Contrasting the Industry Structure of Professional Sports Franchises and Large Technology Firms: The Role of Monopolies and Other Non-Competitive Models

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The article examines the monopolistic structure and other advantages that the four major professional sports leagues in the United States have enjoyed for decades as compared to similar circumstances surrounding the success of Microsoft Corporation. The authors examine the tightly related financial nexus of industry and government using the business models of professional sport franchises and the Microsoft Corporation. Antitrust legislation, collusive arrangements, and franchises are researched as they related to professional sports and public financing. The theoretical construct will become the foundation of future empirical studies concerning monopolistic industry practices.

INTRODUCTION

In a perfect world for business, government would advance a large portion of developmental costs, there would be collusion among allied organizations and industries, a massive cash reserve or a large guaranteed cash flow would exist, and any attempt at meaningful competition would be thwarted. The scenario described is not a myth but a reality, as it exists in the context of major professional sports and certain industries like computer software. In business enterprises that are seemingly very different the above points of similarity are evident. Interestingly, these elements exist in such varied endeavors as a software company and professional sport leagues. This seems to be especially true for large organizations like sport franchises and Microsoft Corporation. The paper examines the similarities of the remarkable success of these two business concerns as they work cooperatively with government and others to ensure their financial success.

The paper will explore the nature and impact of subsidies, monopolies, and collusion. It describes how professional sports teams have obtained and maintained their monopolistic practices and government subsidies, and the extent to which Microsoft emulates the monopolistic and government subvention arrangement of professional sports.

GOVERNMENT SUBSIDY FOR PRIVATE ENTITIES

The exclusive right of member franchises in Major League Baseball (MLB), the National Football League (NFL), the National Basketball Association (NBA), and the National Hockey League (NHL) to their home territory and government subsidies for the construction of facilities has fostered great economic benefit for team owners (Leeds & von Allmen, 2002). The building of facilities for professional sport teams has been a cornerstone of redevelopment programs for many central cities and many larger suburban and edge communities (Austrain & Rosentraub, 2002). For more than 15 years, governments have invested more than $10 billion in the playing facilities used by professional sports teams (Kennedy & Rosentraub, 2000). They often justify subsidies by claiming the projects create valuable public goods and positive externalities, though such benefits are difficult to measure (Johnson & Whitehead, 2000). Indeed, many argue that the public suffers with such projects. By way of example, Lambert (2004, p. 16) identifies the actions of George W. Bush and his fellow investors as the “classic taxpayer shakedown.” The group bought the Texas Rangers baseball franchises in 1989 for $86 million. In less than one year, the new ownership threatened to move the team away from Arlington unless they were given a new ballpark. Bush vigorously campaigned the city of Arlington to put up $135 million by arguing that the stadium would bolster the local economy (Tesone, Platt, & Alexakis, 2005). As managing partner of the ownership group, he and his immense political influence succeeded in convincing the city to use the power of eminent domain to seize extensive acreage around the ballpark and transfer ownership of that land to the Rangers (Lambert, 2004). The government also put up 85 to 90% percent of the funds to build the ballpark through bonds paid off mostly through an increased sales tax. When the team was sold four years after the facility was completed, Bush made millions while the taxpayers, who invested $135 million in the stadium alone, received no proceeds from the sale (Lambert).

At least one scholar suggests that, while eliminating competition may be good for the franchises, it imposes a cost on society and the public may not like the resulting distribution of resources (Leeds & von Allmen, 2002). Kennedy and Rosentraub (2000) document that after making substantial commitments, communities are given new demands for increased subsidies. If these mounting demands are not satisfied, teams frequently move to other municipalities. Taxpayers and sports fans are then left with unused facilities, debt obligations, and a reduced quality of life. The authors assert that if the public sector devotes tax revenues to generate intangible benefits and increased business activity in certain locations, communities are entitled to adequate safeguards to protect their investments. Various economic impact studies examining the merits of subsidizing professional sports teams have arrived at remarkably different conclusions about the size of a sports team’s economic impact on the region in which they are located (Hudson, 2001). Cities still continue to rely on sports facilities for redevelopment strategies even though numerous independent analyses indicate that these structures and teams are not correlated with productive regional economic development (Austrain & Rosentraub, 2002).

Just as professional sport leagues have been the recipients of government largesse, companies such as Microsoft Corporation have also received great benefits. The federal government has made significant contributions to the research base for computing technology. It has accounted for a large portion of the total financial commitment for computing technology research in the United States and a vast majority of all university research funds in the field (National Research Council, 1999). Critics of Microsoft say that Bill Gates is pretty frank about how they have used these advantages to their benefit. He admits to being in the business of ‘embracing and extending’ the ideas of others. Apparently, the government for a number of decades has subsidized computing technologies. In fact, computers were created at public expense as a public investment initiative. In the origination years of the 1950s computing technology initiatives were publicly funded at a level of almost 100%. The same is true of the Internet at its outset. The ideas, the initiatives, the software, the hardware were created by tax dollars, "…and it's being handed over to guys like Bill Gates" (Couey & Karliner, 1998, p. 2). Since 1945 large corporations from various industry sectors have collaborated with the government and relied on public subsidies often through the pentagon. Publicly subsidized systems have included many corporations from the energy sector to the pharmaceutical industry. Microsoft has been no exception, as the reality is that computers and the Internet were created and funded by almost entirely by public programs.

Since the end of World War II, the federal government has been an extremely strong supporter of computing research. The Advanced Research Projects Agency (ARPA) is one government entity that has historically been the main supporter and the single most important force behind technology research and development (Bush, 1954). Between 1962 and 1986, ARPA became part of the Department of Defense (DOD) and provided leadership to the Information Processing Techniques Office (IPTO) for the creation of a new field of computer science that generated breakthroughs in the areas of interactive computing, packet switching network transmissions and the Internet (Hauben & Hauben, 1997). Between 1976 and 1995, federal funding for computer science increased by a factor of five, from 180 million dollars to 960 million dollars (calculated by constant 1995 dollar values). Federal funding for computer science provided nearly all the financial support for research and development (R&D) in 1950. In 1963, the federal government still funded 35% of IBM’s R&D budget, as well as 50% for Burroughs and 40% at Control Data. Federal funding represented approximately one-third of total computer-related research during the late 1970’s (National Research Council, 1999).

The Microsoft Corporation is an obvious beneficiary of years of governmental funding toward the massive costs associated with technology research and development initiatives. It is widely publicized that sport leagues benefit from direct tax dollars and government subsidies. Given the information presented above, it would seem that the same is true for technology firms similar to Microsoft, IBM and others.

THE SYMBIOTIC RELATIONSHIPS AMONG CORPORATE ENTITIES

The broadcast media has a dependence on programming provided by the four major professional sports leagues. In fact, certain networks (i.e.: ESPN, Fox Sports, etcetera) are almost entirely dependent on sports programming. ESPN is more profitable than ABC, NBC, and CBS combined (Spitzer, 2002). In 2003, ESPN provided sports coverage to more than 150 countries in more than a dozen languages. Sports programming is available 24 hours a day (Coakley, 2004).

The professional sports leagues command such high premiums for the right to broadcast their respective products that they effectively eliminate any opportunity for competing interests. Media companies extensively use sporting events to attract revenue that comes in the form of commercial sponsorship. The sport product is ideal for commercial entities desirous in attracting difficult-to-reach audiences that will potentially consume a wide variety of products. Evidence of this is the long-term broadcast/rights package between the NFL and the major broadcast networks (Tesone, Platt, & Alexakis 2005).

Professional sports organizations operating as businesses are equally reliant on the success of media organizations. They are dependent on the media to provide a combination of game coverage and news reporting. As far as the authors can determine, no other individual enterprise has its own section of the newspaper. The broadcast media provides these organizations with extensive publicity, advertising, and information dissemination at relatively no cost. The success of the local team is directly correlated to the financial success of the local media. A successful team equates to increased revenue for the broadcast organization. A professional sport league could not exist in its present form without the media.

Just as the media and professional sports are dependent on one another, Microsoft has a similar symbiotic relationship with the computer hardware manufacturers. Microsoft recognized the importance of a close association from its beginning. Just as the league offices of the four major professional sports leagues grant cities a franchise to operate within their league structure, Microsoft Corporation licensed MS DOS in 1982 to hardware companies. Within 16 weeks, Microsoft sold software licenses for the operating system to 50 microcomputer manufacturers. In effect, Microsoft set up its own franchise system.

In 1983, the total number of personal computers used in the United States exceeded 10 million. In three years this number tripled to 20 million (National Research Council, 1999). By 1989, the number of computers in the U.S. exponentially grew to 50 million. Related to this growth in hardware, Microsoft Corporation’s 1990 fiscal year revenues hit a record high of $1 Billion. By 1992, Microsoft shipped 10 million units of Windows 3.1; several generations of development beyond MS DOS within a mere 10 years (National Research Council). The relationship between the hardware makers and Microsoft was undoubtedly lucrative.

MONOPOLISTIC LEANINGS, FAVORABLE LEGISLATION, AND LEGAL SYSTEMS

There is no stronger monopoly in North American commerce than that of the four major professional sports leagues. While each franchise within these leagues is a separate business, owners have strongly unified to form cartels that protect their collective interests. Each franchise holds a territorial monopoly while each league holds a monopoly on the professional sport (Remelius, 2001).

Successful professional sports leagues have used the principle of monopoly power through antitrust legislation exemptions, which precluded the entry of competing teams in their host cities. It is the broadcast arrangements and the formation of new leagues that comprise the most important antitrust issue in sports today (Scully, 1995). Professional sports leagues have not had to fully comply with the Sherman Antitrust Act of 1890, Clayton Act of 1914, and the Federal Trade Commission Act of 1914. The acts were passed to define how commercial enterprises would compete with each other. The notion of free trade and open competition was clearly the underlying principle. The acts hold that any restraint of trade or commerce is illegal and that anyone attempting to monopolize, either individually or in combination with others, is guilty of a felonious crime (Remelius, 2001). However, professional team sports have not had to comply with these regulations. This monopolistic business model was first challenged in 1922 when the Federal Baseball Club of Baltimore, Inc. sued the National League of Baseball Clubs. The argument was that the industry was being monopolized by the existing professional baseball structure. The United States Supreme Court declared that ‘the baseball game’ was an exhibition, not a good or a product. Baseball then became exempt from antitrust laws as a result of the precedent that was set. No Supreme Court case has ever overturned the ruling nor has Congress ever changed this status. Today, all of the four major professional sports leagues maintain a monopoly over each sport (Remelius, 2001).

Because of the antitrust exemption, there are fewer franchises than cities that desire them. The league’s monopoly power leads it to provide fewer teams in fewer cities than would exist in a truly competitive environment. Existing teams enjoy tremendous leverage as a result of this situation. The threat of moving has continually netted the owners considerable facility improvements, and with those, sharp increases in the value of their equity. For example, the average NFL franchise equity in the middle 1960s was $10 million. In 2003, the average value was $531 million. That represents an average capital gain of $521 million. This makes the average annual return on a $10 million investment $2 million (Coakley, 2004).

The owners collectively act in their own best business interests. Broadcast rights are negotiated and sold as a group, earning revenues that they could not attain by negotiating individually. The number of contests is restricted in some cases, thus creating scarcity and the ability to increase ticket, parking, and concession prices. Most non-economists dislike monopolies because of the high prices they demand. They may hurt the consumers who have to pay them, but they benefit the shareholders, employees, and other stakeholders in the firms that receive them. The higher prices simply take money from one pocket (the consumers) and put it in another (the monopolist’s). Since one cannot say whether the higher prices that monopolies charge help or harm society, economists treat them as a transfer from consumers to producers, which brings no overall change in society’s well-being (Leeds & von Allmen, 2002). The owners in the NFL have even instituted league rules that prohibit television broadcasts of their home games if they have not sold out the stadium 72 hours before game time. The NFL has crafted their monopolistic advantages to the point that they are presently guaranteed revenues approaching $100 million annually while maintaining a league imposed cap on player salaries. The cap stands at 64.75% of revenue (Tesone, Platt, & Alexakis, 2003). Certain large technology firms also enjoy the leverage that comes with limited competition and powerful government alliances.

Microsoft Corporation represents a monopolistic business model that is similar to that of professional sports. Monopoly power is defined by the courts to be the power to control prices or exclude competition. Having a market share above 70% in one particular industry may be seen as monopoly power (Cheeseman, 2005). One might conclude that with a market share of 90%, Microsoft may be considered to be a monopoly (Mott, 2004). In less than 25 years, Microsoft grew from a startup company into the largest software developer in the world. Nearly every individual who uses a personal computer uses Microsoft’s products.

In the mid-1990’s, Microsoft began a campaign to absorb Netscape into its operating system. Netscape was not agreeable to this arrangement and Microsoft launched a campaign to place its own browser, called *Internet Explorer*, onto the desktops of nearly all systems. This was a ‘hardball’ strategy that aimed to squeeze Netscape out of the browser business. After a year and a half of investigation, trials, and settlement negotiations; the U.S. District Court rendered a decision that would prohibit Microsoft from business practices that would inhibit competition. Microsoft appealed the decision and after years of legal wrangling, a federal district court ordered Microsoft to refrain from coercive practices and share certain programming source codes

(Cheeseman, 2005). During the long course of legal action, Microsoft managed to dominate the Internet browser market with its product.

It was made clear during the investigations, trials, settlement negotiations, and court decisions that Microsoft still operates as a virtual monopoly. Akin to the professional sports leagues, Microsoft Corporation is recognized as a monopoly and still operates in practically the same fashion as it has for 25 years. The aforementioned business of major league professional sports has withstood similar challenges. The public is evidently in support of the business model of the professional leagues and Congress has never challenged the anti-trust exemptions that are so favorable to them. Microsoft shares similar support. While 70% of information technology professionals agree with the court that Microsoft has a virtual lock on the personal computer operating systems market, they do not necessarily believe that this is negative (Machlis & Deckmyn, 2000 as cited in InfoWorld 2004). Indeed, 65% of respondents to a Computerworld Magazine survey have stated that Microsoft's practices have had a positive effect. Only 17% of information technology professionals favored breaking the company into separate corporations.

CONCLUSION

This article surveyed the impact of government subsidies, collusive agreements, and permissible monopolistic practices for major professional sport leagues and Microsoft Corporation. The two business structures have obvious similarities. The existing business model has led to great success for these concerns. Future research might further delve into the extent to which this monopolistic business model is utilized and its managerial implications. Common belief is that monopolies are an anathema to the free enterprise system. However, it appears that there are elements of monopolistic practice that both the government and the public have accepted. The disclosure sets the stage for future research that might explore other areas of commerce where society may conceivably perceive benefits from condoning such business practices.

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