotted only 6.6% of their over-the-air national network television advertising to NBA telecasts while NBA/TNT regular season NBA advertisers allotted only 7.5% of their cable national network advertising to NBA/TNT between November 1992 and March 1993.

Moreover, the NBA represented only a small fraction of the advertising inventory available. In 1992 (1991), the amount spent on over-the-air regular season NBA advertisements accounted for only 2.5% (3.2%) of annual sports over-the-air advertising expenditures and a mere 0.7% (0.6%) of annual total over-the-air advertising expenditures.<sup>29</sup>

Despite the statistics cited above, suppose there are a few advertisers that do not have a large range of customers and that need to reach viewers with the demographic characteristics of NBA fans. NBA viewers tend to include a larger fraction of young males than do many other television programs. What about advertisers selling products oriented to young males?

There are several things to be said here. First, the products advertised on NBA telecasts that appear to be so oriented are principally beer and shaving products. Both of these, especially beer, are widely advertised elsewhere. From Figures 3 and 4, we see that regular season NBA advertising accounts for a very small fraction of both over-the-air and cable national network television advertising.<sup>30</sup> It is also evident from Figures 3 and 4 that a successful advertising strategy does not require that a beer producer spend either a large sum of money or a large share of its advertising budget on the NBA. Between 1991 and 1993, only four of fifteen beer producers that advertised on over-the-air national network television purchased spots on the NBA telecasts. Among those that did not advertise was Budweiser, the beer producer with the largest over-the-air national network television advertising budget.<sup>31</sup>

Second, a further study shows that the cost per thousand of reaching young males (that is, the cost per thousand young males, not the cost per

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28. It is also the case that among the ten advertisers spending the most on regular season NBA/TNT spots, between November 1, 1992 and March 1993, none allotted more than a small percentage of their cable national network television advertising expenditures to regular season NBA/TNT (see Figure 2).

29. Shares are based on data from Arbitron and Paul Kagan Associates. At the time of the study, 1993 data were not available.

30. Figure 3 relies on data from 1991 through 1993. Figure 4 includes data from November 1992 through March 1993. We were unable to obtain similar information for earlier years.

31. Although Budweiser did advertise on regular season NBA/TNT, its expenditures were relatively small.

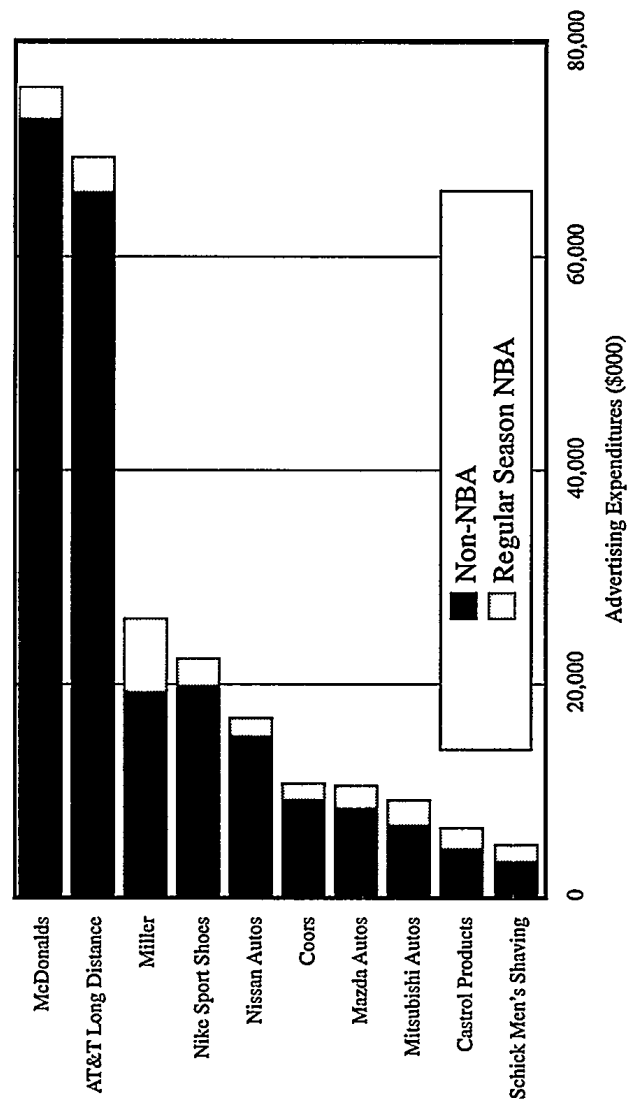
thousand viewers) through NBA telecasts lies within the general range of the cost of doing so through other outlets (see Figure 5).

Finally, it might still be the case that there are die-hard basketball fans, different from other young males, who simply do not watch non-basketball programs. There is no evidence for this whatsoever, but suppose that it is true. Advertisers that (for some mysterious reason) can only sell to such a group must compete with advertisers in general for the right to show commercials on NBA programs. If the price to advertisers in general is competitive, there can be no antitrust injury to any highly specialized advertiser just because it must pay the same price. In short, the NBA, like other sports leagues, competes for the advertiser dollar. It is a mistake to look at matters from the point of view of a particular group of fans or a particular group of advertisers wishing to reach those fans.

## VII. CONCLUSION

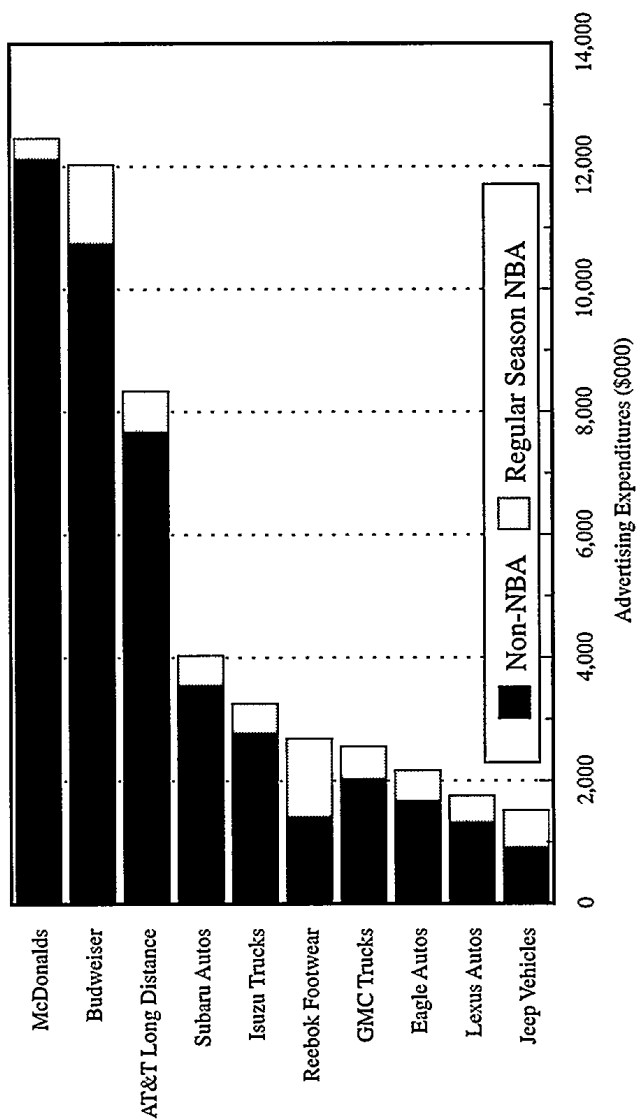
To briefly summarize: sports leagues are not composed of economic competitors. They are effectively single entities, or at a minimum, joint ventures, engaged in the production of a product that competes with other entertainment products. They are not formally organized as single entities because to be so would mean producing an inferior product. Because leagues are necessarily organized as a collection of formally independent teams means, however, that they must (and do) adopt rules in order to deal with externalities that would otherwise be created by the necessary form of organization. As in the Bulls case, those rules are typically pro-competitive restraints that lead to a superior product and aid leagues in their competition with other sources of entertainment products. The ability to charge apparently high prices for a superior product is not an indication of monopoly power.

FIGURE 1. THE 10 ADVERTISERS SPENDING THE MOST ON REGULAR SEASON NBA ALLOT A SMALL PERCENTAGE OF THEIR ADVERTISING EXPENDITURES TO REGULAR SEASON NBA OVER-THE-AIR NATIONAL NETWORK TELEVISION  
JANUARY-APRIL 1993



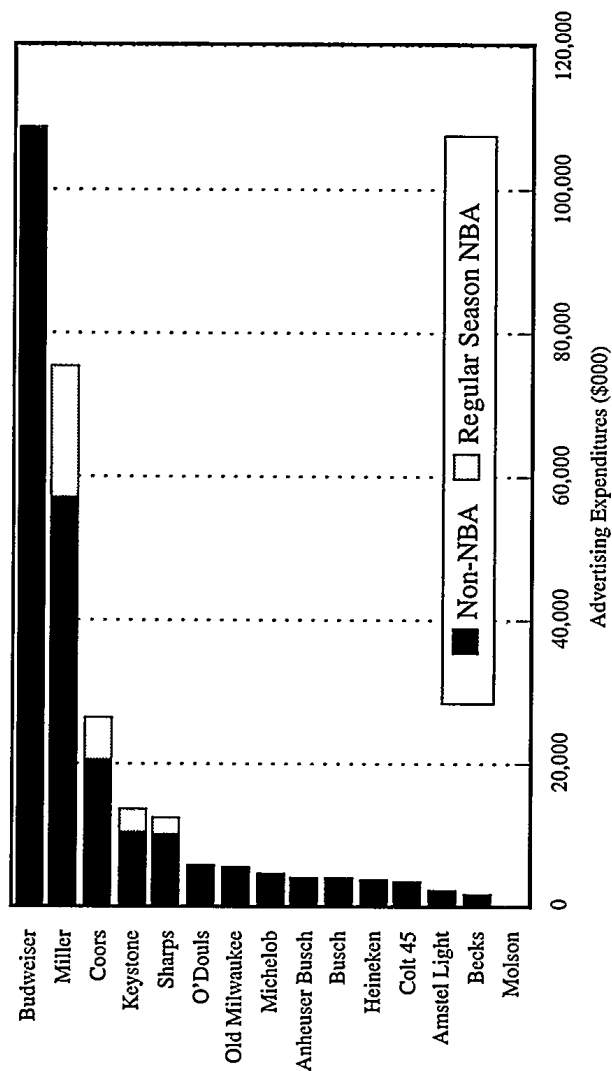
Expenditures exclude spending on NBA All-Star and NBA Post-Season games.  
Expenditures include spending on ABC, CBS, NBC and, in 1993, Fox.  
SOURCE: Arbitron.

FIGURE 2. THE 10 ADVERTISERS SPENDING THE MOST ON REGULAR SEASON NBA/TNT ALLOT A SMALL PERCENTAGE OF THEIR ADVERTISING EXPENDITURES TO REGULAR SEASON NBA/TNT CABLE NATIONAL NETWORK TELEVISION  
NOVEMBER 1991–MARCH 1993



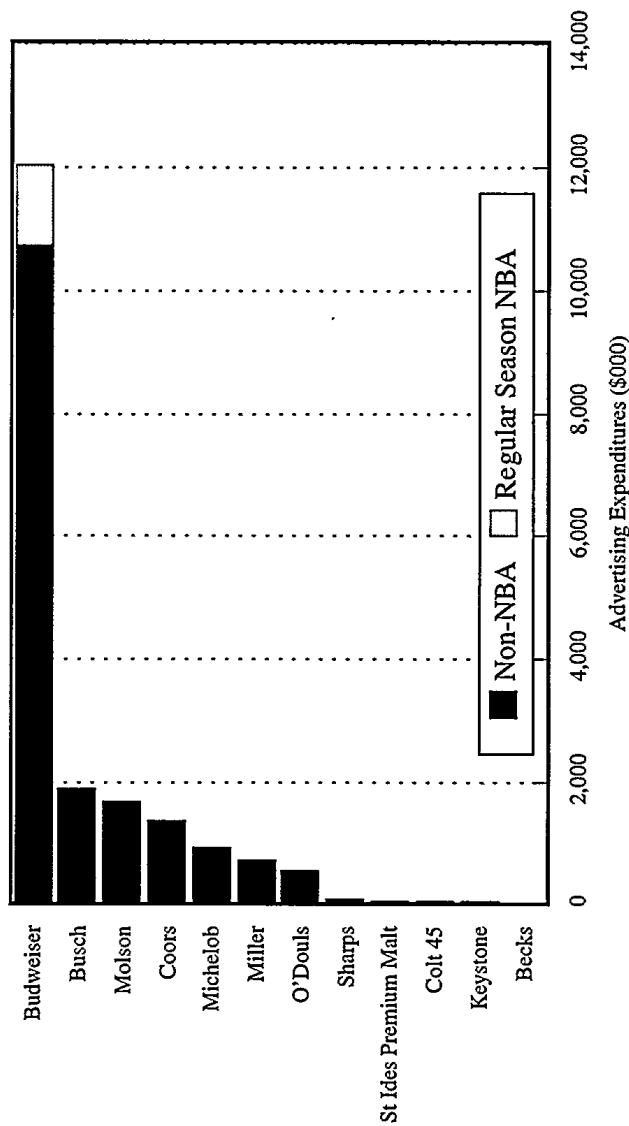
Expenditures exclude spending on NBA All-Star and NBA Post-Season games.  
Expenditures include spending on ABC, CBS, NBC and, in 1993, Fox.  
SOURCE: Arbitron.

FIGURE 3. BEER AND ALE ADVERTISERS ALLOT A SMALL PERCENTAGE OF THEIR ADVERTISING EXPENDITURES TO REGULAR SEASON NBA OVER-THE-AIR NATIONAL NETWORK TELEVISION JANUARY 1991-APRIL 1993



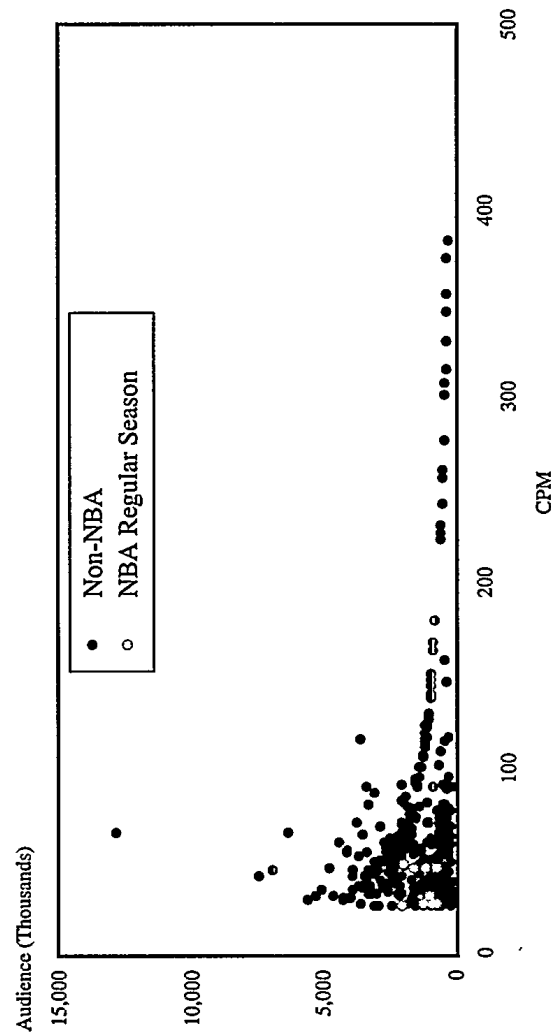
Expenditures exclude spending on NBA All-Star and NBA Post-Season games.  
Expenditures include spending on ABC, CBS, NBC and, in 1993, Fox.  
SOURCE: Arbitron.

FIGURE 4. BEER AND ALE ADVERTISERS ALLOT A SMALL PERCENTAGE OF THEIR ADVERTISING EXPENDITURES TO REGULAR SEASON NBA/TNT CABLE NATIONAL NETWORK TELEVISION NOVEMBER 1992-MARCH 1993



Expenditures exclude spending on NBA/TNT Post-Season and NBA/TBS games.  
Expenditures include spending on the cable networks followed by BAR, which increased from 9 in November 1992 to 12 in March 1993.  
SOURCE: Arbitron.

FIGURE 5. MANY TELECASTS THAT DELIVER AT LEAST AS LARGE AN AUDIENCE SIZE AS REGULAR SEASON NBA TELECASTS HAVE CPMs COMPARABLE TO OR GREATER THAN THOSE FOR REGULAR SEASON NBA TELECASTS  
 MALES 18-34  
 OVER-THE-AIR NATIONAL NETWORK TELEVISION  
 JANUARY-APRIL 1992



Selected telecasts include sports telecasts, as well as non-sports telecasts that pro basketball viewers or males aged 18 to 49 were at least as likely to watch as viewers in general.  
 Includes telecasts on ABC, CBS, NBC, and, in 1992, Fox.  
 Excludes NBA All-Star and NBA Post-Season games.  
 SOURCE: Nielsen Television Index, Household and Person Cost per Thousand [CPM], Simmons Media and Markets Report, Fall Television Survey.