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# Slicing the Rent-Seeking Onion: Why Differential Rent-Seeking Explains the Competitive Disadvantage of United States Sports Franchises in Canada

Ethan Glass

## INTRODUCTION

*As a form of entertainment sports have the ability to create memorable events and develop memories that mark that passage of time and bond generations through shared activities. This romantic bond, coupled with opportunities to escape from the worries of the day, is what owners and leagues manipulate to get what they want from governments, fans, and taxpayers, even in an era of repeated calls for smaller governments and lower taxes.<sup>1</sup>*

Economists find professional sports to be an interesting model upon which to test their economic theories.<sup>2</sup> This is primarily due to three reasons. First, as the popularity and profitability of professional sports<sup>3</sup> grows,<sup>4</sup> its economics become increasingly important.<sup>5</sup> Second, professional sports, more than

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1. MARK S. ROSENTRAUB, MAJOR LEAGUE LOSERS 33 (1997).

2. See SPORTOMETRICS (Brian L. Goff & Robert D. Tollison eds., 1990). See also JESSE W. MARKHAM & PAUL V. TEPLITZ, BASEBALL ECONOMICS AND PUBLIC POLICY (1981) (focusing on the industrial organization, structure, conduct, and performance of professional baseball).

3. For the purposes of this Note the professional sports discussed will be Major League Baseball, the National Basketball Association, and the National Hockey League because of their economic size and international franchises.

4. In 1997, Major League Baseball held 2,268 games, sold 63,100,000 tickets, grossed \$2,000,000,000 in revenue, and netted an estimated \$840,000,000 in revenue. See LEONARD KOPPETT, KOPPETT'S CONCISE HISTORY OF MAJOR LEAGUE BASEBALL 483 (1998). See also ANN E. WEISS, MONEY GAME\$ (1993) (discussing the professionalization of sports and the extent of sports business); DALE HOFMANN & MARTIN J. GREENBERG, SPORT\$BIZ (1989) (discussing sports as a "modern, merchandising monster"); HOUSE RESEARCH POLICY BRIEF, THE ECONOMICS OF SPORTS STADIUMS (Minn. 1997) (discussing the municipal benefits of professional sports teams); KENNETH L. SHROPSHIRE, THE SPORTS FRANCHISE GAME 61-72 (1995) (discussing the true value of sports to municipalities); Melvin L. Burstein & Arthur J. Rolnick, *Congress Should End the Economic War Between the States* (visited Jan. 29, 2000) <<http://minneapolisfed.org/pubs/ar/ar1994.html>>.

5. See BARRIE HOULIHAN, SPORT & INTERNATIONAL POLITICS (1994); DONALD MACINTOSH ET AL., SPORT AND POLITICS IN CANADA (1987); DONALD MACINTOSH & MICHAEL HAWES, SPORT AND CANADIAN DIPLOMACY (1994).

other corporations, have special positions under the law. For example, baseball is exempt from the United States antitrust statutes,<sup>6</sup> which enables economists to focus on rent-seeking and its effect,<sup>7</sup> and not the legality of the corporate and franchise<sup>8</sup> behavior.<sup>9</sup>

Third, and finally, economists study professional sports because professional sports strongly parallel other international businesses in regulated or restricted industries.<sup>10</sup> This similarity allows economists to create theories that encourage progress toward the comparative advantage goals of international trade agreements like the General Agreement on Tariffs and Trade of 1994 (GATT) and the North American Free Trade Agreement (NAFTA).<sup>11</sup>

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6. See *Flood v. Kuhn*, 407 U.S. 258, 283-84 (1972) (“[w]e continue to loathe, 50 years after *Federal Baseball* and almost two decades after *Toolson*, to overturn those cases judicially when Congress, by its positive inaction, has allowed these decisions to stand for so long”), *aff’g* *Toolson v. New York Yankees*, 346 U.S. 356, 356-57 (1953) (“Congress has had [*Federal Baseball*] under consideration, but has not seen fit to bring such business under these laws by legislation”), *aff’g* *Federal Baseball Club of Baltimore, Inc. v. National League of Prof. Baseball Clubs*, 259 U.S. 200, 208-09 (1922) (“[t]he business is giving exhibitions of baseball which are purely state affairs [and] not a subject of commerce”).

7. See *infra* Section I for a definition of rent-seeking.

8. See PAUL C. WEILER & GARY R. ROBERTS, *SPORTS AND THE LAW* 352 (1993) (discussing the corporate structure of sports). See also *North Am. Soccer League v. National Football League*, 670 F.2d 1249, 1252 (2d Cir. 1982) (“NFL teams are separate economic entities engaged in a joint venture”).

9. Baseball (and sports business generally) has a rich legal tradition in the United States courts and universities. See generally ROGER I. ABRAMS, *LEGAL BASES: BASEBALL AND THE LAW* (1998) (detailing the history of baseball in the United States legal system); *BASEBALL AND THE AMERICAN LEGAL MIND* (Spencer Weber Waller et al. eds., 1995) (exploring the “baseball/law nexus”); 2 ROBERT C. BERRY & GLENN M. WONG, *LAW AND THE BUSINESS OF THE SPORTS INDUSTRIES* (1993) (explaining the development of sports business and associated legal problems); 1 ROBERT C. BERRY & GLENN M. WONG, *LAW AND THE BUSINESS OF THE SPORTS INDUSTRIES* (1986) (explaining the development of sports business and associated legal problems); *GOVERNMENT AND THE SPORTS BUSINESS* (Roger G. Noll ed., 1974) (analyzing the operation of professional team sports); GEORGE W. SCHUBERT ET AL., *SPORTS LAW* (1986) (surveying sports law); LIONEL S. SOBEL, *PROFESSIONAL SPORTS & THE LAW* (1977) (detailing legal issues relating to professional sports); *SPORTS LAW AND LEGISLATION* (John Hladczuk et al. eds., 1991) (surveying articles pertaining to sports law).

10. Professional sports are similar to other businesses in this context because they have to obey the legal rules of labor, corporation, agency, contract, and the economic rule of supply and demand.

11. See JOHN H. JACKSON, *INTERNATIONAL ECONOMIC RELATIONS* 7-13, 289-326, 489-500 (3d ed. 1995) (discussing GATT and NAFTA in depth). This Note will not discuss comparative advantage or GATT and NAFTA purposes or provisions.

This Note argues that rent-seeking, a theory developed in economic scholarship,<sup>12</sup> explains why United States sports franchises in Canada do not field competitive teams.<sup>13</sup> Part I of this Note uses historical approaches to defining rent-seeking to create a price-determining equation. Part II examines Major League Baseball's Canadian franchises, their competitive problems, the previous explanations for those problems, and the flaws in those explanations. Finally, Part III concludes that the Canadian sport franchise disadvantage is due to rent-seeking.

## I RENT-SEEKING DEFINED

Rent-seeking is the quotient of the purchaser's alternatives and the purchaser's competition divided by the competition against the seller's product and the seller's alternatives to the purchaser plus an emotional variable, multiplied by a coefficient converting the ratio into dollars. Part I.A assimilates the influ-

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12. Rent-seeking is merely a variation on the theory of supply and demand. Therefore there are numerous related economic theories that could have been used to explain the Canadian franchise competitive disadvantage including:

General law/economic theory. See generally *Union Oil v. Oppen*, 501 F.2d 558, 561-62 (9th Cir. 1974) (using an economic analysis to determine which rule of law to apply); ADAM SMITH AND THE PHILOSOPHY OF LAW AND ECONOMICS (Robin Paul Malloy & Jerry Evensky eds., 1994) (discussing Adam Smith's philosophy of law and economics); PAUL BURROWS & CENTO G. VELJANOVSKI, *THE ECONOMIC APPROACH TO LAW* (1981) (presenting the strengths and weaknesses of the economic approach to the law); *LAW AND ECONOMICS* (Warren J. Samuels & A. Allan Schmid eds., 1981) (discussing the contemporary institutionalist study of the economic role of government); KENNETH G. DAU-SCHMIDT & THOMAS S. ULEN, *LAW AND ECONOMICS ANTHOLOGY* (1998) (summarizing the "classic" law and economics articles); *LAW AND ECONOMICS & THE ECONOMICS OF LEGAL REGULATION* (J.-Matthias Graf von der Schulenburg & Göran Skogh eds., 1986) (selecting papers presented at the conference on "Law and Economics and the Economics of Legal Regulation," 24-26 of June 1984, Berlin); THOMAS F. MICELI, *ECONOMICS OF THE LAW* (1997) (analyzing the economics of tort, contract, property, and litigation); J.M. OLIVER, *LAW AND ECONOMICS* (1979) (examining the affect of law on economic behavior); RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* (5th ed. 1998) (using economic principles normatively to explain legal system); Christine Jolls et al., *A Behavioral Approach To Law And Economics*, 50 *STAN. L. REV.* 1471 (1998) (adding knowledge about human behavior to the law and economics analysis).

Cost-Benefit analysis. See generally *McCarty v. Pheasant Run, Inc.*, 826 F.2d 1554, 1556 (7th Cir. 1987) (using a formulaic cost-benefit analysis for tort); *United States v. Carroll Towing Co., Inc.*, 159 F.2d 169, 173 (2d Cir. 1947) (using a cost-benefit approach to tort liability).

Coasean Economics. See generally *COASEAN ECONOMICS* (Steven G. Medema ed., 1998) (assessing the development of, tensions within, and prospects for Coasean Economics); Ronald Coase, *The Problem of Social Cost*, 3 *J.L. & ECON.* 1 (1960) (asserting that the best cost avoider should bear liability).

13. "Competitive" means both athletically and fiscally competitive.

ential rent-seeking scholarship into a theory of rent-seeking and examines that theory's relationship with price theory. Part I.B converts the rent-seeking theory into an equation, reflecting a purchasing arrangement that determines the product's eventual price. Part I.C uses the price equation to mold the rent-seeking theory into an empirically useful equation.

#### A. DEFINING RENT-SEEKING: FIRST PRINCIPLES

A plane crash has left an engineer, a chemist, and an economist on a deserted island. Their only food is a tin can of beans that washed up on the shore. The plane crash has left the party without anything but the beans and their knowledge, so they discuss how to open the can. The engineer says:

I've calculated that the terminal velocity of a one-pound object—the weight of the can—thrown to a height of twenty feet is 183 feet per second. If we place a rock under the can where the can will impact the ground the seams should burst without spilling the beans.

The chemist's response is:

That's too risky since we can't be sure we will throw the can to the correct height. Your plan may result in the loss of precious food. I've got a better idea. I've calculated the boiling temperature of the beans. Let's start a fire and heat the can for one minute, thirty-seven seconds the time needed to just burst the seams. This method is less risky since we can always push the can off the fire if it starts to burst sooner.

The economist's reaction is:

Both of your methods may work, but they are two complicated. I have a simple solution that will result with successfully opening the can every time. Just assume a can opener.<sup>14</sup>

Many scholars, often to the frustration of others,<sup>15</sup> have made different assumptions, not only regarding how to open the beans' tin can, but even on how to define the tin can.<sup>16</sup> The re-

14. A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 1 (1983).

15. See Mark Kelman, *On Democracy-Bashing: A Skeptical Look at the Theoretical and 'Empirical' Practice of the Public Choice Movement*, 74 VA. L. REV. 199 (1988).

16. See generally *Buckley v. Valeo*, 424 U.S. 1 (1976) (upholding federal statute that limited rent-seeking through political contributions); *Harper v. Virginia Bd. of Elections*, 383 U.S. 663 (1966) (striking down poll tax because it, in light of rent-seeking, deters voting); *Williamson v. Lee Optical of Okla., Inc.*,

sult is different definitions and theories of rent-seeking.<sup>17</sup> There are, however, core principles contained within the more influential theories upon which most scholars agree.<sup>18</sup> For example, persons will commit resources, even to the point of waste, where they produce the greatest profit.<sup>19</sup> The result is that individuals will invest resources in attempts to form monopolies until the marginal cost equals the properly discounted return.<sup>20</sup> When other persons, or the government, try to help or prevent this accumulation of resources, those resources that cancel each other out are wasted.<sup>21</sup> This phenomenon can be isolated by economic equations representing supply versus demand and potential returns versus resource investment.<sup>22</sup> Although this Note will not address the societal loss of the resource expenditure of competing persons,<sup>23</sup> it is central that persons will commit resources to areas that will produce the greatest marginal profit (and that it can be modeled).

The operation of the rent-seeking theory in a particular system depends on the level of restriction in that system. There is a continuum between a system of no restrictions and a perfectly restricted system.<sup>24</sup> On one side of the continuum is an economy

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348 U.S. 483 (1955) (upholding rent-seeking legislation that forbid an optician from fitting glasses without a prescription from an ophthalmologist or optometrist); ROBERT B. EKELUND, JR. & ROBERT D. TOLLISON, *MERCANTILISM AS A RENT-SEEKING SOCIETY* (1981) (asserting that the balance-of-trade objective of mercantilism resulted from the relationships between rent-seeking individuals); DOUGLAS G. HARTLE, *THE EXPENDITURE BUDGET PROCESS OF THE GOVERNMENT OF CANADA* (1988) (discussing of the process of Canadian budget expenditures decisions using rent-seeking); GLENN R. PARKER, *CONGRESS AND THE RENT-SEEKING SOCIETY* (1996) (discussing that significant factors in motivating legislators to seek Congressional careers are the intrinsic returns associated with legislative service); GORDON TULLOCK, *RENT SEEKING* (Edward Elgar ed., 1993) (ground-breaking work on the definition and application of the rent-seeking theory); *THE POLITICAL ECONOMY OF RENT-SEEKING* (Charles K. Rowley et al eds., 1988) (collecting theoretical, empirical, and institutional articles).

17. See *supra* note 16.

18. Rent-seeking is a sophisticated theory with considerable scholarship. This summary is by no means exhaustive. This Part is a sampling of the writing that most influenced this Note.

19. Gordon Tullock, *The Welfare Costs of Tariffs, Monopolies, and Theft*, 5 W. ECON. J. 224 (1967).

20. See *id.* at 230.

21. See *id.*

22. See *id.* at 224.

23. See *infra* note 37.

24. See Anne O. Krueger, *The Political Economy of the Rent-Seeking Society*, 64 AM. ECON. REV. 291, 302 (1974) (stating that persons will expend resources to compete for licenses when imports are limited by quantitative restrictions and marking the introduction of the term "rent-seeking").

with no restrictions.<sup>25</sup> Entrepreneurs would seek windfall gains by adopting new technology, anticipating market shifts, etc.<sup>26</sup> On the other side of the continuum is an economy with perfect restrictions, which would have such persuasive regulations that rent reeking would be the only route to gain.<sup>27</sup> In reality, all market economies have some restrictions that generate higher profits for sellers and higher costs for purchasers.<sup>28</sup> Those higher profits and costs are called "rents."<sup>29</sup> In such a system, entrepreneurs devote time and resources to capturing windfall rents.<sup>30</sup>

These behaviors are not only exhibited by living, breathing humans. Bureaucratic institutions behave like rent-seeking individuals.<sup>31</sup> Each institution acts to attract a more favorable distribution of government production rights<sup>32</sup> and this competition leads to bureaucratic inefficiencies.<sup>33</sup> Therefore, rent-seeking is a balance of competing forces: supply versus demand and potential returns versus resource investment.<sup>34</sup> This balance illustrates that persons are willing to invest resources in attempts to achieve a profit status until the profit margin is eliminated.<sup>35</sup> When supply is restricted by quantitative restrictions, persons and institutions will expend resources to compete for the limited supply.<sup>36</sup>

This statement of rent-seeking is difficult to apply because of its breadth, so a closer examination is needed. Rent-seeking is the tendency of an expected gain to be translated into costs through competitive efforts,<sup>37</sup> explained as a pricing<sup>38</sup> arrange-

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25. *See id.*

26. *See id.*

27. *See id.*

28. *See id.*

29. *See id.*

30. *See* Krueger, *supra* note 24.

31. *See* Roger L. Faith, *Rent-Seeking Aspects of Bureaucratic Competition*, in *TOWARD A THEORY OF THE RENT-SEEKING SOCIETY* 332, 342 (James Buchanan et al., eds. 1980).

32. *See id.*

33. *See id.* *See also supra* note 21 and accompanying text.

34. *See* Tullock, *supra* note 19.

35. *See supra* note 20 and accompanying text.

36. *See* Krueger, *supra* note 24 and accompanying text.

37. *See* POSNER, *supra* note 12, at 41 n.3. Posner focuses on the societal "costs" of rent-seeking. He sees a problem with rent-seeking in the following situation. A ship is abandoned with \$1 million in property. It will cost \$250,000 to claim the property. Four individual parties expend the \$250,000 to recover the \$1 million but only one is successful. The total cost to society is \$1 million and the total benefit is \$1 million. Had only one party searched for, and found, the property the cost to society would have been \$250,000 with the same

ment, illustrated by an equation. The "expected gain" is the benefit the seller will receive from the sale of the property; money is often an expected gain from the sale of property. The "competitive efforts" are multiple sellers trying to attract a purchaser through incentives; lowering the asking price of property may be a competitive effort. When a seller uses competitive efforts to attract a purchaser, the seller incurs costs;<sup>39</sup> as a seller lowers the asking price of property, she will inevitably receive less compensation for that property than before she lowered the price. Therefore, the "tendency" is that the seller, anticipating the expected gain from the sale and attracting purchasers through competitive efforts, will decrease the price resulting in costs to the seller.<sup>40</sup> Any fiscally sound seller will bind its costs so that a premium of its expected gain is preserved while optimizing its competitive efforts.<sup>41</sup> The aforementioned theory is simply an equation determining price by competition. So, to more easily and completely understand rent-seeking, pricing must be addressed.

## B. CONSTRUCTING THE PRICING EQUATION

The pricing of property can be explained by an equation that takes into account sellers' and purchasers' needs to sell and buy

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benefit. Therefore, society lost \$750,000 by the four parties competing. *See id.* at 41. This is Posner's "tendency of an [individual] expected gain to be translated into [societal] costs through [individual] competitive efforts." The "expected gain" is the \$1 million, the "competitive efforts" are the expenditures in pursuit of the "expected gain," and the "costs" is the \$750,000 difference between the "expected gain" and the "competitive efforts." Posner uses *personal* expected gain and *personal* competitive efforts to show *societal* costs. This Note uses *personal* expected gain and *personal* competitive efforts to show *personal* costs. The causal connection is much more clear because the \$750,000 difference is not clearly a societal cost because the money is transferred to others in society. It is more of a societal shift. However, there is clearly a personal cost of \$250,000 for each group that does not find the treasure. Therefore, this Note is less concerned with the question of whether rent-seeking hurts or benefits society or individuals, just whether it helps explain United States-Canadian sports competition disadvantages.

38. "Pricing," "property," "purchase" and other similar terms are not used here as terms-of-art but as general descriptors of the sale transaction.

39. The term "costs" is used in a different manner but for the same idea than earlier. *See supra* note 29 and accompanying text. Note 29 (and accompanying text) refers to the seller seeking rents when the purchaser's opportunity is limited due to quantitative restrictions, thus driving price up. However, here the opportunity to sell is limited, so the sellers are competing for purchasers, thus driving price down.

40. The tendency is also the attraction of the buyers to the transaction that creates the greatest profit. *See supra* note 19 and accompanying text.

41. *See supra* notes 20, 35 and accompanying text.



respectively, where "need" is the term describing competitive efforts. In a standard sales transaction,<sup>42</sup> the seller's need is the ratio between her competition, other sellers, and her substitutable alternatives, purchasers. The purchaser's need is the ratio between his competition, other purchasers, and his substitutable alternatives, sellers.

The following price equation helps to understand rent-seeking because it isolates the factors that contribute to it. The seller's and purchaser's needs are compared to determine the sale price. For example, assume A is the owner of property and wants to sell that property to a prospective purchaser, X, to be used in X's business. Under normal circumstances, A would sell the property to X at a price (P) determined by X's need to buy the property ( $X_n$ ) divided A's need to sell the property ( $A_n$ ) plus a variable (k) representing the emotional necessity to buy ( $k_x$ ) and sell ( $k_a$ ) times a constant coefficient (c) that translates the needs into actual dollars.<sup>43</sup> Therefore,

$$P(n)=c\left(\frac{X_n}{A_n}+k\right) \text{ where } X_n, A_n>0 \text{ and } k=k_x-k_a$$

represents price as a ratio of the seller's and purchaser's needs due to competition.

The equation is better understood by example. Assume for the moment that A and X are the only two parties to the transaction. When A and X are at par needs the property should sell at the coefficient translating need into dollars.<sup>44</sup> A "par" need is one no greater and no less than any other actor would have in

42. The term "sales transaction" is used to describe the general exchange of benefits, in addition to exchanges of money for property. For example, the granting of a stadium and tax benefits by a municipality to attract a professional sports franchise is a sales transaction.

43. Assuming that persons in a transaction are sane, somewhat intelligent and not compelled to participate, a person will not participate in a sales transaction if she has no need. Since A's need to sell and X's need to buy is never zero or below, because they would then not participate in the transaction,  $A_n$  and  $X_n$  are always above zero. The variable "k" actually represents the difference between the purchaser's emotional necessity to buy and the seller's emotional necessity to sell, thus  $k=k_x-k_a$ .

Notice that there is a difference between the words "necessity" and "need." Necessity is used to describe the emotional quotient that enters into every sales transaction. Necessity, which is based upon personality and emotion, may be different for two individuals in the exact same position. However need is used to describe the comparison between a party's competition and substitutable alternatives. Need will be the same for all similarly situated persons because it is solely a mathematic determination.

44. Par exists at the numerical value of one. A need greater than par would be above the value one, and a need less than par would have a numerical value below one.

the same position: A's need equals X's need.<sup>45</sup> The paradigm par sale occurs when there are equal amounts of substitutable alternatives as competitors, both on the sellers' and purchasers' sides.

Now assume there is one party, X, that is interested in purchasing A's property. These are A's substitutable alternatives.<sup>46</sup> Also assume there are five properties for sale that will suit X's purposes—these are A's competitors.<sup>47</sup> A's competition is greater than A's substitutable alternatives so A's need is above par. In this case, the numerical representation of  $A_n$  would be above 1, possibly 1.2.<sup>48</sup> Alternatively, X's need to buy A's property is less than par because X's competition is less than X's substitutable alternatives. The numerical representation of X's need is below 1, possibly 0.8.<sup>49</sup> Finally, assume that A's emotional necessity to sell is the same as X's emotional necessity to buy. Thus, the price to be paid by X for A's property is

$$P(n)=c\left(\frac{0.8}{1.2}\right) \text{ where } k=k_x-k_a=0$$

$$P=\frac{2}{3}c.$$

Logically, the price is drastically below par value, in fact two-thirds par value, because A's need to sell to X is greater than X's need to buy from A.

45. Thus, par is represented by  $X_n=A_n$ .

46. "Competition" is the term this Note uses to describe one party's competition for another's business, while "substitutable alternatives" is the term this Note uses to describe the latter party's competition for the former party's business. For example, a seller's substitutable alternatives are all those who she believes want to buy her property. A seller's competition is all those who she believes are selling property similar to hers.

47. The seller's substitutable alternatives and the purchaser's competition are often not the same. Substitutable alternatives and competition must be viewed from the perspective of the party and not with general omniscience. For example, A owns a rare book. X, a pirate, wants to buy a rare book. A only wants to sell the book to a pirate. A's substitutable alternatives are other pirate interested in buying the book. However, X's competition may be all prospective purchasers of rare books, a group larger than the actual competition (and the substitutable alternatives). Thus, it is easy to see that knowledge about the specifics of the substitutable alternatives and competition may determine eventual price. The greater the parties knowledge about her and the other's needs in respect to the other party's knowledge the better price she will receive. Often the universe for one term is different than the universe for the other, but the two always overlap for at least one case, where the transaction is possible to occur.

48. The number "1.2" is for example only and may not correspond to the actual value of A's need.

49. See *supra* note 48.

In practice, this equation is unhelpful because it oversimplifies the actual pricing phenomenon and does not address how to quantify each party's need.<sup>50</sup> In most transactions there are not just two participants, but many. Each participant engages with the others for many different properties. This leads to many potential sales transactions as different purchasers and sellers interact. Therefore, A's need to sell the property ( $A_n$ ) and X's need to buy the property ( $X_n$ ) should be further examined. The parties' needs can be determined by comparing the substitutable alternatives and competition for those substitutables, including the competition for A's property.

The seller's need may be represented by the ratio of A's substitutable alternatives (purchasers),  $S_a$ , and A's competition (other sellers),  $T_a$ .<sup>51</sup> Therefore,

$$A_n = \frac{T_a}{S_a}.$$

Alternatively the purchaser's need,  $X_n$ , is the ratio of X's substitutable alternatives (sellers),  $S_x$ , and X's competition (other purchasers),  $T_x$ . Therefore,

$$X_n = \frac{T_x}{S_x}.$$

The property sale price equation from above is then completed as such,

$$P(x,a) = c \left( \frac{T_x}{S_x} + k \right) \frac{T_a}{S_a}.$$

### C. DEFINING RENT-SEEKING MATHEMATICALLY: A RETURN TO FIRST PRINCIPLES

The price equation isolates the rent-seeking phenomenon. When A chooses to attract a particular purchaser, X, she can increase X's need,  $\frac{T_x}{S_x}$ , by either decreasing X's perception of the

50. The terms substitutable alternatives and competition are used in the above analysis however are not defined until now in an attempt to break down and simplify the process.

51. The term par is also used in this context for when the substitutable alternatives equal the competition. Again par is numerically represented by the value 1. See *supra* note 44.

substitutable alternatives for A's property, from X's perspective,  $S_x$ , or increasing X's perception of competition for A's property,  $T_x$ . There are many ways A can accomplish this, including lowering the asking price or making capital improvements without increasing price. If there are several sellers competing for a particular X's business, and X can only purchase from a portion of the selling As, rent-seeking comes into play. The selling As will compete to make their properties more and more beneficial and X will buy from the A who makes X's cost the lowest.<sup>52</sup> If enough As compete, X's purchase price may be well below the par value of the property approaching the elimination of marginal gains.<sup>53</sup>

This definition is functional and retains the principles of the earlier scholarship. Individuals will commit resources where they produce the greatest profit<sup>54</sup> and invest resources in attempts to form monopolies until the marginal cost equals the properly discounted return.<sup>55</sup> Here, the seller is taking advantage of the rent-seeking theory to attract a purchaser. Also, economic equations can represent this phenomenon,<sup>56</sup> a basic premise of the preceding subpart. And finally, the operation of the rent-seeking theory in a particular system depends on the level of restriction in that system<sup>57</sup> and these behaviors are evidenced by bureaucratic institutions.<sup>58</sup> Professional sports franchises are bureaucratic institutions in highly restricted industries.

In summary, every sale can be characterized by an equation that equates price paid with the purchaser's need to buy, divided by seller's need to sell, plus the difference of the parties' emotional necessity, times a translation coefficient. The seller's need to sell and the purchaser's need to buy can each be determined by the quotient of the substitutable alternatives and competition affecting each party. By manipulating the seller's or purchaser's need equations a seller can attract a purchaser to a particular property in lieu of other sellers' property. In turn, purchasers will seek the most attractive buying opportunity—the one that will allow for the greatest profit margin. A seller will use that tendency to attract purchasers.

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52. See *supra* notes 20, 35 and accompanying text.

53. See *supra* notes 20-40 and accompanying text.

54. See Tullock, *supra* note 19.

55. See *supra* note 20 and accompanying text.

56. See *supra* note 22 and accompanying text.

57. See *supra* notes 24-30 and accompanying text.

58. See *supra* note 31 and accompanying text.

## II EXAMINING FRANCHISE COMPETITION: A VIEW TO SPORTS POLICY

This Part examines the Toronto Blue Jays' and Montreal Expos' success, or lack thereof, with reference to the competitiveness of other sports franchises in Canada, resulting in the conclusion that Canadian franchises are not competitive. Although this Part focuses on baseball, the other major international American sports franchises located in Canada are not immune from the competitive disadvantage problem.<sup>59</sup> This Note focuses on the Major League Baseball (MLB) teams because they are the oldest existing continuous United States professional sports franchises in Canada and have the most reported information.

MLB arrived in Canada when Montreal was awarded a baseball team in 1969 for a \$13 million franchise fee.<sup>60</sup> Toronto was awarded a franchise in 1977 for \$7 million.<sup>61</sup> Between 1969 and 1995, Montreal won 2148 games and lost 2200 games, for a .494 win-loss percentage, and won two division championships.<sup>62</sup> Between 1977 and 1995, Toronto won 1499 games and lost 1561 games, for a .490 win-loss percentage, and won five division championships.<sup>63</sup> In 1990-1991, Toronto made \$20.1 million in profits on \$83.1 million in revenue, while Montreal made \$1.1 million in profits on \$37.4 million in revenue.<sup>64</sup> A team's revenue earned is directly related to the team's winning percentage.<sup>65</sup> However, it is unclear whether athletic competitiveness leads to fiscal competitiveness, or vice versa.<sup>66</sup> In any case, Montreal had the lowest revenue in baseball in 1990-1991.<sup>67</sup> Whatever success either team may have had in any particular year, the fact that neither team has an overall record

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59. See *infra* notes 69-73 and accompanying text.

60. See FRANK P. JOZSA, JR. & JOHN J. GUTHRIE, JR., RELOCATING TEAMS AND EXPANDING LEAGUES IN PROFESSIONAL SPORTS 49 (1999).

61. See *id.* at 46.

62. See ROSENTRUB, *supra* note 1, at 334. The championships may be explained as an anomaly because both division championships were during strike seasons (1981, 1994). See *id.*

63. See *id.* at 346.

64. See GERALD W. SCULLY, THE MARKET STRUCTURE OF SPORTS 118 (1995). Note that Montreal had the lowest revenue although eleven teams are located in United States cities with a population smaller than Montreal's and seven teams had a win-loss record worse than Montreal's. See *id.* at 119.

65. See SCULLY, *supra* note 64, at 68-69.

66. This Note will not determine which contributes to the other in what situations because it is a "chicken and the egg" problem.

67. See SCULLY, *supra* note 64, at 119.

above .500 indicates that, in general, Canadian teams lose.<sup>68</sup> Therefore, athletically and economically, the Canadian franchises have not demonstrated an ability to compete.

The other United States sports corporations with Canadian franchises have evidenced much of the same problem. The National Hockey League's (NHL) Ottawa Senators will relocate to the United States to avoid Canadian taxes, which caused the team to lose \$7 million during the 1997-98 season.<sup>69</sup> The National Basketball Association (NBA) restrictions on high-end salaries damage the Vancouver Grizzlies ability to attract and keep talent.<sup>70</sup> In 1998, basketball player Kendall Gill threatened to retire if he was traded to the NBA's Toronto Raptors. Similarly, after being traded to Toronto, Kenny Anderson refused to report to his new team.<sup>71</sup> Damon Stoudamire and Doug Christie, formerly of the Raptors, each forced a trade out of Toronto.<sup>72</sup> However, the inability to sign free agents is not limited to basketball franchises. Since 1985, at least 12 superstar-caliber players have left the Montreal Expos to play for other teams.<sup>73</sup> To be competitive, sports franchises, like all other businesses, must have the talent to succeed. The fact that Canadian franchises have trouble keeping that talent, coupled with their losing history and fiscal troubles, supports the conclusion that United States sports franchises in Canada have problems competing.

### III EXPLAINING THE DISADVANTAGE: A CLOSER LOOK AT SPORTS POLICY

#### A. EXAMINING COMPETITION: THE PAST EXPLANATIONS

Some commentators have opined that the competitive disadvantage can be explained by the following factors: perceived distance of Canada, the frigid weather, low Canadian interest in

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68. Year to year variances may be explained by good personnel moves, players playing above their norm, good coaching, strikes etc. See *supra* note 62.

69. See *Taxes Have Senators Considering Relocation*, TAMPA TRIBUNE, Feb. 26, 1999, at 6.

70. See *Inside Dish: Front Office Rumbings and Locker Room Whispers*, SPORTING NEWS, Nov. 30, 1998, at 92.

71. See David Moore, *Disorder off the Court*, SPORTING NEWS, March 2, 1998, at 29, 30.

72. See Bill Harris, *Tax Situation Gets Break*, TORONTO SUN, Feb. 28, 1998, at S14.

73. Gary Carter, Andres Galarraga, Delino DeShields, Tim Wallach, Hubie Brooks, Andre Dawson, Marquis Grissom, Larry Walker, Ken Hill, Mark Langston, Randy Johnson, and John Wettland. See ROSENTRAUB, *supra* note 1, at 337.

United States sports, and the lack of municipal support.<sup>74</sup> This Note does not address the first two factors because Canada is not significantly farther or colder than other cities with professional sports franchises.<sup>75</sup> The critics also claim that the tax structure in Canada and the declining value of the Canadian dollar also make it impossible for Canadian sports franchises to be competitive.<sup>76</sup> Other arguments are that Canadian governments are more reluctant than their United States counterparts to assist teams in building stadiums, United States governments award property tax waivers to teams where Canadian teams pay full taxes, and the level of personal and property taxes makes Canada less attractive to players.<sup>77</sup> One commentator says that "[t]here are 29 teams in the NBA, and each of them competes on the same size floor and the same basket, but there is economic disparity because of the currency and taxes in Canada. You can't have 27 teams playing on one field and two on a slanted field."<sup>78</sup> The argument continues that there is a difference between the treatment of professional sports franchises in Canada and in the United States,

since the Reagan administration slashed the top rate for federal personal income tax from 50 percent to 39.6 percent in 1983, pro athletes in major league baseball, the NBA and the NHL have balked at playing for Canadian teams because of the higher tax rate and lesser value of the Canadian dollar.<sup>79</sup>

Furthermore,

[w]hen Toronto was awarded a [NBA] franchise five years ago, Revenue Canada interpreted its tax code so that players who didn't main-

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74. See David DuPree, *Anderson Might Nix Raptors-Blazers Deal*, USA TODAY, Feb. 16, 1998, at 8C.

75. The distance between: New York, New York and Toronto, Ontario is 347 miles; between New York and Montreal, Quebec is 334 miles; between Los Angeles, California and Toronto is 2183; and between Los Angeles and Montreal is 2475. This should be compared to the distance between New York and Los Angeles (2462 miles). *How Far Is It?* (last visited March 17, 2000) <<http://www.indo.com/distance/>>. The average low January temperature in: Minneapolis, Minnesota is -9° F; Milwaukee, Wisconsin is -1° F; Detroit, Michigan is 6° F; Toronto, Ontario is 1° F; and Montreal, Quebec is 7° F. *Excite Travel Fact Sheet* (last visited March 17, 2000) <[http://www.excite.com/travel/regions/north\\_america/](http://www.excite.com/travel/regions/north_america/)>.

76. See Roscoe Nance, *Many Players Balk at Canadian Taxes*, USA TODAY, Feb. 17, 1998, at 10C.

77. See Al Strachan, *The American Experience: Because of the Crippling Level of Canadian Taxes, Players Will Accept Less In Real Dollars to Play in the United States*, TORONTO SUN, April 29, 1999, at H3.

78. *Canadian Tax Bite Irritates NBA Players*, CHI. TRIBUNE, Feb. 15, 1998, at C12 (Chicagoland edition).

79. Mark Asher, *A Taxing Situation; Playing in Canada May Impact Francis Financially*, WASH. POST, July 27, 1999, at D03.

tain a permanent residence in Canada would have to pay the heavier Canada taxes on roughly 50% of their salaries, based on the fact that half of their games are played there. But last spring the tax code was reinterpreted, and players began to be taxed for each day they worked in Canada, meaning for games *and* practices. They then paid Canadian taxes on about 65% of their salary.<sup>80</sup>

In summary, all of the major criticism falls into one category: that the Canadian government's policy and the Canadian public opinion create the disadvantage.

#### B. EXAMINING COMPETITION: REFUTING THE PREVIOUS EXPLANATIONS

The explanations in subpart A depend on uncited, significant distinctions between the Canadian and United States social and political systems. However, no such distinction exists. If the systems are similar with respect to professional sports, then there must be some other reason the taxes and other economic disadvantages are different.

Upon comparison of the two countries, the argument that the political structure of one is clearly more conducive to locating a successful professional sports franchise is erroneous. The governments are very similar in structure and policy. The Canadian political system is based upon parliamentary sovereignty and a federalism system,<sup>81</sup> while the United States system is based upon separation of powers<sup>82</sup> and federalism.<sup>83</sup> The Canadian authority is split between the centralized federal government and the provinces, with federal superiority where concurrent jurisdiction exists.<sup>84</sup> The Cabinet links the Parliament to the Bureaucracy and local government is created by the provinces.<sup>85</sup> Local government is a mix of unitary and two-tiered local authorities and specialist boards.<sup>86</sup> A powerful interest group policy community moderated by the central role of the Cabinet and the legitimating role of the Parliament best characterizes the Canadian political process.<sup>87</sup> Since the late

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80. Jackie MacMullan, *Inside the NBA*, SPORTS ILLUSTRATED, March 2, 1998, at 118.

81. See British North America Act of 1867.

82. See U.S. CONST. arts. I, II, III.

83. See U.S. CONST. amends. IX, X.

84. See BARRIE HOULIHAN, SPORT, POLICY AND POLITICS 32 (1997).

85. See *id.* at 32, 33.

86. See *id.* at 118.

87. See *id.* at 38.



1960s "the Canadian government has provided substantial financial and organizational support for sport."<sup>88</sup>

Similarly, the United States federal authority is split into executive,<sup>89</sup> legislative,<sup>90</sup> and judicial branches.<sup>91</sup> The states are granted all "powers not delegated to the United States by the Constitution"<sup>92</sup> and most are structured similarly to the federal government.<sup>93</sup> The powers of local government are completely granted by the governing state and typically include city and county subgovernments.<sup>94</sup> The general characteristic of United States local government is its fragmentation of administrative units.<sup>95</sup> The fragmentation and complexity of the United States system increases the number of clearance points for policy and the tendency towards incrementalism.<sup>96</sup> Finally, "the overriding themes of sport in America are class, social integration and commercialism."<sup>97</sup> Therefore, there are no differences between United States and Canadian sports policy or government structure that would explain the professional sports competitive disadvantage.

Nor can the government behaviors explain the competitive difference.<sup>98</sup> Originally, there was tremendous public sector support for the attraction of a MLB team to Canada. In 1994, Montreal and Toronto had populations of about 3.3 million and 4.3 million, respectively, showing a strong consumer base.<sup>99</sup> The two most expensive single site sports projects in North America, the Montreal Expos's Olympic Stadium and the Toronto Blue Jays's Skydome, are found in Canada.<sup>100</sup> The two facilities cost the Canadian government in excess of \$1.625 billion Canadian.<sup>101</sup> Canada's great national debt, Quebec's provincial debt,

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88. *Id.* at 36.

89. *See* U.S. CONST. art. II.

90. *See* U.S. CONST. art. I.

91. *See* U.S. CONST. art. III.

92. U.S. CONST. amend. X.

93. *See* HOULIHAN, *supra* note 84, at 53.

94. *See id.* at 54.

95. *See id.* at 138.

96. *See id.* at 58.

97. *Id.* at 55.

98. This Note acknowledges the difference between government policy and structure and government behavior. Policy and structure are formal, while behavior is not.

99. *See* ROSENTRAU, *supra* note 1, at 327. The provinces of Quebec (Montreal) and Ontario (Toronto) had populations of about 7.3 million and 11 million, respectively, in 1995. *See id.*

100. *See id.* at 321.

101. *See id.*

and the fact that the residents of Montreal still pay a tax for the construction of Olympic Stadium make it very unlikely that the Expos will receive any public sector support for a new stadium,<sup>102</sup> not because of the political or legal structure, but because of fiscal constraints.<sup>103</sup>

In Toronto, where the oft-delayed<sup>104</sup> and greatly over-budget<sup>105</sup> Skydome was built for the Blue Jays, public sector support for the team has also neared economically feasible limits. Funding for the stadium was originally \$60 million (Canadian) public tax share, \$30 million (Canadian) invested by the province, \$30 million (Canadian) invested by the city, and 30 private corporations investing \$5 million (Canadian) each.<sup>106</sup> The private corporations would share in any stadium profits but the public-sector partners would account for all cost overruns.<sup>107</sup> Unfortunately, the stadium never generated enough revenue to pay off its debt, let alone create profit, thus the public-sector partners were still paying \$60,000 (Canadian) a day in interest alone until they sold their share in the stadium to private parties in 1992.<sup>108</sup> Therefore, there was significant Canadian municipal participation in attracting and supporting the professional sports franchises.

Even if the policies or governmental structures were different, the resulting competitive data does not support a claim that the structure, policy, or behavior is to blame. Assuming that the distinctions between the Canadian and United States political arena explain the competitive disadvantage, *any* team in the United States would be better off than *any* team in Canada. However, there are five United States franchises whose competitive ranking is equal to or lower than both Toronto's and Mon-

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102. *But see* Jim Souhan, *Team Paints Picture of Progress*, STAR TRIBUNE, March 16, 2000, at C1 (explaining how the Expos' new owner plans on building a new stadium, possibly with public support, and spending more money on players).

103. *See* ROSENSTRAUB, *supra* note 1, at 341.

104. *See id.* at 348. Ontario's premier, William Davis, appointed a three-person committee to determine the site for the stadium in mid-1983 and the dome opened in mid-1989. *See id.*

105. *See id.* at 348, 351. Initial budget proposals were approximately \$150 million (Canadian) and the final cost is estimated at \$628 million (Canadian). *See id.*

106. *See id.* at 349.

107. *See* ROSENSTRAUB, *supra* note 1, at 350.

108. *See id.* at 351-54.

treat's.<sup>109</sup> Therefore, any argument that explains the Canadian franchise competitive disadvantage by drawing a distinction between the two Country's political structure and sports policies is misleading.

### C. EXPLAINING THE PROBLEM: APPLYING DIFFERENTIAL RENT-SEEKING

As discussed above, rent-seeking does not occur in a vacuum.<sup>110</sup> Rather, it occurs in multi-dimensional layers. On the whole, it is best described as an onion. Each layer contributing to and building on the other. When the layers are individual, it is unidentifiable, but when together the onion is apparent. The onion can be sliced across the layers to isolate particular tendencies, like the sweet flesh near the top or the juicy matter near the middle. One of these rent-seeking slices is "differential rent-seeking." Differential rent-seeking occurs when *multiple* competitors benefit from *different* rent-seeking schemes because of *different* situations surrounding their individual sales transactions.<sup>111</sup>

For example, using the rent-seeking equation presented *supra* in subpart II.C, X and Y are purchasers of A's product. X lives on the West Coast of the United States and Y lives on the East Coast. X purchases A's product in 1995 and Y purchases it in 1997. A's product sales on the West Coast in 1995 have no competition, but A's product sales on the East Coast in 1997 have several competitors. For simplicity, it can be assumed that there are no substitutable alternatives for A's product, that X and Y are the only purchasers of the product, that A, X, and Y have the same knowledge, that the emotional necessity equations for X and Y in respect to A are equal, and that the product is essentially the same on the West Coast in 1995 as it is on the East Coast in 1997.<sup>112</sup> The rent-seeking equations will look as such:

109. See Jozsa, *supra* note 60, at 139 (The rank is determined by adding performance, attendance and value. Minnesota, Kansas City and San Diego are ranked below Toronto and Montreal; Milwaukee is tied with Montreal).

110. See discussion *supra* Part I.

111. Again this Note is using sale/price terminology to describe the situation generally. See *supra* notes 38, 42.

112. Therefore in 1995 on the West Coast X's substitutable alternatives for A's product equal A's competition, because there are none of either. Conversely, A's substitutable alternatives for X's purchase equal X's competition, because there are also none of either. Of course, X's substitutable alternatives then equal X's competition and A's substitutable alternatives equal A's Competition. In 1997 on the East Coast A's substitutable alternatives and Y's competition

$$P(x,a) = c \left( \frac{\frac{T_x}{S_x}}{\frac{T_a}{S_a}} + k \right) \text{ where } S_x = T_x = S_a = T_a$$

$$P(y,a) = c \left( \frac{\frac{T_y}{S_y}}{\frac{T_a}{S_a}} + k \right) \text{ where } S_y = T_a > 1 > T_y = S_a > 0.$$

The two equations each represent a different layer in the rent-seeking onion. The comparison of the two layers is the slicing of the onion. These equations may be simplified as such:

$$P(x,a) = c(1+k).$$

$$P(y,a) = c\left(\frac{1}{r} + k\right), \text{ where } r > 1.$$

Therefore,  $P(y,a)$  is smaller than  $P(x,a)$ <sup>113</sup> which means that the price paid by X for A's product will be higher than the price paid by Y for A's product. This is logical, because if all else is equal, the purchaser purchasing when A has no competition will pay a higher price than one purchasing when A has competition.

This equation isolates the problem of differential rent-seeking. Assume, in this limited context, that X and Y are competitors and that the price charged by A remains the same so long as a purchaser purchases from her. Since the price paid by X is higher than the price paid by Y, Y has an advantage in creating a greater profit margin. Y may either charge the same price as X and receive more profit, or charge less than X and receive more market share.<sup>114</sup> X therefore has a continuing competitive disadvantage.

The differential rent-seeking theory is supported by the principle rent-seeking theories discussed earlier.<sup>115</sup> Rent-seeking can be viewed by equations representing supply versus demand and potential returns versus resource investment.<sup>116</sup> The price equation asserted in this Note does just that. It uses substitutable alternatives and competition to determine the supply

are also equal with the A-X situation, but Y's substitutable alternatives and A's competition, are equal at a higher value.

113. Assuming Y's emotional necessity to buy A's product is not so much greater than X's as to override the need factors.

114. Note that this assumes the operating costs for the two persons are similar. Additionally, the choice of whether to increase profits or market may not be mutually exclusive.

115. See discussion *supra* Part I.A.

116. See *supra* notes 19, 34 and accompanying text.

and demand and results in a "price" which is just the return on resource investment. Under the price equation, a person is willing to invest resources in attempts to achieve a profit until the price exceeds the potential profit. In the case of differential rent-seeking, supply is restricted by quantitative restrictions, and persons expend resources to compete for the limited supply.<sup>117</sup> Any program that creates rent-seeking will be more difficult to modify or repeal, thus differential rent seeking will be a continuing disadvantage. And finally, because institutions behave like rent-seeking individuals, the fact that franchises and corporations are discussed does not change the dynamic.<sup>118</sup> Therefore, differential rent-seeking is supported by the aforementioned scholarship.<sup>119</sup>

The theory of differential rent-seeking can be used to explain why the Canadian franchises of United States sports leagues have a competitive disadvantage versus their United States counterparts. The significant rent-seeking problem in professional sports is that the sports corporations have inadvertently adjusted the "needs" in the price equation discussed in Part I.C.<sup>120</sup> Part II.C merely lists the symptoms of the disease. During expansion, the sports corporation will place a franchise where it believes the corporation will receive the most benefit.<sup>121</sup>

117. See *supra* note 36 and accompanying text.

118. See Faith, *supra* note 31, at 332.

119. Ann O. Krueger spoke of a continuum of rent-seeking, from strictly limited to completely free. Differential rent-seeking merely states that in certain competitive atmospheres on business can be closer to one side of the spectrum while another business is near the other. See *supra* notes 24-30 and accompanying text.

120. The league itself sometimes creates limitations that affect the price equation.

The real issue is how we can protect our cities from blackmail by vagabond sport franchises playing the cities and their taxpayers against each other. This is a problem we face in all professional sports. Even baseball, which boasts of its franchise stability courtesy of its non-statutory [antitrust] exemption, frequently uses the threat of relocation to negotiate lucrative stadium deals at taxpayer expense.  
[. . .]

Unfortunately, I have seen precious little indication that the NFL or other sports leagues are willing to do anything to respond to the problem. Instead, the leagues have created a chronic shortage of franchises. . . .

*Professional Sports Franchises Relocation: Antitrust Implications: Hearing before the House Comm. on the Judiciary*, 104th Cong. 4 (1996) (statement of John Conyers, ranking minority member of Judiciary Committee).

121. There are several factors that must go into determining where to locate a franchise including profitability and league exposure. This Note combines all those factors into a net benefit to the corporation.

When there were no franchises, the corporation was able to locate teams anywhere limited only by clearly apparent economic feasibilities. However, as the leagues grow, the level of benefit each potential expansion city offers decreases.<sup>122</sup> As the benefit each city can offer dips below the level of competitiveness, that city ceases to be in the running for an expansion franchise. Therefore, once a league has significantly expanded, the number of cities competing to woo a franchise decreases. With that decrease of competition comes a decrease in rent-seeking benefit awarded to each franchise, resulting in differential rent-seeking. With the change in geographic wealth distribution, some franchises are able to rent-seek more freely than others.<sup>123</sup>

Again, an example best illustrates the phenomenon. A professional sports corporation decides to expand in two phases, one new team in 1990 (franchise X) and two new teams in 2000 (franchises Y and Z). City A is competing with cities B and C for franchise X. No other cities can compete for the franchise. Assuming that each city is exactly the same and every party knows all the pertinent details of the expansion, the price equation for the expansion may look like this,

$$P(x,a)=P(x,b)=P(x,c).$$

The substitutable alternatives and competition for city A are equivalent because cities B and C are the same as A. The need of each city is equal. However, in reality, each city will not be the same and each may not know of the other's situation. Similarly, the seller, the expanding professional sports corporation, may not be completely aware of the entire circumstances. For example, A and B may know of the second phase of expansion while C does not. Since they realize that every city will receive a team their need and X's need, in respect to them, is different than C's need and X's need in respect to C. Thus, the hierarchy may look like this:

$$\frac{T_c}{S_c} > 1 > \frac{T_a}{S_a}, \frac{T_b}{S_b} > 0.$$

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122. The decrease can also be accounted to rent-seeking. Remember cities behave like a rent-seeking individual and each franchise is just like a license where a quantitative restriction exists. See discussion *supra* Part I.A. Where a city's competition decreases because of previous expansion, the price it has to pay proportionally decreases. See discussion *supra* Part I.C.

123. Even if only one city is potentially competitive, rent-seeking is probably not eliminated because several different ownership groups may compete for the franchise even though the region is already determined.

Therefore,

$$P(x,c) > P(x,a), P(x,b).$$

The price paid by city C to the franchise will be greater than the price paid by cities A and B. Rent-seeking dictates that the franchise will then be located in city C, because that is where it will derive the most benefit. However, in 2000, when the second round of franchises are granted, cities A and B will be awarded franchises at a lower cost, because the competition between cities is nominal and the substitutable alternatives are limited. Therefore, franchises Y and Z will not receive the same benefit received by franchise X and will not be able to compete.

The problem then created is that the franchises benefiting from limited rent-seeking may be at a disadvantage vis-à-vis those franchises with less restricted rent-seeking.<sup>124</sup> This, not the tax or municipal participation differences, is why Canadian franchises of American sports corporations cannot compete with their American counterparts. When MLB decided to expand to Canada in 1969 and 1977, those franchises did not receive the full benefit of rent-seeking. This created a continuing deficiency in the profitability of those franchises versus their counterparts in the United States.<sup>125</sup> Therefore, Canadian sports franchises cannot compete because of their restricted ability to rent-seek when first inducted into the corporation.

Though the theory is powerful, superior management decisions overrule differential rent-seeking. Teams often like to use their financial troubles as an excuse for poor performance; sometimes it is nothing more than that—an excuse.<sup>126</sup> This is sup-

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124. Of course this phenomenon is not limited to Canadian franchises. United States franchises are also disadvantaged by differential rent-seeking and overexpansion, the extent of which depends on the factors that contribute to differential rent-seeking. However, the public opinion, refuted by this Note, is that there is something fundamentally different about the Canadian franchises that make them losers.

125. An example of the continuing disadvantage is that several changes aimed at remedying the problem have been proposed including changes to the sports' rules, Canadian law and government support of sports teams yet little assistance has been provided. See Bill Harris, *Canadian Teams Taxed by Taxes: NBA Must Offset Vast Difference in Laws Says Agent*, TORONTO SUN, Feb. 3, 1998, at 67; *Taking One for Our Teams: Ottawa Recommends Federal Aid for Pro Franchises*, TORONTO SUN, October 3, 1998, at S5; *Hockey Committee Wants to Lower Canadian Taxes*, STATE JOURNAL-REGISTER, December 4, 1998, at 40; See also *Canada To Aid Ailing Franchises*, STAR TRIBUNE, January 19, 2000, at C3 ("The Canadian government announced Tuesday that it is prepared to provide up to \$2 million to each of the country's six NHL franchises each year. . .").

126. See Al Strachan, *Strachan on Hockey*, TORONTO SUN, December 27, 1998, at SP9.

ported by empirical data interpreted by a complex function of team efficiencies.<sup>127</sup> Under this formula, teams are assessed to be from well-managed to poorly-managed.<sup>128</sup> A well-managed team may be able to overcome the effects of adverse differential rent-seeking, while a poorly-managed team may lose despite favorable differential rent-seeking.

The differential rent-seeking theory explains the root of the problem better than earlier theories' because it offers a response to the other explanations' inherent question: "Why doesn't the city that wants the franchise give benefits to make up for the disadvantage?"<sup>129</sup> This can not be answered by the prior explanations, but is answered by differential rent-seeking. Differential rent-seeking states that the laws of economics, more powerful than man-made laws, drove the price for the franchises so low that neither municipalities nor the corporations were compelled to accommodate the new franchises, leaving them at a competitive disadvantage.

### CONCLUSION

The ebb and flow of economic feasibility for professional sports franchises is responsible for the Canadian franchises' competitiveness problems. Rent-seeking behavior has created a discrepancy between Canadian sports franchises and some of their United States counterparts because the expansion into Canada limited the benefits granted to the Canadian franchises in respect to those United States counterparts. This differential rent-seeking has created an ongoing disadvantage because the benefit margin granted to the Canadian franchises is smaller than that granted to some franchises in the United States. Without significant change, the Canadian franchises will always be at a competitive disadvantage that can be temporarily overcome only by superior management decisions.

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127. In  $WP_i = \beta_0 + \beta_1 \ln SLG_i + \beta_2 \ln BA_i + \beta_3 \ln SB_i + \beta_4 \ln FP_i + \beta_5 \ln ERA_i + \epsilon_i$ . The equation takes into account each team's winning percentage (WP), batting average (BA), slugging percentage (SLG), stolen bases (SB), fielding percentage (FP) and earned run average (ERA) from the 1982-1993 seasons. See *BASEBALL ECONOMICS* 194 (John Fizel et al. eds., 1996).

128. See *id.* at 197-98.

129. Differential rent-seeking provoked by overexpansion is a subtle but powerful disadvantage that is not apparent when a municipality is awarded a franchise. Because it is almost unnoticeable, it is rarely compensated for. In contrast, the socio-political answers would be obvious, and probably compensated for up front.



